

## Joint Public Procurement and Innovation Lessons Across Borders

*Innovation in public procurement* is essential for sustainable and inclusive growth in an increasingly globalized economy. To achieve that potential, both the promises and the perils of innovation must be investigated, including the risks and opportunities of joint procurement across borders in the European Union and the United States.

This in-depth research investigates innovation in public procurement from three different perspectives. First, leading academics and practitioners assess the *purchase of innovation*, with a particular focus on urban public contracting in smart cities involving meta-infrastructures, public-private partnership arrangements and smart contracts. A second line of inquiry looks for ways to *encourage innovative suppliers*. Here, the collected authors draw on emerging lessons from the US and Europe, to explore both the costs and the benefits of spurring innovation through procurement.

A third perspective looks to various *innovations in the procurement process* itself, with a focus on the effects of joint and cross-border procurement in the EU and US landscapes. The chapters review new technologies and platforms, the increasingly automated means of selecting suppliers, and the related efficiencies that “big data” can bring to public procurement.

Expanding on research in the editors’ prior volume, *Integrity and Efficiency in Sustainable Public Contracts: Balancing Corruption Concerns in Public Procurement Internationally* (Bruylant 2014), this volume builds on a series of academic conferences and exchanges to address these issues from sophisticated academic, institutional and practical perspectives, and to point the way to future research on the contractual models that are emerging from new procurement technologies.

Directed by G.M. Racca and C. R. Yukins, this book contains the texts of: A. Asatryan, J.-B. Auby, M. Borodina, R. Cavallo Perin, L. Diesing, G.M. Di Giuda, D. Dragos, G.F. Ferrari, L. Folliot-Lalliot, J.M. Gimeno Feliu, M. Ismail, J. Kaufman, C. Kronke, I. Locatelli, P. Magina, P.T. McKeen, A. Miño Lopez, J. Molino, M. Pignatti, S. Ponzio, G.M. Racca, B. Racolța, A. Romeo, C. Santerre-Funderburg, D. Schoeni, M.A. Simovart, P. Valcarcel Fernandez, Ch. R. Yukins

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Joint Public Procurement and Innovation



Gabriella M. RACCA  
Christopher R. YUKINS

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Edited by  
Gabriella M. RACCA and Christopher R. YUKINS

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**Joint Public Procurement  
and Innovation**

**Lessons Across Borders**

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## FOREWORD

Edited by Gabriella M. Racca and Christopher R. Yukins, *Joint Public Procurement and Innovation: Lessons Across Borders* brings in contributions by internationally recognized experts. It is therefore with great pleasure that we have included this book in the “Droit Administratif / Administrative Law” Series.

The book is based on joint efforts made by the Public Contracts in Legal Globalization (PCLG) international research network, whose members have carried out collective research on a number of topics linked to public contracts since 2007.<sup>(1)</sup> Driven by the Sciences Po Governance and Public Law Centre (Chaire Mutations de l’Action Publique et du Droit Public), the PCLG Network comprises European and non-European researchers and practitioners as well. The PCLG Network publication *Comparative Law on Public Contracts* (2010) has shown that public procurement law offers suitable topics for comparative research also on account of its cross-border implications.

This book comes after many other volumes of the “Droit Administratif / Administrative Law” Series. The most recent one, *Contrôles et contentieux des contrats publics – Oversight and Challenges of Public Contracts* edited by L. Folliot-Lalliot and S. Torricelli (2018), has shown the strategic importance of European Union Law in the evolution of public contracts law. The previous work, *Integrity and Efficiency in Sustainable Public Contracts: Balancing Corruption Concerns in Public Procurement Internationally* edited by G.M. Racca and C.R. Yukins (2014), has shown how corruption, collusion, favoritism, and conflict of interest undermine the efficiency of public spending. It has also shed light on how corruption implies violations of fundamental rights, and undermines the fiduciary relationship between citizens and public institutions. In that view, transparency and accountability could be regarded as prisms for evaluating the suitability of public contracts – an analysis that led to identifying the need for a strategic reorganization of the public contracts sector.

Building on the aforementioned publications, the aim of this book is to focus on procurement innovation in organizations, cross-border procurement, and award procedures while examining the subject matter of the contract and the procurement process also with a view to suggest ways of encouraging the participation of innovative suppliers.

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(1) The Network site address is [www.public-contracts.org/](http://www.public-contracts.org/).

All this developed from discussions carried out during the workshop “Public Contracts and Innovations – Contrats Publics et Innovation” led by Gabriella M. Racca, Professor at the University of Turin, and Christopher R. Yukins, Professor at the George Washington University (Government Procurement Programme), which was held at the International Training Centre of The International Labour Organisation (ILO) in Turin on 27 May 2016. The Turin workshop, in fact, focused on the demand-side driven innovation for sustainability, efficiency, and integrity in public contracts as well as techniques and instruments for electronic and aggregated procurement (joint procurement and centralized purchasing bodies, framework agreements, eProcurement). Also discussed were innovation partnerships, risks of collusion, public contracts and smart cities.

During the PCLG Network meeting held in Paris on 16 December 2016 (“Public Contracts and Innovation – Contrats publics et innovation”), further discussion involving the participation of the Procurement Unit of the Public Governance and Territorial Development Office of the Organization for Economic Co-operation and Development (OECD) brought about updates on ongoing research on innovation in the evaluation of procurement systems, and also on the relationship between smart cities and procurement.

The latest updates on the subjects of interest were discussed during the PCLG Network meetings held in Paris on 15 December 2017 and 14 December 2018.

Indeed, the Turin workshop and Paris meetings provided the fundamentals for this edited collection by offering insights into a wide range of means that can foster innovation in the public contracts cycle, and outlining future prospects.

The work of our academic consortium has emphasized progress in four different areas as far as public procurement is concerned. Firstly, the digital transformation of public procurement since traditional processes have given way to what we now call “e-procurement”. Secondly, innovation has emerged as a key theme in public contract law and administrative law as well in that both have to adapt to change despite the fact that assimilating innovation in public procurement has often proved to be challenging – as discussed thoroughly in this volume. Thirdly, smart cities (cities built and designed around electronic data) have become a key issue, partly because reshaping public purchasing is necessary to meet the smart cities’ special needs of innovative and integrated procurement. Finally, owing to rapid advances in transnational procurement (and law), it has become clear that existing administrative structures, including procurement rules, need to be revisited and reformed. Our consortium’s work has spanned all these areas, and set the stage for this volume on innovation in procurement in many ways.

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This book examines innovation from three different perspectives. Firstly, innovation in the subject matter of contracts, considering smart cities and strategies for buying innovative solutions. Secondly, innovation in award procedures envisaging the efficient use of award criteria with the aim to encourage innovative suppliers in the procurement process. And lastly, innovation in procurement processes envisaging the strategic use of organizational models and contractual tools (such as central purchasing bodies, cross-border procurements, electronic means and framework agreements).

It should be noted that the differences between the U.S. and EU procurement systems have been taken into consideration by the editors of this book, whose comparative approach has offered views from academic, institutional, and practical standpoints. Their work, supported by different worldwide networks, has created a sound basis for further and more thorough developments in the fields under examination.

The authors of the chapters of this book are all specialists in their own disciplines, respectively. Their diversity in terms of cultural and professional backgrounds is a valuable resource that has provided fertile ground for the scholarly research presented in this book.

In continuity with the previous books, we hope that this research will foster further transnational academic cooperation, and encourage innovation in public contracts for the benefit of public institutions and their citizens.

Torino, Italy 20 May 2019

Jean-Bernard AUBY

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A great opportunity for a better understanding of the book's issues was the involvement in the EU Projects Happi, PPI2Innovate and, more recently, CirePro and Euriphi, with the fruitful discussions with all the partners.

The Editors owe gratitude to the University of Turin for supporting the research activities at the heart of the scholarly work presented in this book.

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Amongst his main publications are *Tortious liability of Statutory Bodies. A Comparative and Economic Analysis of Five English Cases*, co-authored with B.S. Markesinis, D. Coester-Waltjen and S.F. Deakin (Oxford, Hart Publishing, 1999); *The Public Law | Private Law Divide; Une entente assez cordiale?*, co-edited by Mark Freedland (Hart Publishing, 2006); *Droit de l’urbanisme et la construction*, 10th edition, (Montchrestien, 2015); *Droit des collectivités locales*, 5th edition, (PUF, 2015); *Droit de la fonction publique*, 5th edition, (Dalloz, 2009); *Droit administratif des biens*, 6th edition, (Dalloz, 2016); *La globalisation, le droit et l’État*, 2nd edition, (Montchrestien, 2010) (Spanish translation, 2013; English translation, *Globalization, Law and the State*, Hart Publishing, 2017); Chinese translation, *La décentralisation et le droit*, LGDJ, 2006; and *Droit de la Ville. Du fonctionnement juridique des villes au droit à la Ville*, 2nd edition, (Lexis Nexis, 2016).

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using the electronic procurement environment in all the procurements to be conducted by the contracting authority. Over the years, Marina has had the chance to evaluate comprehensively all the advantages and disadvantages of the electronic tendering process – the topic explored in the article.

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**Giuseppe Martino DI GIUDA** is Associate Professor of Building Production at the Politecnico of Milano. He specialises in the implementation of Building Information Modeling (BIM) for Public Administrations as an element of analysis and strategic definition of public investments. His research also focuses on the digitization of tenders through the Most Economically

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**Lena DIESING** has been a policy analyst for public procurement at the Organization for Economic Cooperation and Development (OECD) Directorate for Public Governance since 2016. She works on the development of the Methodology for Assessing Procurement Systems (since 2015) while conducting public procurement reviews in OECD countries. Throughout her career, Lena has shown her commitment in promoting value for money. Her most recent engagements include working with the OECD's Development Assistance Committee on the nexus of development and corruption, money laundering, and organised crime. She also worked in the financial industry by conducting due diligence reviews for a risk management firm.

Lena holds a Master of Arts in International Economics and International Relations from the Johns Hopkins School of Advanced International Studies (SAIS). She studied in Washington DC (US), Bologna (Italy), and Bonn (Germany).

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His research publications include two edited books, seven chapters in international books, four single-author books in Romanian and four co-authored volumes adding to over thirty papers in scientific journals. His recent publications include Dragos and Caranta (ed.), *EU Public Procurement – Outside The*

*Directives, Inside The Treaty?* (Copenhagen, Djøf, 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), *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*, Brussels, Bruylant, 2013; Dragos, Neamtu and Veliscu, 'Judicial Review in Romania between Tradition and Dialogue', in Caranta and Gerbrandy (eds), *Traditions and Change in European Administrative Law*, Groeningen/Utrecht, Europa Law Publishing, 2011; Dragos, Neamtu, Veliscu, 'Remedies in Public Procurement in Romania', in Treumer and Lichere (eds), *Enforcement of EU Public Procurement Rules*, Copenhagen, Djøf, 2011; Dragos, Gellen, Kovac and Langbroek (eds) 'The NISPAcee', in *Journal of Public Administration and Policy*, Vol. IV, No. 2, 2011/2012, Special Issue: Law and Public Management Revisited.

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Dr. Ismail has been awarded by the Arab Republic of Egypt the 2011 State Prize Laureate in Academic Legal Research, the highest academic recognition in the MENA region since 1958. Currently, his research work includes projects undertaken as a Member of the Public Contract in Legal Globalization research network at the Sciences Po University in Paris.

In academia he has fulfilled teaching positions internationally. He is Visiting Professor and PhD examiner at the British universities, and Guest Speaker at the University of London. He has been a Visiting Professor at the Cairo University in Egypt, Lecturer at the Cairo Regional Centre of the International Commercial Arbitration (CRCICA), and Lecturer at the Arab League and BCDR-AAA in the Kingdom of Bahrain since 2000, where he has taught International State Contracts and Arbitration focusing more particularly on infrastructure projects.

Dr Ismail is an internationally renowned specialist on State contracts, public procurement, international arbitration in State contracts and public private partnerships as far as the legal systems of the MENA countries are concerned. He distinguished himself as one of the few scholars to have published extensively in English and in Arabic in the UK, Germany, the MENA region, and other countries as well.

**Justin B. KAUFMAN** serves as an Assistant Commissioner for the State of Minnesota's Information Technology Services agency. In his role, Justin works to leverage business operations teams, including information technology procurement, to build value for the State of Minnesota and support the delivery of efficient and effective information technology solutions. Prior to his current position, Justin worked within the State of Minnesota's Office of State Procurement for eleven years, where he served as counsel, focused on public contract negotiations, established a procurement negotiation training program, ensured fair and open competition in the procurement process, worked extensively with cooperative purchasing contracts and programs, and oversaw statutory compliance for executive branch contracts.

Since 2008, Justin has served as an Adjunct Professor at William Mitchell College of Law (now Mitchell Hamline School of Law), teaching a variety of courses, including Business Practicum, Deals and Dispute Resolution, and Transactions and Settlements. Since 2014, Justin has been an annual guest lecturer for the Government Procurement Law Program at George Washington University. He is actively involved in the National Association of State Procurement Officials, where he serves on the advisory board for the association's annual Law Institute.

Justin holds a Juris Doctor degree from William Mitchell College of Law and a Bachelor of Arts in International Affairs and Political Science from Marquette University.

Akad. Rat a. Z. Dr. **Christoph KRÖNKE** is a postdoc fellow ('Habilitation') at the Institute of Public Policy and Law of the Ludwig Maximilian University in Munich, Germany. He received his Doctor Juris degree from Munich University in 2013. Dr Krönke has published several books and articles in the field of public law, including his dissertation on "The Procedural Autonomy of the Member States of the European Union" (2012) and two text books on the law of State organization (1st ed. 2012, 2nd ed. 2015) and on fundamental constitutional rights (1st ed. 2012, 2nd ed. 2015, 3rd ed. 2018). Besides public procurement law, his research focuses on constitutional law, European and international law, administrative law – with a focus on public commercial law – as well as legal and administrative theory. Dr Krönke graduated from Munich University in 2009 (First State Examination) and passed his Second

State Examination in 2014, after practical legal training in civil, criminal and administrative law courts in Munich and in the cabinet of the President of the Court of Justice of the European Union.

**Ivo LOCATELLI.** After graduating from the University of Rome, in 1989 he started his professional career as an economic researcher supporting the preparation of Structural Funds for the Italian regions. He then completed a traineeship at the research department of Confindustria, the Italian business trade association.

Since joining the European Commission in 1992, Ivo Locatelli has worked in different departments of that institution, initially fulfilling a position at the Directorate-General XIII (Telecommunications) which required focusing on economic issues and studying other aspects as well. He then worked as a Japan expert within the unit in charge of industrial cooperation, thereby managing an important programme of industrial cooperation between European and Japanese ICT industries.

At the Information Society and Media Directorate-General he began working as member of a team in charge of implementing the liberalisation of the telecommunications sector in the EU. Thereafter he was involved in the negotiation process for the adoption of the EU Directives regulating electronic communications, which would be adopted by the EU legislator in 2009. He also worked in the international relations unit as a member of the Euromed Group of Telecommunications Regulators, and then in the eHealth unit.

In 2012 he joined the Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (DG GROW), within the unit in charge of innovative and e-procurement. By leading the e-procurement and cooperative procurement teams, he contributed to shaping policies and strategies in those areas of work. As cooperative procurement team leader, he designed and was responsible for the training course on the SME-friendly policies in central purchasing bodies. He was also responsible for the feasibility study on the implementation of joint cross-border procurement procedures in the EU.

Since Summer 2018 he has been working in the Dir A – European Semester and Member States Competitiveness, thereby focusing on public procurement issues as well. Back to public procurement directorate, Ivo now deals with procurement of innovation and cooperative procurement, leading the corresponding team. He is Senior Expert.

**Antonio MIÑO LÓPEZ** is Lawyer of the Xunta of Galicia (Regional Administration of Galicia, Spain) and contract Lecturer at the University of Vigo (Spain).

As a lawyer representing a public litigant, he fulfilled the role of barrister before the Spanish courts from 2002 to 2004. During that period, he gained

extensive experience in litigation on administrative, civil, and labour issues. With regard to public litigation in particular, he defended the Xunta of Galicia against claimants in any proceeding issued on the activities run by that Regional Administration, including the provision and management of public goods, liability of regional public goods, compulsory expropriation, public procurement, proceedings for civil matters filed by civil servants, and other administrative procedure issues. As far as civil litigation is concerned, the cases he managed range from controversies on regional real estates to issues in connection with minor children under public guardianship. At labour court, he served as defendant of the Galician Administration in hearings for cases filed by their own staff as claimants.

Since 2004 he has been working as Lawyer of the Xunta of Galicia, thereby advising two Departments, Social Affairs and Public Works, while gaining other experience as detailed below.

In 2006 he was temporarily transferred to the headquarters of regional lawyers, where he worked until 2009 as advisor on European law matters such as competition, State aid and European projects. In his role, he took part in two proceedings before the Court of Justice of the European Union (CJEU), ruling on coastal shipping and freedom of services in one case, and in the other on the rights of temporary public staff. From May 2006 to March 2007, the Xunta of Galicia supported him in his study-and-work year in Brussels, where he obtained a Master's degree in European Projects Consultancy from the Université Libre de Bruxelles while working as a *staggere* at the European Commission, Directorate General for Competition, regional aids unit (mainly granting aids to enterprises upon prior evaluation).

During the 2009-2011 term he worked as advisor for the Rural Affairs Department.

From May 2011 to November 2015 he was Head of Investigation of the Galician Council of Competition. In his role, he investigated potential malpractice and filed claims against firms breaching the Spanish Competition Law for collusive practices, abuse of dominant position, unfair competition, and other infringements.

Since May 2015 he has been serving as an advisor to the Rural Affairs Department of the Xunta of Galicia.

Furthermore, since 2010, he has fulfilled a contract lecturer position at the University of Vigo, thereby teaching Public Procurement, Administrative Law, Public Ethics, and Electronic Government and Administration.

He has written several articles and book chapters on public procurement and competition law, and the connections between both areas. Currently, he is concluding his doctoral research on antitrust behaviours in public procurement.

**Paulo MAGINA** has headed the Public Procurement Unit at the OECD Public Governance Directorate since March 2014.

On the strength of his ten-year experience in the public sector, he recently served as Board Member and CFO of the Portuguese Central Government Shared Services Agency managing finance, accounting, HR, IT, and public procurement for the public administration. From 2010 to 2010 he was President and CEO of the Portuguese National Public Procurement Agency, where he led the set-up of the central purchasing body and the e-procurement implementation. He also worked with the EBRD and UNCITRAL to advise policy and legal reforms, develop action plans and road maps for restructuring public procurement systems in the CIS region in the 2012-2014 period.

Former deputy member of the Cabinet of the Secretary of State for transport in Portugal, he has held managerial positions as Member of the Board of Directors and CFO of the Portuguese national railway company CP. Earlier on, for more than twelve years, he worked as Investment Director in the transportation, banking, and private equity sectors. During those years he was responsible for assessing several PPPs and infrastructure projects, and also led the financial team in the design and setting up of light-rail projects and motorways in Portugal.

Paulo Magina holds a Master's degree in Business Administration and Management from the Catolica Lisbon School of Business & Economics. He has been an invited lecturer in that university, where he has taught Financial Strategy, Private Equity, and Venture Capital in postgraduate and MBA programs. He has also given lectures and led courses on PPPs and, more recently, on aspects of Public Procurement.

**Peter T. MCKEEN's** procurement career spans twenty-five years, during which he has been teaching courses in public procurement while working in contract administration and as a procurement law analyst for national law firms specializing in government contracts law. He currently works as an analyst with the government contracts practice at Arnold & Porter in Washington, D.C. Mr. McKeen has served on the adjunct faculty at the University of Virginia since 2002. He teaches courses to the U.S. public procurement workforce in procurement law and contracts management in the University's School of Continuing and Professional Studies. He is active with academic groups and international organizations involved in the study and reform of national procurement systems. He has also conducted training and instruction for procurement officials in countries seeking to enhance their national procurement systems.

McKeen earned a B.A. from the University of Southern Maine and an M.A. from the George Washington University.

Among his numerous publications, mention should be made of ‘United States – Discretion, Oversight and the Culture of Compliance’ in L. Folliot Lalliot, S. Torricelli (eds), *Oversight and Challenges of public contracts* (Bruylant 2017); Michael E. Giboney and Peter T. McKeen, *Federal Services Contracting for the Contracts Professional* (SMG 2016); Michael E. Giboney and Peter T. McKeen, *Federal Procurement Law for the Contracts Professional* (SMG 2014); ‘The Importance Of A Professionally Educated Public Procurement Workforce: Lessons Learned From The U.S. Experience’, in G. M. Racca and C. R. Yukins (eds) *Integrity And Efficiency In Sustainable Public Contracts* (Brussels, Bruylant, 2014); and Michael E. Giboney and Peter T. McKeen, *Capstone Course Topics In Federal Procurement* (SMG 2011).

**Jellie MOLINO** is finishing her PhD research on *The Role of Multilateral Development Banks in Promoting Sustainable Public Procurement for Innovation Toward Smart Cities* at the University of Turin (Italy). She holds an LL.M in Government Procurement and Environmental Law from The George Washington University Law School (2016), an Executive Master’s Degree in Business Administration (EMBA) from the Asian Institute of Management (2014), a Doctor of Jurisprudence degree from the University of Batangas (2005), and BA degree in Philosophy from the University of the Philippines-Diliman (October 1998). Her research interests focus on the improvement of regulations and practices on government procurement, sustainability, and anti-corruption mechanisms in developing countries.

She has been a member of the Philippine Bar since 2007 and has been active in litigation on environmental and administrative cases, including corporate compliance. She has well-rounded experience in public procurement. She was a former member of the Bids and Awards Committee (BAC) of Batangas State University (BatStateU) (2006-2010), Chair of the BAC in Pangasinan State University (PSU), and Head of the Technical Working Group of BAC in PSU (2015). She also has experience in international procurement. She was a legal and procurement specialist in the Office of General Counsel at the Asian Development Bank (2015), a visiting professor for sustainable public procurement, private-public partnership and corporate social responsibility at the International Training Center of the International Labor Organization in Turin, Italy (August, 2018, 2019), and a consultant for the Supreme Court of the Republic of the Philippines on procurement related issues in the Official Development Assistance (ODA) funded projects in the Philippines (January – February, 2019).

Prior to pursuing her graduate studies, she had positions of responsibility in the academy in the Philippines. She joined the faculty of Batangas State University as College Instructor in 1999. She was promoted to Assistant

Professor IV in 2006, and, started teaching law subjects. In 2007, she was appointed to the position of Board and University Secretary V, and, in 2010, she became the first Vice President for Resource Generation and External Affairs. She also served as Vice President for Administration and Finance in PSU in 2015. She left those positions to pursue her international graduate studies.

**Matteo PIGNATTI** is Post-doctoral researcher at the Department of Management of the University of Turin (Italy). He obtained his PhD in Administrative Law at the University of Turin (2012) with a dissertation on the contractual activity of central purchasing bodies. Having successfully passed the bar examination (2011) at the Court of Appeal of Turin, he has become a legal practitioner. He is an assistant professor teaching Public Law, Administrative Law, and Public Contract Law. His research interests include public contracts, organizational models for Central Purchasing Bodies (CPBs), contractual tools such as framework agreements and dynamic purchasing systems for demand aggregation by public purchasers, eProcurement, transparency and integrity issues.

He took part in the Italian Research Unit working at a EU project on Public Procurement for Innovation (PPI), Healthy Ageing and Public Procurement of Innovations, funded by the EU Commission (DG Enterprises – Call ENT/CIP/11/C/N02C011). He currently takes part in the Italian Unit of the project on Public Procurement for Innovation Capacity Building to Boost the Usage of Public Procurement of Innovation (PPI) in Central Europe – PPI2INNOVATE funded by the Central Europe Programme of the European Regional Development Fund (Interreg) for the 2016-2019 period (*see* [www.interreg-central.eu/Content.Node/PPI2Innovate.html](http://www.interreg-central.eu/Content.Node/PPI2Innovate.html)). The project directly targets public procurers at all administrative levels in the EU with a view to building regional capacities in PPI. He is also involved in the Interreg Europe project Smart Circular Procurement (CircPro) and in the project Financing Impact on the Regional Development of Cultural Heritage Valorisation (FINCH) – Interreg Europe. A member of the Public Contracts in Legal Globalization comparative law network (*see* [www.contrats-publics.net](http://www.contrats-publics.net)), he has published several articles in the field of public contracts.

**Silvia PONZIO** is Associate Professor of Administrative Law at the Department of Management of the University of Turin. She teaches Administrative Law, Public law for Economics, Labour Law and Public Contracts Law in graduate and postgraduate courses. She is responsible for the teaching activities of the SEIIC Master's degree course on Italian public contracts, which has been organised with the National Authorities on Anticorruption (ANAC).

Her research interests include public contracts and public procurement, collaborative procurement and central purchasing bodies, public procurement

of innovation (PPI), and the liability of public administrations in connection with general and special contracts as well as technical specifications and documents defining the rules for awarding procedures. Also, in the scope of her study is evaluating transparency in the activities performed by public bodies and civil servants, as well as their accountability not only in the light of ethical issues and disciplinary measures to be undertaken. She has shared her research outcomes through publishing books, essays, and articles.

She has been involved in the Italian Unit of the EU project on Public Procurement for Innovation (PPI), Healthy Ageing and Public Procurement of Innovations, funded by the EU Commission (DG Enterprises – Call ENT/CIP/11/C/N02C011). The HAPPI Project, underpinning the first joint cross-border procurement with an FA anticipating art. 39 of the Dir. 24/14/EU, was referenced in the *Feasibility Study Concerning the Actual Implementation of a Joint Cross-border Procurement Procedure by Public Buyers from Different Member States* prepared for the EU Commission by the BBG, Ski and EU Commission, *Making Public Procurement Work in and for Europe*, 3.10.2017, COM (2017) 572 final. She is currently involved in the Italian Unit of the project on Public Procurement for Innovation Capacity Building to Boost the Usage of Public Procurement of Innovation (PPI) in Central Europe – PPI2INNOVATE, funded by the Interreg Central Europe Programme (European Regional Development Fund for the period 2016-2019 (see <http://www.interreg-central.eu/Content.Node/PPI2Innovate.html>)). The project directly targets public procurers at all administrative levels in Central Europe with a view to building regional capacities in PPI, changing attitudes towards PPI, strengthening linkages among relevant stakeholders in regional innovation systems, thus boosting use of PPI in Central Europe. Moreover, she is involved in the Smart Circular Procurement Project (CircPro) – Interreg EUROPE, and the project Financing Impact on the Regional Development of Cultural Heritage Valorisation (FINCH) – Interreg Europe.

She is a member of the editorial board of the *Diritto amministrativo* journal, and also of the Italian editorial board of the *Ius Publicum Network Review*. Furthermore, she is a member of the Public Contracts in Legal Globalization research network ([www.contrats-publics.net](http://www.contrats-publics.net)) and the Procurement Law Academic Network ([www.planpublicprocurement.org/main/](http://www.planpublicprocurement.org/main/)).

**Gabriella M. RACCA** is Professor of Administrative Law at the Department of Management of the University of Turin (Italy) and coordinator of the PhD in Law and Institutions at the University of Turin. She has been Deputy Dean of the School of Economics (2005-2012). She is the Director of the Master SEIIC, on Efficiency, Integrity and Innovation in Italian Public contracts, organized with the National Authority on Anticorruption (ANAC).

She is the coordinator of the *Ius Publicum Network Review* and Italian Head of the 'Public Contracts' section. Founded in Madrid, on 26 April 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 this network is to follow the developments in Administrative and Public Law in each network member's country and their relevance to other legal cultures ([www.ius-publicum.com](http://www.ius-publicum.com)).

Her main research interest is the public procurement cycle, from the definition of needs to the execution of the contract. She has also steered her studies toward public services, concessions, PPP, public liability, compensation for damages, the accountability of public administrations, and integrity issues. More recently, she has broadened her research field by focusing on collaborative procurement and central purchasing bodies, GPOs, framework agreements (especially in the European Healthcare Systems), sustainability (environmental and/or social) and public procurement of innovation.

She has been a consultant to the Organisation for Economic Co-operation and Development (OECD) on public procurement in the healthcare sector. She also is Member of the Steering Committee of the Public Contracts in Legal Globalization research network (*see* [www.contrats-publics.net](http://www.contrats-publics.net)). With Christopher R. Yukins, Professor at the George Washington University School of Law, she has co-directed the research project *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* which led to the publication of the previous book in this series (2014) in *Droit administratif/Administrative Law* collection. She is co-director of the research project *Joint Public Procurement and Innovation: Lessons Across Borders*, since 2016, aimed at highlighting the key role of innovation in Public Procurement.

Prof. Racca led the Italian Unit of the EU project on Public Procurement for Innovation (PPI), Healthy Ageing and Public Procurement of Innovations, funded by the EU Commission (DG Enterprises – Call ENT/CIP/11/C/N02C011). The HAPPI project is aimed at conducting a legal study on innovative procurement models for an EU cross-border joint procurement system in Healthcare. It is also aimed at bringing to the fore relevant legal aspects while identifying the most appropriate tools to open the way to collaboration among public entities, or CPBs from different countries, in order to overcome the existing barriers within Europe, thus encouraging competition and the Internal Market opening. From that perspective, data recording, benchmarking, and information exchange among Public Interest Entities in the EU may help achieve the goals set out in the *Europe 2020* strategy. According to that strategy, high quality health care should be provided without increasing

the expenditure budget. The HAPPI project led to establishing one of the first joint cross-border procurement, with a FA anticipating art. 39 of the Dir. 24/14/EU. The project was referenced in the *Feasibility Study Concerning the Actual Implementation of a Joint Cross-border Procurement Procedure by Public Buyers from Different Member States* prepared for the EU Commission by the BBG, Ski and EU Commission, *Making Public Procurement Work in and for Europe*, 3.10.2017, COM (2017) 572 final “in the HAPPI project, innovative solutions for healthy ageing have been procured jointly by contracting authorities in several Member States”, recalling that “more than 20 health-care organisations from France, Italy, Luxembourg, Belgium or Netherlands purchased HAPPI solutions”.

She has recently been appointed a member of the Advisory Committee to the EURIPHI (“European Innovative Procurement of Health Innovation”) project, funded by the EU’s Horizon 2020 research and innovation programme. The project aims to establish an effective and sustainable cross-border Community of Practice to share experiences and support development of cross-border public procurement and value-based approach.

Combining her commitment to education and scholarly expertise, she has led the Job Placement High Education Project named “Educational Path in Collaborative Public Procurement”, funded by the Regional Government of Piedmont (European Social Fund).

Currently, she is Head of the Italian Unit working at the project Public Procurement for Innovation Capacity Building to Boost the Usage of Public Procurement of Innovation (PPI) in Central Europe – PPI2INNOVATE, funded by Interreg Central Europe Programme (European Regional Development Fund) for the 2016-2019 period (see [www.interreg-central.eu/Content.Node/PPI2Innovate.html](http://www.interreg-central.eu/Content.Node/PPI2Innovate.html)). The project directly targets public procurers at all administrative levels in Central Europe so as to build regional capacities in PPI, change attitudes towards PPI, strengthen ties among relevant stakeholders in regional innovation systems, thus boost the use of PPI in Central Europe. As its spearhead, the PPI2Innovate project is aimed at delivering three thematic tools (Smart Health, Smart Energy and Smart ICT), fully customised to six national institutional frameworks and translated into the national language of each of them, and at the implementation of regional joint competence centers in PPI.

She is also Scientific Director of the Smart Circular Procurement Project (CircPro) – Interreg Europe (see <https://www.interregeurope.eu/circpro/>). Project CircPro aims to promote the transition to Circular Economy in the procurement sector and to combine efficiency, sustainability and innovation with the principles of Circular Economy in the whole procurement cycle. She

is involved in the project Financing Impact on the Regional Development of Cultural Heritage Valorisation (FINCH) – Interreg Europe (see <https://www.interregeurope.eu/finch/>).

Moreover, she is Member of the Scientific Board of two postgraduate programmes. Firstly, the Master's of Science degree in Public Procurement Management for Sustainable Development, jointly organized by the International Training Centre of International Labour Organisation (ITC – ILO) of the University of Turin. Secondly, the *Master en Gouvernance et management des marchés publics en appui au développement durable*, jointly organised by the International Training Centre of International Labour Organisation (ITC – ILO), the University of Sciences Po Paris, and the University of Turin.

She is currently involved as a teacher in the postgraduate diploma/master in Public Procurement Regulation in the EU and in its Global Context MA/Pg Dip, at the King's College in London.

Aside from the network mentioned earlier, Prof. Racca is Member of the steering committee of different organisations, including the Association of Italian Professors of Administrative Law (AIPDA) (see [www.diritto-amministrativo.org/](http://www.diritto-amministrativo.org/)), and of the Italian section of the International Institute of Administrative sciences (see [www.iias-iisa.org](http://www.iias-iisa.org) and [www.iisa.it/](http://www.iisa.it/)). She is also a member of the Procurement Law Academic Network (<http://www.planpublicprocurement.org/main/>), the Research Network on EU Administrative Law ([www.reneual.eu/](http://www.reneual.eu/)), the European Law Institute ([www.europeanlawinstitute.eu/](http://www.europeanlawinstitute.eu/)), the International Society of Public Law ([icon-society.org/](http://icon-society.org/)), the European Procurement Law Group ([eplgroup.eu/](http://eplgroup.eu/)), the British Institute of International and Comparative Law ([www.biicl.org/](http://www.biicl.org/)), the Italo-Brasilian Administrative Law Professor Network, the Smart Cities and Digital Administration Network the Transnational Administrative Law Network ([www.transadmlaw.eu](http://www.transadmlaw.eu)) and the Future of Administrative Law Network. She has published extensively. Selected writings by her are available from the SSRN web site (see [ssrn.com/author=1571949](http://ssrn.com/author=1571949)).

**Bianca RACOLȚA.** PhD Candidate at the Babes Bolyai University Faculty of Law in Cluj Napoca (Romania) with a thesis on State Aid and Public Procurement, she is a practicing lawyer in the Cluj Napoca Bar.

She graduated in law in 2013 and holds a Master's Degree in International Law. She taught Labour Law at the Babes Bolyai University Faculty of Law in 2013-2014. Still at the Babes Bolyai University, since 2017 she has taught a course on Administrative Law in English at the College of Political, Administrative and Communication Sciences. She has won the 2<sup>nd</sup> Prize in the 2016 FBE International Contract Competition (Commercial Contract Negotiations) held in Warsaw. As a speaker she has attended international conferences as

well, for instance the 2017 and 2018 annual conferences of the European Group of Public Administration held in Milan and Geneva, respectively, as well as the 2017 and 2018 Transylvanian International Conference in Public Administration that took place in Cluj-Napoca. She has published in the *European Procurement and PPP Law Review*, *The Scientific Journal of Humanistic Studies*, and the *Romanian Journal of Legal Notes and Studies*.

**Anna ROMEO** is currently Professor of Administrative Law at the Department of Law of the University of Messina. She obtained her PhD in Public Law at the University of Turin, she was researcher of Administrative Law at the LUSPIO University of Rome and Associate Professor of Administrative Law at the Faculty of Law of the University of Messina. She is Vice-Coordinator of the PhD in Legal Sciences – curriculum *Company, Society and Market Regulation*, and an expert, appointed by the Ministry of Education, for the revision of research projects of national interest, member of the Insurance Commission of the quality of the research at the aforementioned Department of Law in Messina. She holds the courses of Administrative Law, Urban Planning Law and Comparative Administrative Law, and, previously, of Local Government Law, as well as at the School of Specialization for Legal Professions of the University of Messina. She also taught at the School of Public Administration, at Masters and Training Courses and at the School of Specialization for Legal Professions of the “Mediterranea” University of Reggio Calabria. She is author of two monographs and more than 60 publications on the subject of administrative procedure, silence of the public administration, public tenders, expropriation, administrative justice. She has been speaker at numerous national and international conferences and she was Visiting Fellow at the Chengdu Administration Institute in Chengdu-China. She is a member of the Italian Association of Professors of Administrative Law (AIPDA), of the Italian-Argentine, Italian-Spanish and Italian-Brazilian Associations of Professors of Administrative Law.

**Daniel SCHOENI** has been with the U.S. Air Force JAG Corps since 2004. His past assignments include California, Germany, Washington DC, Massachusetts, and Arizona. He has served as prosecutor, trial and appellate defense counsel, program counsel, and deputy staff judge advocate. He has twice deployed (six months to Colombia, a year to an undisclosed location in Southwest Asia), and is now assigned to Creech AFB, Nevada. He is a graduate of Brigham Young University (B.A. Philosophy 2000), the University of Iowa Graduate College (M.A. Philosophy 2003), the University of Iowa College of Law (J.D. 2003), the University of Nottingham (LL.M. Public Procurement Law and Policy 2011), and the George Washington University (LL.M. Government Procurement Law 2014). Prior to the military, he clerked for the Honorable Jerry Larson of the Iowa Supreme Court. He has published

articles on a variety of procurement subjects, including defense offsets, cybersecurity, suspension and debarment, the World Trade Organisation's Agreement on Government Procurement, public-private partnerships, and defense innovation. His writings have earned several awards, including the American Bar Association's Standing Committee on Armed Forces Law's Keith E. Nelson writing award and the U.S. Air Force JAG School's Thomas P. Keenan award for international and operational law. He is a Ph.D. candidate at the University of Nottingham, and his dissertation considers the subtle non-tariff barriers that would impair transatlantic public procurement trade between the United States and the European Union even if the overt barriers were removed. He is an adjunct at King's College London's school of law, teaching a course on defense procurement in the European Union.

Dr Iur **Mari Ann SIMOVART** is Associate Professor at the School of Law, University of Tartu, Estonia. Her research is focused on EU public procurement law, in particular the public contract performance stage, featuring contract modification and termination, contractual liability, and more broadly the interaction of national contract law with the EU public procurement law. Recently, she has been engaged in projects on the enforcement of remedies in public procurement matters as well as innovation in public procurement. She teaches public procurement law classes on postgraduate courses by classes which have repeatedly been awarded the title of the best class of the School of Law. Furthermore, she has led training courses and seminars on public procurement law.

As a speaker, Dr Simovart has attended several conferences on EU public procurement law, for instance the 'Public Procurement: Global Revolution' conference held in Nottingham (UK) in 2017, the 2016 and 2017 *Upphandlingskonferensen* in Stockholm (Sweden), and others.

Dr Simovart has published numerous articles on EU public procurement law and participated in international book projects. For instance, she co-authored the recently published commentary on the EU public procurement remedies directives in *Brussels Commentary on EU Public Procurement Law* edited by Steinicke/Vesterdorf (C.H. Beck, Hart, and Nomos, 2018). Currently, she leads the project of writing the Commentary on Estonian Public Procurement Act, to be published in 2019. She is a Member of the Council of the procurement law journal *URT*, issued in Stockholm (*see* [www.urt.cc/?q=radet](http://www.urt.cc/?q=radet)); an academic member of the Procurement Law Academic Network (*see* [www.planpublicprocurement.org/main/](http://www.planpublicprocurement.org/main/)), and a Member of the Public Contracts in Legal Globalization research network (*see* [www.contrats-publics.net](http://www.contrats-publics.net)).

**Patricia VALCÁRCEL FERNANDEZ** is Associate Professor of Administrative Law (with the qualification for Full Professor), at the University of Vigo

(Spain). She holds a Ph.D. in Law (Summa Cum Laude and Extraordinary Doctorate Prize). She has been a visiting scholar in different Universities, including the Università degli Studi di Firenze (Italy), the Universidade da Lusíada in Lisbon (Portugal), and the University of Nottingham (UK).

Professor Valcárcel is an author of nearly 100 publications on Administrative Law. She has published extensively on public contracts, and is the author of a monograph on the execution and financing of public works, *Ejecución y financiación de obras públicas. Estudio de la obra pública como institución jurídico-administrativ* (Thomson-Civitas, Madrid, 2006). She has also written articles and book chapters on public-private partnership, the strategic use of public procurement, and innovation in public procurement. She has edited two books, the most recent of which is *Joint Purchasing and Aggregate Demand of Contracting in the Public Sector. A Legal and Financial Analysis* (Aranzadi Thomson Reuters, 2016).

She is a founding member of the Spanish Public Procurement Observatory (OBCEP) in 2011, and a member of different international research networks in this field: Procurement Law Academic Network (PLAN), Public Contracts in Legal Globalization (PCLG) and the European Procurement Law Group (EPLG).

She has participated in different national and international research projects, the most recent of which is a national research project funded by the Spanish Ministry of Economy, Industry and Competitiveness (Spanish Government) on Smart Procurement (Ref: DER2015-67102-C2-2-P).

Professor Valcárcel was a former counsel for the *Garrigues Abogados y Asesores Tributarios*, a position that allowed her to gain extensive experience in the practice of Administrative Law, in the fields of national and international public contracts. Currently, she is a consultant in public procurement for public bodies and private firms.

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**Introduction.**  
**The Promise and Perils of Innovation  
in Cross-Border Procurement**

BY

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This is a time of transition in procurement law, a time for new beginnings, and for rethinking old approaches in an increasingly globalized economy. Recognizing these enormous changes underway in our discipline, this volume seeks to capture some of the best ideas, from some of the leading academic writers and practitioners in our field.

***1. Innovation in Procurement:  
Its Meanings, and How It Is Addressed  
in this Book***

This volume centers on ‘innovation in procurement’, which can mean many things.<sup>(1)</sup>

The first, of course, is the *purchase of innovation*: buying cutting-edge technology in public procurement markets.

A second meaning of ‘innovation in procurement’ is *encouraging innovative suppliers* in the procurement process.

A third meaning is *innovation in the procurement process itself*: new methods and approaches for the procurement process.

The book deals with all of them, and they are often variously mixed, as for example in the cases of the networks of Centralized Purchasing Bodies in the EU (which use innovative procurement measures to spur development), and the use of the Small Business Innovation Research (SBIR) program to advance

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(1) See, e.g., P. SMITH, “Innovation Procurement – What Exactly Does It Mean?”, *Public Spend Forum*, May 2017.

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technological innovation in the United States, a program which Santerre-Funderburg and co-editor Yukins assess in their chapter.

While the EU and the U.S. landscapes for encouraging innovation in procurement are very different, the two systems' emerging issues and concerns are often the same.

Interestingly, the working EU definition for innovation, that is, the “implementation of a new marketing method, or a new organisational method in business practices, workplace organisation or external relations, inter alia, with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth,”<sup>(2)</sup> is echoed in one of the generally accepted procurement goals in the U.S. federal administration, that is, to focus on ‘innovative acquisition methods’, with a view to new ways of doing things that can enhance performance.<sup>(3)</sup> According to the Office of Innovation and Technology in the U.S. city of Philadelphia, a subject of the analysis by Laurence Folliot-Lalliot and Peter McKeen in their chapter on procurement and smart cities, innovation focuses on “[d]eveloping and sustaining innovative technology practices within the City through engaging and empowering citizens, improving business processes, working collaboratively and constantly searching for new opportunities”.<sup>(4)</sup> This book, therefore, tries to add value in the on-going debate on how public procurement across borders ‘innovates’ in what seems to be a common direction, regardless of jurisdiction.

### 1.1. Purchase of innovation

Purchasing new or significantly improved products, services or processes of production, building or construction is the first meaning of innovation in procurement. Several chapters in this book focus on the use of public procurement in obtaining “technologically-advanced and innovative products and services at better prices”, more particularly, the chapters by Jean-Bernard Auby, Laurence Folliot-Lalliot and Peter McKeen, and Giuseppe Franco Ferrari on smart cities.<sup>(5)</sup>

Ferrari highlights the role of ‘smartness in the cities’ in the development of procurement regulations and policies, *i.e.*, from an intelligent city to a future ‘cyber-civic’ city. He emphasizes the importance of enhancing the capacity of

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(2) Art. 2, § 1(22), Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC.

(3) S. KELMAN, “Reinventing government, 25 years on: has the procurement system improved?”, *PPLR*, 2018, 3, p. 101.

(4) See L. FOLLIOT LALLIOT and P.T. MCKEEN, “Procurement and Smart Cities: Exploring Examples on Both Sides of the Atlantic”, Chapter 7 in this book.

(5) See J.-B. AUBY, “Public Contracts and Smart Cities”; L. FOLLIOT LALLIOT and P.T. MCKEEN, “Procurement and Smart Cities: Exploring Examples on Both Sides of the Atlantic”; G.F. FERRARI, “Smartness and the Cities”, Chapters 6, 7, 5 in this book.

a smart city to use artificial intelligence in the performance of its sociological function such as governance, attracting business, and even facilitating democratic processes for the establishment of innovative regulations, not only in government contracting but also in the advancement of the highest social and environmental protections.

Although Jean-Bernard Auby negates the presence of an exclusive definition for the ‘smart cities’ movement, he shares Ferrari’s analysis on the phases of its implementation by asserting the role of a ‘triple set of transformation’ – transformation of infrastructures, the growing importance of digitalization and data, and changes in governance – in the evolution of smart cities. He claims that the transformation of the urban infrastructure (‘meta-infrastructures’), digitization and data (‘smart procurement’), and changes in governance (new public-private partnership arrangements) will likely change urban public contracting in smart cities. He further explains the possible long-term consequences of the transformation in the urban functioning (*i.e.*, becoming ‘smart cities’) in the categories of contracts, that is, urban public contracting in smart cities is leaning toward a multi-party system. More parties will be assembled both on the part of the contracting authorities and a wider range of contractors, complex contracts, *i.e.*, more (functionally) global contracts, and long-term contracts, so that contractors’ responsibility will extend beyond the completion of the infrastructure project to include its overall management in a given period of time.

The chapter by Folliot-Lalliot and McKeen explores some of the innovative procurement techniques that have been adopted in cities that are actively promoting smart development in the US and EU. In particular, they underline the special clauses, concerning data collection, data release policy, data protection, and dissemination in contracts for smart cities, which in the case of the City of Philadelphia, US, have resulted in the promotion of FastFWD, an innovative public procurement concept. Under FastFWD, the City gathers data across departments on a given problem and then will, where, possible, describe that problem in a manner suited to creative solutions (“problem-based procurement methods and practices”). Once the need is identified, a multi-phase process follows, with an initial request for solutions for the identified need. This effort has attracted new companies and small businesses, with innovative ideas.

In the end, the procurement of ‘innovative’ products and services for the development of smart cities is a “key component in the creation and management of smart cities, and effective city governance structures influence its success”.<sup>(6)</sup> The discussion presented in the above-mentioned chapters on

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(6) See, e.g., N. VERGOULIAS, “Smart cities: is cutting-edge technology the method to achieving global sustainable goals?”, in *J. Envtl. L. & Litig.*, 2017, 32, p. 272.

smart cities is an example of how the procurement of innovative products, services and works, e.g., procurement of new technology collaborations for traffic congestion, and crime prevention in local communities in the US, calls for new practices in public procurement such as the development of smart public-private collaboration.(7)

Other equally important approaches are laid down in the EU Directive on Public Procurement. In fact, Recital 47 of the Directive is very clear in encouraging public authorities to use public procurement to spur innovation; it states in part:

“Buying innovative products, works and services plays a key role in improving the efficiency and quality of public services while addressing major societal challenges. It contributes to achieving best value for public money as well as wider economic, environmental and societal benefits in terms of generating new ideas, translating them into innovative products and services and thus promoting sustainable economic growth”.(8)

In addition to the different approaches to innovation, *i.e.*, pre-commercial procurement, the new Directives promote other models such as the use of *public procurement for innovation* (PPI) and *innovation partnerships* in helping Member States to ensure the promotion of “sustainable high-quality public services in Europe.” Through the EU’s public procurement of innovation, a procuring entity can act as the “launch customer or early adopter” for products and services that either are not available on the market, or have yet to reach a significant market share.(9) Some of the successful PPI projects are discussed in the chapter by Cavallo Perin and co-editor Racca. Interestingly, their chapter argues that central purchasing bodies had already experienced challenges in promoting innovative forms of cross-border administrative cooperation, according to European and national principles, even before the implementation of the 2014 Directive. In this regard, among the most advanced and innovative joint procurement experiences, the “Healthy Ageing Public Procurement of Innovations” (HAPPI) project(10) provided one of the first joint cross-border procurements to buy innovative solutions to promote healthy ageing. This experience stands out(11) for having combined product innovation (“what

(7) See L. FOLLIOT-LALLIOT and P. McKEEN, “Procurement and smart cities: exploring examples on both sides of the Atlantic”, Chapter 7 in this book.

(8) Recital no. 47, Dir. 2014/24/EU.

(9) M. BLAY, “The Strategic Use of Public Procurement in Support of Innovation”, *EPPLR*, 2014, 9, pp. 3-11.

(10) BBG and SKI, *Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, 2017, pp. 33 et seq.

(11) As recently recognized by the EU Commission, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, “Making public procurement work in and for Europe”, Strasbourg, COM (2017) 572 final, October 2017.

to buy”) in order to share the risks connected to the purchase of innovative solutions in the field of active ageing with a significant innovation of the procurement process, jointly designed and conducted by Central Purchasing Bodies (CPBs) (partners in the project) of different Member States (‘how to buy’). The choice was to establish a European Purchasing Group which delegated the intermediary functions to the French CPB for the conclusion of a closed framework agreement with one economic operator, in accordance with EU and French law, with a combined effort of harmonization.

From the same perspective, Valcarcel shows how PPI can trigger the promotion of aggregation in public procurement among EU Member States. Citing various examples such as the project on the “Distributed European Community Individual Patient Healthcare Electronic Record” (DECIPHER) and the “Public Administration Procurement Innovation to Reach Ultimate Sustainability” (PAPIRUS), she highlights the role of collaborative and joint cross border procurement for buying innovative solutions. In the DECIPHER project, several EU Member States (*i.e.*, Spain, Italy, United Kingdom and Finland) formed a consortium in conjunction with technology suppliers to define the technological solutions in health sectors which promote the use of mobile applications for ease of access of health data, which is an innovative product that has been developed during pre-commercial public procurement.

The chapter by Racolța and Dragos elaborates on the importance of innovation partnership in promoting research, development and innovation (RDI) in the EU by comparing it with another legal instrument, State aid for RDI. They discuss the relationship between these two instruments, including the opportunities and challenges for the use of each. Depending on the level of policy design, the specifics of legal regimes make the use of public procurement and State aid desirable in promoting RDI in different settings. Unlike State aid RDI, RDI under Article 31 of the EU Directive on innovation partnership allows the contracting authorities and the innovator-participants to agree on the subsequent purchase by the contracting authority of the resulting supplies, services or works that meet the authority’s required performance levels within a maximum cost. In essence, the prospect of future procurement helps fuel research and development.

The procurement of innovative products is not a practice peculiar only to the European Union. It has become a common strategy among procuring entities across the globe. In the United States, for example, the promotion of innovative products is tied to a policy favoring advancement of small enterprises through the federal government’s Small Business Innovation Research (SBIR) initiative. The chapter of Santerre-Funderburg and co-editor Yukins discusses how the U.S. SBIR program fosters innovation among small businesses by

funding concepts at their earliest stages and then granting a procurement preference as those concepts are commercialized. Notably, the U.S. SBIR strategy is in many ways the forerunner to the European initiative on “innovation partnerships”; Christophe Kronke’s piece discusses the goals and contours of that initiative in the European Union while Ponzio’s chapter highlights the criticalities among PCP and PPI as addressed in the innovation partnership model, possibly taking advantage of knowing in advance the criticalities of the U.S. experience in SBIR.

Asian countries have also encouraged the procurement of innovative products through the promotion of the use of high-level technology (HLT). The Asian Development Bank (ADB) has already launched the “High-Level Technology Fund” with an objective of assisting ADB’s developing member countries to adopt high-level technology and innovative solutions through the acquisition of equipment and goods that employ HLT, construction or civil works based on specifications that require contractors to meet enhanced performance standards and/or employ HLT in the construction process, materials and other inputs; and the hiring of consultants with specific knowledge and expertise in the use of HLT.<sup>(12)</sup> As of December 2018, the ADB High Technology Fund had financed thirteen (13) projects for the acquisition of HLT projects such as implementing innovative approaches for water governance in Mongolia which promotes the acquisition of HLT technology on groundwater quality and quantity monitoring systems. Molino’s chapter summarizes the other innovations in public procurement that the ADB is currently promoting in its Member States.

Irrespective of approach, a successful purchase for innovation requires an intensive market consultation, an argument posited by Lopez in his paper, “Preliminary Market Consultation in Innovation Procurement: a principled approach and incentives for anticompetitive behaviours” and supported by Gimeno Feliu in his extensive analysis of the EU’s procurement reform as a strategy for the development of innovation policy; more particularly, his arguments on leveraging the purchasing power by the EU public procurers in acquiring innovative products and services in order to improve the efficiency and quality of public services with a view to promoting the Europe 2020 plan for smart, sustainable and inclusive growth.

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(12) Asian Development Bank, “High-Level Technology Guidance Note on Procurement”, June 2018.

## 1.2. Innovation in Procurement

A second meaning of ‘innovation in procurement’ is *encouraging innovative suppliers* in the procurement process<sup>(13)</sup> – to encourage those that will provide innovative solutions, rather than simply low price. This tension between low price and best value divides modern procurement, for while most systems presumptively favor awards based on low price, as they are simpler and pose less corruption risk, more advanced procurement systems typically strive towards more subjective best-value awards and broader value-based approaches which embrace innovation and yet also entail further risks and require special evaluating capacities.

What is interesting about this approach is that while most of the innovative solutions in public procurement address the issues from the demand side (collaborative procurement, for example, encourages the use of collective purchasing power among public authorities, or the use of e-procurement to leverage technology for a more efficient administrative procedure), the move to encourage innovation through procurement is shifting the so-called ‘burden’ to innovate to the supply side.<sup>(14)</sup>

One leading example is the use of Building Information Modelling (BIM) for the procurement of construction or work services, a topic that is extensively discussed in the chapter of Di Guida and co-editor Racca. Under the traditional approach to public procurement, collaboration between and among contractors or economic operators, unless they will participate as a single offeror by submitting a single bid or proposal in a particular project as a joint-venture or consortium, is often highly regulated, if not totally prohibited. The reason for this is that collaboration among them poses a high risk for potential bid-rigging or may even trigger the possibility of creating a harmful collusion or worse corruption in the market, which would contravene the overarching principle of open competition in public procurement.<sup>(15)</sup> BIM, on the other hand, encourages collaboration even among contractors through the establishment of what is known as a ‘framework alliance’ or a contract between

(13) See S. KELMAN, “Meet the Contracting Folks Who are Encouraging New IT Vendors”, Public Spend Forum, March 2018.

(14) G.L. ALBANO, “Demand aggregation and collusion prevention in public procurement”, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (G.M. RACCA and C.R. YUKINS eds), Brussels, Bruylant, 2014, p. 155; G.L. ALBANO and C. NICHOLAS, *The Law and Economics of Framework Agreements*, Cambridge, CUP, 2016.

(15) A. SÁNCHEZ GRAELLS, “Prevention and deterrence of bid rigging: a look from the new EU directive on public procurement”, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, op. cit., p. 171; A. LÓPEZ MIÑO and P. VALCARCEL FERNANDEZ, “Contracting authorities’ inability to fight bid rigging in public procurement: reasons and remedies”, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, op. cit., p. 199.

“one or more suppliers in order to establish the terms governing the project contracts that are awarded over an agreed period”,<sup>(16)</sup> albeit, not necessarily creating a single proposal or bid among parties therein. While a framework agreement is used in times when the contracting officer has an open-ended for the products or services, subject to the framework agreement, the framework alliance is an agreement between and among suppliers or contractors within a supply chain, though they may not necessarily be within the same line of industry. For example, in the supply chain for building construction, an alliance may be formed among a group of architects for the design, another group of engineers for the building phase, and a new group of economic operators for future construction maintenance. An Alliance Manager, supported by the new technologies (smart contracts, blockchain), should assure the right incentives for all the alliance partners to further the common goal of a prompt and efficient execution, overcoming the opportunistic behavior of suppliers after the award.

Another important approach under this category is the innovation in public procurement under the Egyptian public private partnership (PPP) legislation. While establishing a public private partnership is, more often than not, exempted from the coverage of public procurement legislation,<sup>(17)</sup> Judge Ismail explains that the Egyptian legislation governing PPPs stipulates that investor selection is subject to the principles of publicity, transparency, free competition, equal opportunity, and equality. Although there is no special administrative organ in Egypt that is concerned with State procurement, the PPP legislation stipulates that a special pre-qualification committee shall be established by an administrative decree from the concerned authority, and to maintain fair competition and equality the administrative authority may use a ‘dialogue process’ in selecting the best private partner.

Innovation under this perspective is not or should not be limited to the ability of the procuring entities to acquire the ‘best-value’ products or services from innovative suppliers. Procuring entities must also be able to do it in the most efficient way, that is, at the time when the products or services are actually needed. Otherwise, no matter how innovative the products or services that are delivered by so-called innovative suppliers, if the products or services arrive after the fact, then their ‘use value’ diminishes in time. This may be one

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(16) G.M. DI GUIDA and G.M. RACCA, “From Works Contracts to Collaborative Contracts: The Challenges of Legal BIM”, Chapter 8 in this book.

(17) See World Bank Group, “What are public private partnership?”, February 2018: “PPPs typically do not include service contracts or turnkey construction contracts, which are categorized as public procurement projects, or the privatization of utilities where there is a limited ongoing role for the public sector.”

of the reasons why the concept of ‘amazon.gov’ even emerges, which is a topic covered by the chapter of McKeen.

McKeen shows us a picture of a future-scenario that is already unfolding: an official ordering goods to meet public requirements much as a private person would order home supplies from one of the biggest online markets, such as Amazon. The failure of a procurement system – even one from a highly-advanced economy such as the US – to address public requirements efficiently and well has triggered government support (in both Congress and the agencies) for a platform for public procurement that is more expedient and more market-responsive at a presumably reasonable price, by attempting to simulate, if not necessarily adopt, the procurement processes in the “current commercial e-portal market” through the use of e-portals on a government wide basis. Whether this will in fact encourage innovative suppliers to participate in public procurement is yet to be seen. Or to pose a simple question, can a more liberalized model of public procurement promote more innovation? The risks of non-transparent algorithms and discrimination in commercial platforms remain and provide an extraordinary incentive for promoting effective procurement systems using more traditional means.

### 1.3. Innovation in the Procurement Process

A third meaning is *innovation in the procurement process* itself as new methods and approaches for the procurement process. This introductory chapter, and the accompanying chapters by Locatelli, Simovart and Borodina, Pignatti, Ponzio, and McKeen, address these new approaches.

Locatelli discusses digitization, the use of self-declaration via a standard form European Single Procurement Document (ESPD), joint cross-border procurement (JCBPP) and cooperative procurement via institutional bodies (e.g. CPBs) as the main innovations under Directive 2014/24/EU on public procurement. He argues for the need for the EU Member States to go beyond the compulsory requirements of the Directives by combining full digitization of the procurement process from planning to archiving (‘end-to-end e-procurement’), and stresses the possibility of cooperation between large buyers in areas of mutual interest or between buyers not necessarily located in bordering areas (‘joint cross-border procurement’). Although public procurement remains highly regulated, he explains that the novel approaches under the new Directives encourage the Member States to establish public procurement systems which may overcome market fragmentation and generate efficiencies and savings, and which can contribute to economic growth. He argues, importantly, that the Directives mark a pathway to improved procurement systems in the Member States.

Since the transition to ‘digitized’ procurement process is becoming inevitable in EU Member States, *i.e.*, the new directives call for the gradual yet mandatory transition of the initial phases in the procurement cycle to e-procurement, then the development of innovative procurement tools that will enhance efficiency in public procurement without compromising other procurement principles such as integrity, transparency, and competition is now a necessity. That objective can best be addressed by expanding the procurement networks among contracting officials across borders in order to share best practices that may be adopted or modified to meet the requirements not only of the end-users or the public in general, but, more importantly, to ensure compliance with the evolving regulations in procurement processes.

Simovart and Borodina give us a good example of the implementation of digitization under Directive 2014/24/EU using the Estonian e-Procurement Model (e-PR). They attribute the success of the e-PR (*i.e.*, increasing the share of electronic procurement to 92% in 2016 and facilitating a smooth transfer to 100% e-procurement soon) to the comprehensive nature of the whole electronic procurement environment, that is, e-PR not only supports full electronic award procedures (*i.e.*, from pre-award phase to the awards of the contracts), it also contains an electronic register of complaints (*i.e.*, registration of complaints is limited to the lists of the complaints submitted to the Complaints Board and the decisions made; submission of complaints is not yet included) as well as access to a user help and information portal (e.g., legal regulations on both EU and the national level, references to Court cases and summaries of case law of both the CJEU and Estonian Supreme Court, research conducted on the request or by the Ministry of Finance, etc.). Pignatti, on the other hand, elaborates on various electronic tools that may be used within the entire procurement cycle, which Ponzio supports by expounding on the best practices in innovative procurement across Eastern Europe. From another perspective Romeo, in her chapter on “Autonomy and Innovation in Italian Regional Procurement: The Sicilian Model” analyzes whether the European principles of opening the market and free competition can actually prevent various forms of barriers and/or possible discrimination in access to regional public procurement markets.

Despite the various forms of innovation in public procurement, there is still a challenge in how other jurisdictions, most particularly those in developing countries and even some countries with emerging economies, might catch up with the innovations in public procurement among advanced economies such as the U.S. and the EU Member States. In fact, while ‘best value’ or Most Economically Advantageous Tender (MEAT) procurement is already a staple in advanced economies; that is, it is rare (in the U.S. federal market)

to see a complex procurement procedure that is not based on a “best-value” trade-off between quality and price, it is still a principle sometimes resisted among procurement specialists in developing countries where procurement is primarily based on ‘low-priced’ awards.

The evolution of the MEAT to a value-based approach in specific sectors seems to be the future challenge for innovation.<sup>(18)</sup> The outcome-based healthcare model, for example, should provide a patient-centric approach with outcome measurements of the improvement both to the quality of care for patients and to the system in terms of sustainability (circular economy principles) and efficiency, to assure the long-term strength of healthcare systems.

The good news is that international organizations such as the Organization for Economic Cooperation and Development (OECD) have international tools (e.g., the Methodology for Assessing Procuring Systems – MAPS) that are used to promote quality assurance, among other goals. MAPS was originally intended to protect the funds from OECD donor-countries that are being spent in developing countries from potential risks caused by those countries’ procurement systems; MAPS has, in fact, evolved into a quality-assurance tool for a more “innovative” procurement system in non-OECD countries. For a complete appreciation of the OECD MAPS, please refer to the chapter of Magina and Diesing on innovation in the evaluation of public procurement systems.

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In our introduction here, we have decided to focus on innovative procurement that crosses borders not only because it poses some of the toughest challenges in modern procurement, but also because it so successfully captures the other forms of innovation: cross-border procurement, while very innovative, also makes it easier for agencies to purchase innovative solutions emerging around the world, and nurtures innovative suppliers.

## ***2. Innovation Through Cross-Border Procurement: Key Constraints***

At present, probably the most ambitious innovation in procurement is ‘joint procurement’, either inside a country (overcoming the traditional coincidence

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(18) See EURIPHI project (European wide Innovation Procurement in Health and Care) Consortium (involving 14 PPOs, of which 10 have a regional or national remit and service providers from 6 countries who, together, procure for more than 200 care service providers), developing a Value-Based Procurement of innovative solutions to enable the cross-border transformation of health and social care delivery.

of the procuring entity that buys for itself) and the even more challenging cross-border procurement, which typically involves cross-border cooperation (often cooperation between public agencies, or central purchasing bodies) from different countries.

This type of cross-border cooperation is emerging around the world; in the United States, it is commonly referred to as ‘cooperative purchasing’,<sup>(19)</sup> while in Europe it is called ‘joint procurement’. In his chapter on cooperative purchasing in the United States, Kaufman discusses some of the U.S. strategies for cooperative purchasing among States – strategies that present, in many ways, illustrative examples of the same legal and management issues that dog joint purchasing in the European Union, described by Roberto Cavallo Perin with co-editor Gabriella Racca, Ivo Locatelli and Patricia Valcarcel in their respective chapters.

The main focus here is on cross-border procurement, which presents ancient problems but offers remarkable promise for the future.

The 2014 Procurement Directive not only explicitly allows contracting authorities to cooperate in joint cross-border procurement but forbids Member States to prohibit such possibility. It explicitly states that “[a] Member State shall not prohibit its contracting authorities from using centralized purchasing activities offered by central purchasing bodies located in another Member State”, and indicates that national law in conflict with these provisions would be in breach of the Directive. It is clarified that cross-border procurement should not be used for the purpose of avoiding the application of national mandatory public law provisions. As with any European provision the Directive language endorses, cross border-procurement should not be applied with elusive, distorting illegal purposes. The same Directive recalls the legal and practical difficulties in purchasing from contracting authorities located in other Member States or jointly awarding public contracts; yet, it also recalls that the aforementioned cooperation was already possible according to common principles of cooperation.

The initial cross-border procurement supported by EU pilot projects saw the evolution from benchmarking to directed coordination, and eventually to the definition of common technical specifications related to separate procedures, to award procedures delegated to other contracting authorities, and purchases of goods and services from delegated central purchasing bodies of other Member States or more recently through the establishment of European

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(19) See, e.g., F. TROWBRIDGE VOM BAUR, “A Personal History of The Model Procurement Code”, *Pub. Cont. L.J.*, 149, 1996, 168; *id.*, “Early Days of Government Contract Practice”, *Public Contract L.J.*, 1989, 18, pp. 446-459.

joint subjects established under national or Union Law.<sup>(20)</sup> Also European Groupings of Territorial Cooperation (EGTCs) might fit the cooperation among CBPs from different countries for the purpose of establishing cooperation for joint cross-border procurement.

In the U.S., some examples of joint purchasing: cooperative purchasing, as made available to State, local and tribal governments by the U.S. federal government's primary centralized purchasing agency, the General Services Administration (GSA), under GSA's Multiple Award Schedules (MAS) contracts (the largest framework agreements in the U.S. federal government, worth tens of billions of dollars per year); and, cooperative purchasing made available to a broad variety of State and local agencies under the National Association of State Procurement Officials (NASPO) ValuePoint contracts (which are described in much more detail in Justin Kaufman's accompanying piece).

We should stress that we are drawing on selective examples here. Not all GSA framework agreements, for example, are available for cooperative purchasing; our focus here is only on the information technology agreements, which can be used by State and local purchasers in the United States. For an effective comparison, we will similarly focus on the information technology contract sponsored by NASPO-ValuePoint, the multi-billion-dollar contract which is run by the State of Minnesota on behalf of the other NASPO-ValuePoint members.

To gain a better sense of joint procurement's future trajectory, the focus is on the institutional constraints that do so much to shape joint procurement. Those constraints also relate back to the first two types of innovation in procurement – though cross-border procurement is itself innovative, the constraints that slow this strategy make it more difficult to purchase innovative technology across borders, and to foster innovation among prospective contractors.

Cross-border procurement is inherently clumsy, because it requires different public agencies to reconcile and apply their sometimes radically different rules. While recent moves towards harmonization make it easier to reconcile different systems' regulatory regimes,<sup>(21)</sup> stark differences remain, in part because those differences reflect divergent approaches to the social and political issues that often inform procurement law. At the end of the day, therefore, joint or cooperative purchasing (we will use the terms interchangeably) demands compromises between legal regimes.

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(20) In particular, art. 39, Dir. 24/2014/EU, includes "European Groupings of territorial cooperation under Regulation (EC) No. 1082/2006 of the European Parliament and of the Council" among those joint entities which may be set up by "contracting authorities from different Member States" to carry out joint cross-border procurement.

(21) *See, e.g.*, United Nations Commission on International Trade Law (UNCITRAL), "Model Law on Public Procurement", 2011; WTO, "Agreement on Government Procurement", 2012.

Despite the awkwardness inherent in cooperative purchasing, it does offer real promise as an innovative way forward.

Cross-border purchasing makes it possible to consolidate public purchasing demand in not one but *many* jurisdictions, and so makes it easier for public agencies to deliver higher quality, lower-priced goods and services to their constituent populations.

In the case of the European Union, cross-border procurement could become a strategic tool for strengthening the European single market, promoting capacity building among contracting authorities, and advancing social and environmental goals.(22)

The different perspectives that inform cooperative purchasing in the United States will become evident and of great interest especially as they show that the rules and principles of the European Directives on procurement deeply affect all levels of European procurement, from the national level to the smallest municipalities. This difference, as outlined already in our previous book, shows how from this perspective the European Union goes much further in fostering cross-border procurement than the U.S. federal government, with all the subsequent consequences.

The combined purchasing power and the possible goals of industrial policy of Member States, focused on specific sectors or in a much limited scale among public central purchasing bodies or even municipalities or regions from the same or different Member States, can be advanced through joint procurement.

Joint procurement, especially in the European context, does not necessarily mean huge contracts but can promote specific strategies related to each relevant market. Such strategies may call for the division of requirements into smaller lots in order to encourage participation and the growth of SMEs, depending on how many economic operators are involved in any relevant procurement market.

Cross-border purchasing also might allow public agencies to leapfrog corruption and, from this perspective, there is a continuity with the previous book in this series(23) that focused on integrity and efficiency issues that, in this new and wider perspective, are always taken into account. A public buyer in a corrupt country, isolated in a sea of corruption, could in principle purchase from, through cross-border procurement instruments, a “clean” centralized

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(22) R. CAVALLO PERIN and G.M. RACCA, “European Joint Cross-border Procurement and Innovation”, Chapter 3 in this book.

(23) G.M. RACCA and C.R. YUKINS (eds), *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, coll. Droit administratif/Administrative Law Collection (J.-B. AUBY dir.), Brussels, Bruylant, 2014. See also G.M. RACCA, R. CAVALLO PERIN and G.L. ALBANO, “Public Contracts and International Public Policy Against Corruption”, in *Transnational law of Public Contracts* (M. AUDIT and S.W. SCHILL eds), Brussels, Bruylant, 2016, p. 845.

purchasing agency in another jurisdiction, which would thus be in a stroke both bypassing and disabling a corrupt procurement system. Similarly, joint purchasing might permit procuring entities to face down cartels or unreasonable fragmentations of the market in specific sectors.

Finally, and most practically, cross-border procurement allows public purchasers to diversify their supply chains, which sharply reduces the risk that those supply chains will collapse – or concomitantly, that prices will balloon out of control – when local emergencies or natural disasters strike, as inevitably they do.

The promise of cross-border procurement must, of course, be weighed against its perils. Joint procurement faces severe constraints, some of which are detailed below. Those constraints impose practical limitations on cross-border procurement, and – equally importantly, for our purposes here – suggest how lawyers and regulators should think critically about cross-border procurement, as it expands in importance.

### 2.1. First Constraint: A Friendly Environment

The cross-border compromises inherent to joint procurement in turn present the first institutional constraint: *only cooperative public bodies* can embark on joint procurement together, which probably means that only friendly governments or other contracting entities, not adversaries, can engage in joint procurement.

Reciprocal defense procurement agreements between the United States and its allies<sup>(24)</sup> probably mark the outer boundary of this practical constraint: they demand technical cooperation in the purchase of defense materiel and supplies, to enhance interoperability in defense operations, which means as a practical matter that only allies, not enemies, can join these agreements. For many of the same reasons, Schoeni shows how it is probably no accident that the two most prominent examples, internationally, of cross-border procurement – in the European Union, and between States in the United States – arose in the context of stable systems, already politically and economically integrated.

As noted, one example for integration might be the European Grouping of Territorial Cooperation (EGTC). Interestingly, no similar integration is prevalent among U.S. States. EU Member States are encouraged to develop various forms of administrative cooperation towards an integrated system of public administrations for the enhancement of EU social cohesion. In fact, most EGTC structures remain within limited geographical areas (‘non-hostile

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(24) See U.S. Department of Defense, “Reciprocal Defense Procurement and Acquisition Policy Memoranda of Understanding”, October 2017.

environments’) and particular sectors with ‘common economic interests’ that might also entail joint procurement activities.(25)

Conversely, this constraint – cooperative procurement works far better among friends – means that it probably will be much more difficult to use cross-border procurement in hostile environments, such as in post-conflict circumstances or in countries experiencing hyper-corruption. Thus, for example, it would be very difficult for a schoolteacher in a war zone to purchase through a centralized purchasing agency in another, safer country; although the purchase itself might be done across the Internet, perhaps even on a mobile phone, the practical, legal and financial obstacles might well make the purchase unworkable or very difficult.

To overcome these challenges and fulfill the promise of cross-border purchasing, much more careful attention will need to be paid to ‘ruggedizing’ joint procurement if it is to be extended to high-risk environments. To serve as a useful tool in hostile environments, cross-border purchasing should be made as simple as possible, and delivery and payment should be straightforward and, where necessary, secured through traditional means of assuring performance, such as stand-by letters of credit.

In considering these efforts to make cross-border purchasing work in hostile environments, purchasing authorities may wish to consider the electronic commerce model suggested by Section 846 of the U.S. National Defense Authorization Act for fiscal year 2018.(26) U.S. agencies will be pilot-testing commercial electronic commerce platforms for purchases under the lowest threshold (roughly \$10,000, and potentially much higher). This new approach – dubbed ‘amazon.gov’ by some – means that public purchasers will be able to buy directly from commercial marketplaces, bypassing traditional public procurement requirements for publication, qualification and competition. Despite misgivings by some, this new highly commercial approach might make it easier for government users in post-conflict or highly corrupt environments to purchase across borders. As already recalled the transparency issues with this approach have yet to be taken fully into account.

## 2.2. Second Constraint: The Context

The second, related constraint stems from the *broader political, legal and administrative context* in which public agencies undertake joint procurement – and while it is related to the first, this constraint highlights differences, not similarities.

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(25) R. CAVALLO PERIN and G.M. RACCA, “European Joint Cross-border Procurement and Innovation”, Chapter 3 in this book.

(26) See generally, U.S. General Services Administration, *Procurement Through Commercial E-Commerce Portals Phase II Report: Market Research & Consultation*, April 2019.

Joint procurement in the European Union receives strong support from Brussels because (it is hoped) that cross-border cooperation in procurement will also help to develop internal market and to *integrate* the European States – the ultimate goal of EU policy.(27)

In the United States, in contrast, cooperative purchasing has grown as a means of reducing cost and improving procurement outcomes; there is almost no overarching goal of integrating the U.S. economy through cooperative purchasing.

These partially differing policy goals lead to different legal outcomes. While our focus here is on institutional issues, the rules reveal a great deal – like the wind’s ripples on a sand dune, the institutional forces seem to leave tracing marks on the legal rules that govern cooperative purchasing.

Take, for example, the legal issue of which procuring entity will bear the risk of transparency and competition – which entity, in other words, is ultimately responsible for ensuring that cross-border awards are done in a fair, competitive and transparent manner. How that risk is allocated and addressed is an important measure of the rules governing a system of joint procurement.

The two U.S. models under study here (the GSA schedules and the NASPO ValuePoint vehicle) leave that risk largely with the customer agency. The GSA schedule contract says the risks of loss or damage to the supplies under the GSA contract typically will remain with the supplier until delivery,(28) while the ValuePoint contract shifts the risk of loss to the local customer agency.

While historically the NASPO ValuePoint contract might have read a local requirement into the contractual framework, the NASPO ValuePoint master agreement (the master framework agreement between a lead State and its vendors) was redrawn recently. Previously, the master price agreement provided that if a customer agency’s laws required a specific provision – a provision mandating competition, for example – that provision would be read into the framework contract between a vendor and the purchasing agency – and the framework contract would take precedence.

That strong precedence for special local requirements has disappeared from the ValuePoint contracting system. The current master agreement now provides merely that the local jurisdiction’s direct contract with the contractor (the ‘Participating Addendum’) is to be interpreted consistently with local law; the revised contractual structure, however, gives no effect to local requirements not called out in the Participating Addendum. In practice, this means that if

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(27) EU Comm., “Recommendation on the professionalisation of public procurement: Building an architecture for the professionalisation of public procurement”, C(2017) 6654 final, October 2017.

(28) See, e.g., General Services Administration Federal Supply Service Authorized Federal Supply Schedule Price List, Contract No. GS-00F-0049M Ordering Period: 3/29/02 - 8/23/19, 37.

the implementing contract is silent, local requirements – such as competition or transparency requirements – can be bypassed completely. What this means, in practice, is that the buying agency bears almost all risk of compliance.

The GSA schedule contracts shift those burdens even more starkly to the State and local governments that use the GSA framework agreements under cooperative purchasing. This may be because cooperative purchasing was, to some extent, forced on GSA by Congress: GSA offers cooperative purchasing for only certain frameworks (such as information technology, Schedule 70), and even that arrangement had to be specially mandated by Congress.

The standard GSA schedule terms, which define certain obligations that are shaped by federal law and policy – how payment will be effected, for example – may be amended to accommodate non-federal customers (the payment clause, for example, can be modified to accommodate a local buyer standing in the shoes of a federal agency). Beyond that, though, the GSA acquisition regulations cut the local or State framework agreement free from the master framework agreements (the GSA MAS contracts): the regulations provide that a contract between a vendor and a buying agency forms a *new* contract, “which incorporates the terms and conditions of the Schedule contract” but under which the “U.S. Government shall not be liable”, whether for performance or nonperformance.<sup>(29)</sup> The GSA contracts, in short, do not resolve how local mandatory requirements should be addressed when local governments use these federal contracts.

The terms of the GSA schedule agreements, when applied to cooperative purchasing by State and local governments, thus reflect the federal government’s very limited interest in integrating procurement regimes across the United States: the federal government is willing to allow State and local governments to economize by using (replicating, really) the GSA schedule contracts, but the federal government makes essentially no effort to use the framework agreements as an integrative tool. Conversely, in fact, the federal government’s ‘hand’s-off’ approach shifts substantial transaction costs to customer agencies at the State and local levels (because they must fill all the contractual gaps left by the federal government), and (by neutralizing the robust federal framework agreements) can increase risks for using agencies.

The European Union’s main procurement directive suggests another way forward, one that reflects the European Union’s abiding interest in economic integration, and in joint procurement as a means of encouraging innovation. The European directive’s recital 71 states, in relevant part (with emphases added):

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(29) GSAR 552.238-79, 48 CFR § 552.238-79, Use of Federal Supply Schedule Contracts by Non-Federal Entities.

“Where several contracting authorities are jointly conducting a procurement procedure, they should be *jointly responsible for fulfilling their obligations* under this Directive. However, where only parts of the procurement procedure are jointly conducted by the contracting authorities, joint responsibility should apply only to those parts of the procedure that have been carried out together. *Each contracting authority should be solely responsible in respect of procedures or parts of procedures it conducts on its own*, such as the awarding of a contract, the conclusion of a framework agreement, the operation of a dynamic purchasing system, the reopening of competition under a framework agreement or the determination of which of the economic operator party to a framework agreement shall perform a given task”.

From a U.S. perspective, the Directive’s allocation of responsibilities in joint procurement seems commonsensical: by allocating responsibility among the parties based on which party controls a particular step in the procedure, the Directive is following the same principle of ‘cheapest cost-avoider’ which is a staple of U.S. risk-allocation approaches. More markedly, the Directive’s allocation of responsibilities does *not* follow the approaches of the ValuePoint and GSA arrangements discussed above, which aggressively shift many more burdens to the State and local purchasing agencies. In Europe, by the same logic, national mandatory requirements should be applied in European joint cross-border procurement too.

Perhaps most importantly, though, the Directive’s recitals reflect an understanding in the European Union that remedying the allocation of risks and obligations between parties to a joint procurement should facilitate that cross-border procurement. Recital 73 notes that joint procurement “by contracting authorities from different Member States” often encounters “legal difficulties concerning conflicts of national laws”, and as a result “contracting authorities are still facing considerable legal and practical difficulties in purchasing from central purchasing bodies in other Member States or jointly awarding public contracts”. To ease these problems, the recitals suggest that in “order to allow contracting authorities to derive maximum benefit from the potential of the internal market in terms of economies of scale and risk-benefit sharing”, new “rules on cross-border joint procurement should be established in order to facilitate cooperation between contracting authorities [...] by creating cross-border business opportunities for suppliers and service providers”.

The text of the Directive’s Article 39 goes a step further, and suggests a burden-allocation that could radically reshape the way that joint procurement is done – a reallocation apparently driven, again, by the institutional support in Europe for joint cross-border procurement and administrative cross-border cooperation.

The Directive's Article 39 shifts the center of gravity towards the *selling* agency (the centralized purchasing agency which coordinates the joint procurement), and says that the national laws of that centralized purchasing agency (including, presumably, national laws regarding competition and transparency) will govern important steps through joint procurement:

“The provision of centralised purchasing activities by a central purchasing body located in another Member State shall be conducted in accordance with the national provisions of the Member State where the central purchasing body is located.

The national provisions of the Member State where the central purchasing body is located shall also apply to the following:

- (1) the award of a contract under a dynamic purchasing system;
- (2) the conduct of a reopening of competition under a framework agreement;
- (3) the determination pursuant to points (a) or (b) of Article 33(4) of which of the economic operators, party to the framework agreement, shall perform a given task”.<sup>(30)</sup>

Applying these European rules to the U.S. structures apparently would mean, for example, that an order awarded under a ValuePoint contract would be governed by the sponsoring State's competition and transparency rules. Similarly, were this rule to apply in the United States, orders by State or local governments made through cooperative purchasing under the GSA schedules might be covered by strict federal competition and transparency rules, and could be subject to the federal government's protective terms and conditions. The rule proposed by the Directive, in other words, could lend cooperative purchasing in the United States very important legal structure and protections.

Rather than leaving important elements of the contracting process undefined – as ValuePoint and the GSA schedules do – the European rule, born of integration, could integrate joint cross-border procurement into mature, protective regulatory regimes. This could lead to effective harmonization of national implementations, through administrative cooperation and joint procurement experiences.

There could be practical effects, too, if the European rule were applied to U.S. forms of cooperative purchasing. The sponsoring agencies' mature procurement systems – GSA's relatively sophisticated means of ensuring competition and transparency for schedule orders, for example – could be extended, in practical terms, to orders by customer State or local governments. In the ValuePoint system, if the orders were subject to stricter and enforceable rules of competition and transparency, the sponsoring agencies would

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(30) Dir. 24/2014/EU, Art. 39(3).

have incentives to develop transparent and competitive ordering systems that customer agencies could use; in this way, ValuePoint orders by State or local governments could no longer be made ‘invisibly’. By making the sponsoring agency’s own rules applicable to cooperative purchasing, the European rule could, in effect, nurture contracting processes (transparency and competitive ordering, for example) which took advantage of the sponsoring agencies’ mature contracting systems.

Those practical changes of course would need to take into account the third constraint we will discuss here: the nature of the sponsoring centralized purchasing agency itself. In assessing whether and how joint procurement should be regulated and directed, policymakers must be frankly conscious of the unique perspectives – and conflicts of interest – that the centralized purchasing agencies may bring to joint procurement.

The European pioneering experiences on joint procurement might take advantage of all the risks and challenges faced in the U.S. and promote the European goals through similar tools applying EU social goals.

### 2.3. Third Constraint: The Centralized Procurement Agencies

The third constraint relates to *who* is coordinating the joint purchasing (or joint procurement): the *centralized purchasing bodies which carry their own sets of problems and pathologies*. The using agencies which rely on joint procurement typically are as disparate as their missions, from health to defense. In contrast, the *selling* agencies – the centralized purchasing agencies (bodies) that offer cross-border procurement – tend to be focused on common business imperatives of increasing sales, revenues and (sometimes) profits, in the U.S. experience. Again, in this perspective the European experience is still at the very early stages except for some more advanced experiences in national joint procurement. The strategic use of public procurement for industrial policy objectives, to drive sustainability and innovation, is highlighted in the text below as the next challenge.

The centralized purchasing agencies’ goals are not, of themselves, objectionable; they do suggest, though, that prudent regulation may be needed in cross-border procurement, because the central actors themselves may be distracted by institutional imperatives that are not resolved by the normal dynamics of a procurement market.

The two examples from the United States may help illuminate these points. The first is GSA, the centralized purchasing agency at the heart of the federal government which oversees tens of billions of dollars in annual purchases. GSA’s centralized purchasing function is sustained by user fees, not

appropriations, an institutional imperative which shapes GSA's procurement strategies – including cooperative purchasing.

Because GSA has strong institutional imperatives to contain costs and risks, and because State and local governments across the United States present a geographically dispersed, fractured market outside GSA's normal core mission of serving federal agencies, GSA has every incentive to contain its exposure to cooperative purchasing. The contracting system used to implement GSA's cooperative purchasing reflects that approach: as was described above, while GSA allows State and local governments to use certain GSA schedule contracts through cooperative purchasing, GSA extends almost none of its normal legal protections or processes to those State and local government user agencies. GSA has, it seems, structured cooperative purchasing to minimize its own administrative costs and legal exposure.

The ValuePoint model offers its own lessons, informed by the unique posture of the State purchasing officers who shape the model. Their membership organization, the National Association of State Procurement Officials (NASPO) is, after all, the sponsor of the ValuePoint model, NASPO earns fees from the ValuePoint contracts, centralized State purchasing agencies run the master framework agreements, and State agencies typically may buy from those agreements only if the State purchasing officers give their permission. The NASPO ValuePoint structure thus presents a welter of potential conflicts of interest; we will focus here on only one, as illustration, which manifests in ValuePoint's heavy reliance on original equipment manufacturers (OEMs) rather than resellers.

Centralized purchasing agencies present a classic principal-agent conflict of interest problem in procurement: they are agent-intermediaries whose interests may diverge radically from those of user agencies. The centralized purchasing agencies that sponsor the ValuePoint master agreements are no different: while they have an interest in making goods and services available to customer agencies in other jurisdictions in order to spread administrative costs across more sales and enhance the agencies' collective negotiating leverage with vendors, the sponsoring centralized purchasing agencies have an acute interest in reducing costs and legal exposure.

That self-interest in the sponsoring agencies helps explain why the ValuePoint information technology contract, which is used for billions of dollars in annual purchases, is limited to 30 OEMs. (The counterpart GSA Schedule 70 information technology contract, in contrast, includes thousands of OEMs and resellers). The centralized purchasing agency implementing the ValuePoint contract has decided not to rely on resellers – typically smaller businesses which offer more diverse solutions, but which can present idiosyncratic

performance risks – and instead to contract only with OEMs, which naturally limits competition and choice in the ValuePoint marketplace. The focus here is not on whether that trade-off makes sense, but rather on the fact that it *is* a trade-off – a conscious management decision driven by the centralized purchasing agency’s own posture and institutional imperatives, which may not yield optimal results.

The U.S. experience on central purchasing bodies through either the GSA model (sanctioned by the U.S. federal government) or the ValuePoint model (sanctioned by the participating States) points up the fact that the European Union does not have a ‘EU central purchasing body’ comparable to the GSA, but the U.S. experience suggests the importance of cooperation to reduce administrative costs and to consolidate public purchasing powers though with the same perils in potential conflicts of law.

It is interesting to learn how U.S. federal procurement, with all its sophistication and efficiency, has not been a constraining model for most State and local procurements. The States generally maintain a separation from the federal government in terms of procurement means and goals. Aside from limited guidance for State and local procurements done with federal grants, there is no ‘Federal Procurement Directive’ to promote the opening of a ‘U.S. procurement market’, comparable to the EU Directives, which seek to open EU public procurement markets, with strategic goals underlying European procurement policy.

In fact, the European experience on joint cross-border procurement may be considered in an early stage when compared to the U.S. one, so that many of the issues are not yet manifested or have been solved through European principles or have been correctly addressed in the rules. In fact, most of the EU joint cross-border procurements were developed as pilot projects funded by EU funds. One may argue that the EU is trying to, so to speak, avoid the similar risks posed by the U.S. ‘umbrella contracts’, which is why it opts to learn from the pioneering experiences of cooperating EU Member States.

The actual aim is to encourage the ‘horizontal cooperation agreements’ of joint entities such as the ETCGs in order to take full advantage of a European single market for the benefit of the European citizens. Unlike the U.S., the EU’s approach in promoting joint and cross border procurement through central purchasing bodies is not only to ensure cost-savings but also to promote other goals such as encouraging cross-border participation of SMEs, counteracting cartels, assuring integrity and efficiency, furthering environmental and other social goals, and developing circular economy tools. Interestingly, despite convergence, the EU’s perspective on “Unity in Diversity” allows EU Member States to promote those ‘other goals’, which can be shared cross-border on a

case by case basis and which could result in some of the same ‘trade-off’ issues that U.S. agencies are currently addressing.

#### 2.4. Fourth Constraint: Language Barriers and Limited Procurement Professionals

Since cross-border procurement covers contracting authorities from different procurement entities in multiple States and local agencies, it calls for procurement professionals who are adept not only in their own procurement regulations and practices but also, potentially, in the regulations and practices of other procuring entities that use the cross-border procurement vehicle. As already discussed in the chapters of Kaufman, Cavallo Perin and Racca, cross-border procurement poses challenges not only in addressing significant issues arising from variations in their procurement regulations and practices, but more importantly in managing cooperative contracts. Cross-border procurement requires a balance between efficient delivery of products and services that offer best value for the government, and the need to ensure fair and open competition in a manner that is ethical and transparent. Procurement professionals must strike that balance while they continue to search for innovative ways of improving the acquisition process without violating the basic principles of fairness and competition.(31)

The 2017 European Commission report on cross-border trade in public procurement highlighted “unfamiliar legal context or formal requirements (e.g., contract, labor law, certificates to provide such as special permits necessary for offering services abroad etc.) leading to market entry barriers in awarding the country” and language barriers as two of the perceived obstacles to cross-border procurement by both the businesses (sell side) and the contracting authorities (buy side).(32) While a language barrier might not be an issue in cooperative purchasing among U.S. States, *i.e.*, English is the common language irrespective of States and local agencies, it can be a big challenge among procurement professionals in EU Member States, since the EU has 24 official languages.(33) In fact, the EU small and medium enterprises (SMEs) regarded language barriers as the foremost barriers to cross-border procurement.(34)

(31) D.A. HINDMAN III and R.N. PARKER, “Piggyback Contracts: The Benefits and the Limits of Shared Purchasing”, *Procurement Lawyer*, 49, 3, p. 16.

(32) EC, “Measurement of impact of cross-border penetration in public procurement”, February 2017.

(33) There are currently 24: Bulgarian, Croatian, Czech, Danish, Dutch, English, Estonian, Finnish, French, German, Greek, Hungarian, Irish, Italian, Latvian, Lithuanian, Maltese, Polish, Portuguese, Romanian, Slovak, Slovene, Spanish and Swedish.

(34) *See also* R. WILLIAMS QC, “Improving access for SMEs to cross-border defence procurement”, *PPLR*, 2017, 2, NA41-NA42: “SMEs find it particularly difficult to access cross-border defence contracts due to a lack of information, administrative burdens, language barriers, cultural, legal and administrative differences between EU countries, and costs related to distance”.

Nonetheless, professionalism in public procurement – the other and related constraint considered here – is not a new concept. In the United States, the creation of a position for contract specialist, an upgrade from its previous position as purchasing agent, began in 1959. In 1970, the U.S. Comptroller General emphasized the need “to develop a competent procurement workforce with the capacity for exercising more initiative and judgement in making procurement decisions”. After a series of reports and recommendations, the U.S. Congress passed the Federal Acquisition Reform Act (FARA) in 1996 which provided for the joint authority of the Administrator of the Office of Federal Procurement Policy (OFPP) and the Director of the U.S. Office of Personnel Management (OPM) in establishing the specific requirements for contracting personnel. In 1997, OPM and OFPP jointly issued the new qualification standards for contracting officials, that is, either a college degree or twenty-four semester hours of study in specified business/legal subjects for entry level positions, and, both for all senior-level positions.

In 2015, the OECD recommended the development of a procurement workforce with the capacity to continually deliver value for money efficiently and effectively by ensuring that procurement officials meet high professional standards for knowledge, practical implementation and integrity by providing a dedicated and regularly updated set of tools, for example, sufficient staff in terms of numbers and skills, recognition of public procurement as a specific profession, certification and regular trainings, integrity standards for public procurement officials and the existence of a unit or team analysing public procurement information and monitoring the performance of the public procurement system.(35)

More recently, the European Commission adopted a Recommendation on the Professionalisation of Public Procurement on October 3, 2017. The document enumerated a series of recommendations aimed at increasing the overall professionalism of contracting authorities/entities staff, and particularly focusing on policy architecture, cooperation between and within public administrations, efficiency, transparency, integrity, careers and HR management.(36) Interestingly, the Commission identified three lines of action in professionalisation: 1) developing appropriate policy architecture for professionalisation; 2) improving training and career management of procurement practitioners; and 3) providing tools and methodologies to support professional procurement practice.(37)

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(35) OECD, Recommendation to the Council on Public Procurement, 2015.

(36) EC, Recommendation on the professionalisation of public procurement: Building an architecture for the professionalisation of public procurement, 3.10.2017, C(2017) 6654 final, October 2017.

(37) A. SOLOMONYAN, “A soft tool for making public procurement more professional”, *PPLR*, 2018, 1, NA3-NA4.

Measures have been adopted to address these challenges, as in the case of the innovations related to the Tenders Electronic Daily (TED) common procurement vocabulary when drafting and publishing public procurement notices.(38) Cavallo Perin and co-editor Racca also emphasize the support to contracting authorities in overcoming linguistic barriers during the drafting stage of tender documents and contractual terms, while ensuring that these documents are available in different languages.(39)

In addition, new technologies have been introduced, both at the European and the national levels. As of 15 January 2016, an online machine translation service has been made available, free of charge, for all public procurement notices published in Tenders Electronic Daily (TED), which is the online version of the Supplement to the *Official Journal of the EU*, dedicated to European public procurement. The development of ‘smart contracts’ through new technology may also favor new forms of cooperation with collaborative agreements among suppliers and public administration with different legal and language background, aiming at a shared goal, *i.e.*, the correct and prompt execution of public (smart) contracts.(40)

Tender documents offered in different languages can assure wider transparency to facilitate cooperation which will strengthen the capacity of public administrations to pursue public interests, and further the objectives of growth, innovation and integrity of the European Union.(41)

Within this framework, innovative, joint and cross-border procurement represent unique chances to reshape the relevant systems and achieve a digital transformation towards modern, innovative and sustainable procurement systems fit for the 21<sup>st</sup> century.

### 3. Conclusion

This brings us full circle, then, to the purpose of this book: to foster critical discussion of innovation in procurement. In the case of cross-border joint procurement, as the discussion above reflects, important issues – the governments and the contracting entities which can cooperate, the legal and political

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(38) R. WILLIAMS, “European Communities: proposed adoption of mandatory common procurement vocabulary”, *PPLR*, 2002, 2, pp. 19-20.

(39) E.g., in the HAPPI project, the documents were available in the English, French and Italian languages. For further information on the HAPPI project, see also R. CAVALLO PERIN and G.M. RACCA, “European Joint Cross-border Procurement and Innovation”, Chapter 3 in this book.

(40) G.M. RACCA, “The role of third parties in the execution of public contracts”, in *Contrôles et contentieux des contrats publics | Oversight and Challenges of public contracts* (L. FOLLIOT-LALLIOT and S. TORRICELLI eds), Brussels, Bruylant, 2018, p. 415.

(41) EU Commission, Making Public Procurement work in and for Europe, COM(2017) 572 final, October 2017, p. 7.

imperatives which will inform that procurement, and the institutional biases of the sponsoring agencies, among others – are only now being assessed. To make cross-border procurement work, those issues need to be recognized and, where possible, addressed; as the discussion above shows, and as this volume more generally shows, perspectives from other systems will, we hope, ease those solutions.

BRUYLANT



# **PART I**

## **Crossborder Procurement and Innovation**

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# CHAPTER 1

## Process Innovation

### Under the New Public Procurement Directives

BY

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#### 1. Introduction(1)

With public expenditure on goods, works, and services representing approximately 14 % of European Union Gross Domestic Product with an annual value of nearly €2 trillion, public procurement is critical to the European economy. Transparent, fair, and competitive public procurement across the Single Market creates business opportunities for European enterprises and contributes to economic growth and job creation.

To create a level playing field for all businesses across Europe, EU law sets out minimum harmonised public procurement rules. These rules organise the way public authorities and certain public utility operators purchase goods, works and services. They are transposed into national legislation and apply to tenders whose monetary value exceeds a certain amount while for tenders of lower value, national rules apply (but these national rules must also respect the general principles of EU law).

From 18 April 2016, new rules have changed the way EU countries and public authorities procure. This date was the transposition deadline for three directives on public procurement and concessions adopted in 2014.<sup>(2)</sup> The new rules aim at making it easier and cheaper for small and medium-sized enterprises (SMEs) to bid for public contracts, ensuring best value for money for public purchases and respecting the EU's principles of transparency and competition. To encourage progress in terms of public policy objectives, the new rules also

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\* The views expressed are the author's alone and do not necessarily correspond to those of the European Commission.

(1) I would like to thank Isabel da Rosa for her valuable comments on this paper.

(2) The public procurement Directives are 2014/24/EU on public procurement (the Classical Directive), Directive 2015/25/EU on procurement by entities operating in the water, transport, energy and postal sectors (Utilities Directive), and the new 2014/23/EU on the award of concession contracts (Concessions Directive). The reference of the provisions in this article refers to the Classical Directive only. The three Directives were published in the *OJEU*, L 94 of 28 March 2014.

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allow for environmental and social considerations, as well as innovation, to be taken into account when awarding public contracts.

These new rules simplify public procurement procedures – drastically reducing the number of documents needed for selecting companies – and introduce e-procurement. This will benefit public purchasers and businesses, particularly SMEs. The new rules also open up new forms of joint procurement, clarifying the norms applicable to aggregation. This can spur innovation or/and green procurement, which are hard to implement for the individual and small buyer.

## 2. Joint Cross-Border Public Procurement

A different kind of process innovation has been introduced by the new Public Procurement Directives to those assessed so far. This refers rather to nationality of the parties involved in the process and aims at addressing limitations and lack of clarity of rules in place under the ‘old’ Directives of 2004.

The Directive itself acknowledged that under the previous regulatory regime (Directive 2004/18/EC) joint cross-border public procurement (JCBPP) contracting authorities were still facing considerable legal and practical difficulties in purchasing from central purchasing bodies in other Member States or jointly awarding public contracts by contracting authorities from different Member States. Recital 73 of the Directive is even more explicit, stating that “Joint awarding of public contracts currently encounters specific legal difficulties concerning conflicts of national laws”.

The provisions on JCBPP set out by Directive 2014/24/EU provide for a new legal framework at the EU level.<sup>(3)</sup> Under the previous EU legislation, the possibility for JCBPP was implicit and consequently failed to grant buyers sufficient legal stability. The new rules create a framework that contributes significantly to creating legal certainty for all parties involved and are a significant innovation from a regulatory point of view. In particular, the Directive clarifies the applicability of national measures, determining the applicable procurement legislation.<sup>(4)</sup>

In short, the regulatory framework provides for two different options for joint cross-border procurement: i) procurement via a CPB; and ii) joint procurement involving two or more contracting authorities from different Member

(3) G.M. RACCA, “Joint Procurement Challenges in Future Implementation of the New Directives”, in *Modernising Public Procurement: the New Directive* (F. LICHÈRE, R. CARANTA and S. TREUMER eds), Copenhagen, Djof Publ., 2014, pp. 225-254; S. PONZIO, “Joint procurement and innovation in the new EU Directive and in some EU-funded projects”, *Ius Publicum Network Rev.*, f. 2/2014, pp. 1 and ff.

(4) Parallel provisions are included in Art. 55-57 of the Utilities Directive 2014/25/EU.

States. This latter case includes a further option, relating to the creation of a joint entity.

### 2.1. Joint cross-border procurement using a CPB

Joint cross-border procurement via a CPB is regulated by Articles 39(2) and (3) of the Directive. The provisions set out the terms of the cooperation between a contracting authority and a CPB in another Member State; essentially, they mirror those governing the relations between contracting authorities and CPBs operating within the same Member State in Article 37. The Directive stipulates that Member States should not prohibit the contracting authorities from buying from CPBs located in another Member State. However, in implementing the Directive, Member States are granted the power to specify which type of centralised purchasing activity of the foreign CPB (wholesaler or intermediary<sup>(5)</sup>) can be used by the contracting authority. The wholesaler type is apparently far less common across the EU. Therefore, if a Member State determines in the transposition law that its contracting authorities can only buy from foreign CPBs acting as wholesalers, the chances that its contracting authorities will become involved in joint cross-border procurement are likely to be low. In any event, the provision of centralised purchasing activities via a CPB shall be conducted in accordance with the national provisions of the Member State where the CPB is located; the same logic is applied to the applicable rules on the award of contracts under framework agreements, a Dynamic Purchasing System (DPS) managed by the CPB, or mini-competitions under a framework agreement and the rules governing a multi-supplier framework agreement.<sup>(6)</sup> The objective of this provision is to avoid applying different national legislations to mini competitions when the JCBPP project involves several contracting authorities from different Member States. As regards the rules governing contract management, the Directive is silent and therefore this aspect is to be established by between the parties in a specific agreement.

### 2.2. Joint cross-border procurement between contracting authorities from different Member States

The second case covered by the Directive concerns the case of two or more contracting authorities from different Member States, who jointly award a contract, conclude a framework agreement or operate a DPS. The Directive

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(5) The two roles of CPBs are described in more detail in section 3 of this article.

(6) *See* Art. 39(b) and (c). The principle therefore is that applicable law for the procurement procedure is that of the host CPB; this also applies to remedy procedures.

provides for two different options in order to allocate specific responsibilities among participating buyers: i) an international agreement between the Member States concerned including the necessary elements, or ii) an agreement between the participating contracting authorities setting out the responsibilities of the parties and the relevant applicable national provisions (to be explicitly referred to in the procurement documents); and the internal organisation of the procurement procedure. A ‘safe harbour’ clause concludes the paragraph, making clear that a participating contracting authority fulfils its obligations when procuring from a contracting authority which is responsible for the procurement procedure.

As indicated above, the Directive provides for an alternative way for contracting authorities willing to engage in joint cross-border procurement: the creation of a joint entity established under national or EU law. This entity may include European Groupings of Territorial Cooperation under Regulation 1082/2006 or other entities established under Union law. The Directive sets out the conditions for determining the applicable national procurement rules while the relevant choice is to be made by the participating contracting authority via a decision by the joint entity’s competent body.

### 2.3. Joint cross-border procurement: the policy dimension

The use of joint cross-border procurement is going to be rare, especially if considered as a share of total public procedures run yearly in the Member States. In broad terms, these provisions are intended for niche cases, as they require administrative capacity and resources. Conducting JCBPP involves managing a number of legal and administrative complexities, especially for the coordinating organisation. The challenges to be faced by contracting authorities can be legal, cultural, linked to the coordination effort required, the use of a foreign language in the procedure etc.

Despite these challenges, JCBPP is gaining unexpected interest from a range of stakeholders:<sup>(7)</sup> large cities, cross-border projects involving administrations near borders, projects aiming at using public procurement to develop innovative products or services, inherently cross-border applications such as satellite services etc. In the end, most buyers operating in the EU have similar needs in terms of procurement (schools, providing health services to

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(7) An interesting case is the one of European Procurement Coordination Office (EPCO) hosted by the Luxembourg Central Bank, which supports joint procurement by the central banks of the Eurosystem since 2008. The case is described by S. KAISER, “International joint public procurement. A new initiative hosted by the Luxembourg Central Bank”, 2010, [www.ippa.org/IPPC4/Proceedings/01ComparativeProcurement/Paper1-15.pdf](http://www.ippa.org/IPPC4/Proceedings/01ComparativeProcurement/Paper1-15.pdf).

its citizens, building roads, etc.) and establishing a partnership with another buyer may provide new opportunities.(8)

In any event, the new rules on joint cross-border procurement represent a major process innovation in public procurement procedures. They set the conditions for cross-border use of CPBs and between contracting authorities, for the applicable public procurement law, including the applicable legislation on remedies. From a policy point of view, the main innovative aspects of JCBPP are the following:

- i) JCBPP contributes to exploiting the whole of the internal market from the demand side. Pooling buyers across the single market can more effectively strengthen buyers' bargaining power in oligopolistic markets and contribute to reducing market segmentation.(9) For instance, the BBG-SKI case(10) compelled the supplier to adjust its pricing policy and to prepare one offer for two separate markets. The larger volume was one key negotiating bargaining chip of the two CPBs to challenge the market with regard to selling and pricing policy (large price differences existed for the same product in the two Member States concerned). Besides, exploiting this demand side dimension of the internal market creates new opportunities for generating savings via economies of scale and process efficiency. The cross-border dimension may also lead bidders to offer higher discounts in order to win a contract with a certain prestige (such as an international one).
- ii) JCBPP allows involving a larger number of buyers and this can facilitate risk sharing, for instance in the case of Public Procurement for Innovation (PPI) projects. As pointed out in Recital 73 of Directive 2014/24/EU, this is relevant to innovative projects involving "a greater amount of risk than reasonably bearable by a single contracting authority". In practice, demand aggregation involving two large cities can be used to leverage

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(8) With regard to cooperative and joint cross-border procurement, *see* in particular G.M. RACCA, *Joint Procurement Challenges in Future Implementation of the New Directives*, *op. cit.*, who well identifies the opportunities and challenges deriving from partnering in procurement both from a national and cross-border perspective.

(9) It is worth noting that procurement alliances have also been established by large multinational firms. For instance, several relevant cases operate in the telecommunications sector: BuyIn (Deutsche Telekom – France Telecom), Vodafone Procurement Alliance, and Telefonica Global Services. The main objectives of these alliances are: strengthening negotiating power; reducing costs; and changing supplier behaviour. Although private firms operate in a completely different environment and the cases cited here are not subject to public procurement rules, these objectives are not substantially different or in contradiction with those of most public buyers.

(10) BBG – SKI, Study commissioned by the European Commission, DG GROW, "Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States", Ref. No. 492/PP/GRO/IMA/15/15111e.

the development of new products or services (for instance, an innovative street lighting system which is more energy efficient).

- iii) JCBPP can stimulate cross-border bidding, *i.e.* contribute to the consolidation of the internal market from the supply side. It can be observed, in fact, that the larger volume resulting from combining two or more (originally) separate markets has the potential to attract foreign bidders and increase competition in general terms. For example, in the Brenner Base tunnel project, the cross-border nature of the project and its volume attracted more interested companies than initially expected by the contracting authority. Furthermore, an accurate tender strategy in JCPBB projects(11) can also push economic operators from the countries concerned to cooperate and bid together, which in some cases represents a novelty challenging traditional selling patterns.
- iv) JCBPP can be a driver for the improvement of national procurement practices. Improving knowledge about markets and procedures, and sharing best practices, are a significant value-add of JCBPP projects, as reported by the ‘Feasibility study’. In most of the cases analysed, the know-how gained by exchanging strategies and best practices was considered useful not only for possible future JCBPP projects, but also for national tenders. In some cases, this experience gained led to an improvement in contractual terms and conditions.
- v) JCBPP may potentially contribute to reducing the risk of corruption. In this respect, involving a larger number of parties in the procedure acts against possible malpractices by any of them.

### 3. Cooperative procurement

Another important novelty that has been introduced by the Directive concerns aggregated purchasing. The provisions of Directive 2014/24/EU introduce new provisions(12) defining centralised purchasing activities as those conducted on a permanent basis in one of the two following forms:

“(a) the acquisition of supplies and/or services intended for contracting authorities;

(b) the award of public contracts or the conclusion of framework agreements for works, supplies or services intended for contracting authorities”.

(11) *See* the BBG-SKI case, in which the buyer strategically decided not to divide the market into 2 separate geographical lots.

(12) *See* respect. Art. 2(1) (14), (15) and (16) of Dir. 2014/24/EU for the definitions of centralised purchasing activities, and ancillary purchasing activities and central purchasing body.

The same Article in the Directive on definitions also introduces that of ‘central purchasing body’ as a “contracting authority providing centralised purchasing activities and, possibly, ancillary purchasing activities” consisting in the provision of support to purchasing activities, such as technical infrastructure (typically IT) enabling contracting authorities to award public contracts or to conclude framework agreements; advice on public procurement procedures; and preparation and management of procurement procedures for the contracting authority concerned.

Recital 69 of the Directive clarifies the different functions carried out by these bodies. The first category corresponds to the role of wholesalers which stock and resell what is then procured for the contracting authorities. This role is rather peculiar and has significant implications for the organisation of the CPB itself. It is less often used in practice in Member States, as in the case of UGAP, the national French CPB with a large staff located all over France to ensure that what is procured is sold to the contracting authorities.

The second category of centralised purchasing corresponds to bodies acting as “intermediaries by awarding contracts, operating dynamic purchasing systems or concluding framework agreements to be used by contracting authorities”, as stated in Recital 69. In this context, the CPB might conduct “the relevant award procedures autonomously, without detailed instructions from the contracting authorities concerned”. In a few cases the CPB conducts “the relevant award procedures under the instructions of the contracting authorities concerned, on their behalf and for their account”, as they imply a full delegation of the purchasing role to the CPB.

The relevant provisions regulating the techniques for aggregated procurement are at Article 37 on central purchasing activities and central purchasing bodies. Those provisions are significant as they set out the key elements of the relations between CPBs and contracting authorities.

The first paragraph of this article leaves it to the discretion of Member States to define the type of CPBs which may be used by the contracting authorities, *i.e.* a wholesaler or a CPB acting as intermediary as defined at Article 2(1) referred to above. This is a significant since it allows for a defining of the conditions in which CPBs operate in the relevant Member State.

The second paragraph clarifies that the contracting authorities fulfil their obligations pursuant to this Directive when they acquire works, supplies or services by using contracts awarded by a CPB, typically a framework agreement. This same principle applies to both types of CPBs, wholesalers and intermediaries. In short, this is a sort of ‘safe harbour’ clause for the contracting authority, creating a significant incentive for contracting authorities to

delegate to a third party (*i.e.* the CPB) the burden and the risk of conducting public procurement procedures.

However, the contracting authority retains several responsibilities with regard to the parts or stages of a public procurement procedure it conducts itself, for example when awarding an individual contract under a Dynamic Purchasing System operated by a CPB, or when reopening competition under a framework agreement. In practice, as cooperative procurement necessarily involves more than one party in the procedures, it is necessary to clearly establish the responsibility of each specific party (the CPB and the individual contracting authority using one or more of the tools made available by the CPB to procure goods or services) in relation to the fulfilment of the obligation deriving from the Directive. As stated in recital 72, “where the central purchasing body has sole responsibility for the conduct of the procurement procedures, it should also be solely and directly responsible for the legality of the procedures”. This has significant implications in terms of liability and legal challenges in procurement procedures.

The third paragraph of Article 37 concerns the use of electronic procurement by CPBs. As pointed out in Recital 72, “Electronic means of communication are particularly well suited to supporting centralised purchasing practices and tools because of the possibility they offer to re-use and automatically process data and to minimise information and transaction costs”. Not by chance does the legislator include in the same chapter the rules concerning electronic techniques and those on aggregation. Some of these were already covered by the previous Directive (like those on e-auctions and framework agreements), while others, such as those on Dynamic Purchasing Systems (DPS, Art. 34) and e-catalogues (Art. 36), are also new and provide innovative tools for running procurement procedures. Consequently, an earlier deadline for the transition to e-procurement is set for CPBs (*i.e.* April 2017) which are supposed to be better equipped (in terms of IT infrastructure, staff, and resources in general) to cope with the digitisation of the process.

Finally, the Directive clarifies the regime for awarding a contract for the provision of centralised procurement activities to a CPB; in practice, the contracting authorities can award this type of public service contract without applying public procurement procedures, also with regard to the support activities referred to above (*i.e.* ancillary purchasing activities). However, contracts for the provision of ancillary purchasing activities are subject to provisions of the Directive when performed by other parties than a CPB.

### 3.1. CPBs and process innovation in public procurement

Several issues should be noted here, which highlight the innovative features introduced by the Directive in terms of process.

- The Directive acknowledges the importance of Central Purchasing Bodies (CPBs), and this requires defining their main role and the allocation of responsibility between them and the contracting authority.
- Such functions are to be carried out on an institutionalised and systematic basis, and therefore a distinction is made between cooperative procurement carried out by CPBs and occasional joint procurement.<sup>(13)</sup> In fact, CPBs are semi-permanent or institutionalised bodies.
- These norms clarify the legal framework regulating the activity of CPBs which have operated in the Member States for several years or decades (the oldest dates back to 1927, although there have been several subsequent phases in which Member States have decided to establish or merge existing bodies with different characteristics).<sup>(14)</sup>
- The provisions on CPBs themselves, combined with the new specific techniques on Dynamic Purchasing Systems and e-catalogues, and the clarifications to the provisions on framework contracts, bear the potential of increasing competition and streamlining the process for buyers and suppliers alike. The digitisation of public procurement is an essential element of the simplification of the process, as illustrated in section 1.
- CPBs can play many different parallel roles and have different functions: wholesaler, intermediary, expert centre, provider of IT infrastructure, buyer (on behalf of the individual contracting authorities) etc., “with or without remuneration”. The provision of IT infrastructure is typical of certain type of tools (e.g. e-catalogues). As a result, CPBs play a different role than merely aggregating demand, and operate in areas bordering private markets sheltered from competition, as we have seen earlier.
- CPBs are positively associated with the professionalization of public purchasing and procurement management, as explicitly stated in Recitals 59 and 69 of the Directive. Their staff includes experts specialised in relevant product markets. They are regularly trained and subject to internal rules aiming at preventing malpractices.

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(13) Occasional joint procurement is addressed in Art. 38 of the Directive which is intended to be less institutionalised and less systematic, as stated in Recital 71.

(14) The original bodies which more recently led to the creation of CPBs date back to the end of the 1960s. A first wave of CPBs was created around the year 2000 (in Italy, Austria, Belgium and Finland). A second phase took place starting from 2007-2010 and ran until 2014 (Portugal, Sweden, Slovenia, Croatia and Bulgaria).

### 3.2. Current state of play

As we saw in the previous section, the legislation leaves to the discretion of Member States the definition of CPBs' scope (national, regional, sectoral etc.), markets in which they operate, organization,<sup>(15)</sup> financing, set up etc. Their legal status varies significantly across the EU, ranging from internal departments of ministries (e.g. Croatia, Slovenia, Spain), to State agencies (as in Austria, Germany and Italy); the variety of cases is too broad to include profit-making bodies distributing dividends to their members. The latter case raises interesting questions as to possible interest from large private players in offering competing services as a result of the digitisation of procedures. At least one CPB operates in almost all Member States at the national level; the exceptions are Luxembourg, Netherlands, Romania, the Czech Republic, and Slovakia, where there are no CPBs procuring for the central administrations.

CPBs most often establish framework agreements for standardised goods and services. Those operating for the central administration at the national level typically operate in office equipment and furniture, telecommunications services, energy, cleaning services, facility management etc. Some cover more advanced types of services, including architectural and engineering consultancy, audit services, or purchase sophisticated goods such as helicopters. Health procurement, which represents a large share of public procurement expenditure, is often managed by sectoral CPBs.

According to a recent study, based on data extracted from TED, centralized purchasing constitutes nearly 20% of the total value of contracts awarded in the EU over the last few years (corresponding to only 4% of contracts awarded in number).<sup>(16)</sup> This data is influenced by the UK (55%) where the largest CPBs in the EU operate; this value is not representative of the situation in most EU countries – in half of the Member States, the level of aggregation is estimated at no higher than 10% of total public procurement value. According to the same source, there are about 50 CPBs which award more than 15 contracts each year, with 200 CPBs awarding between 5 and 15 contracts annually.

Unfortunately, it is difficult to quantify the impact of CPBs and centralised procurement with exact precision, due to the lack of precise micro data identifying all CPBs. Such difficulty is coupled with the lack of accurate data

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(15) CPB organisational models are extremely diverse: for example, the Swedish central purchasing system consists of a set of specialised CPBs, all of which are organised as divisions within government agencies; in most other countries, the CPB is a single and independent government agency. UGAP, the French CPB, is *de facto* a large wholesaler buying goods and reselling them to the individual contracting authorities.

(16) PWC, ICF GHK and ECORYS (Study commissioned by the EU Commission, DG MARKT), "SMEs' access to public procurement markets and aggregation of demand in the EU", 2014.

on the total value of public procurement (including above and below the EU thresholds) in many countries.

Table 1 below illustrates the place of national CPBs in the total value of public procurement, as extracted from TED. It does not include procurement of utilities and in defence and works, since national CPBs generally do not operate in these markets. It covers the main CPBs operating at the national level only in the EU and therefore procuring a range of goods and services mainly for the central administration bodies (ministries, State agencies etc.).(17) The data relating to the CPB volume cover the total of their activities; it may include procurement below the EU thresholds(18) as well as other ancillary services supporting individual buyers.(19) Therefore, the data on the share of CPB are only indicative and tend to overestimate the level of public procurement conducted via such bodies.(20)

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(17) In some cases, however, many buyers subscribe to the framework agreements of the CPB from other parts of the public administration and end up being a large share of the CPB volume.

(18) For example, this is the case of Consip, which operates a large electronic marketplace MEPA for below-threshold procurement. The value of purchases through Consip's framework agreements in 2014 reached 3.457 million euro.

(19) The data on CPB volume are extracted from public sources and refer to the years between 2012-2016, available online.

(20) Another significant element leading to overestimation is the fact that in some Member States TED data do not capture all the procedures above the EU thresholds taking place at the national level.

(21) These data refer to the volume of public procurement called off via the framework agreements set out by the CPB and other contracts. The data do not refer to the value of the framework contracts, but rather to the amount actually procured by the contracting authorities. This also includes projects in which the acquisition is carried out by the CPB.

(22) DG GROW G4, "Public Procurement Indicators 2014", 2 February 2016; DG GROW G4, "Public Procurement Indicators 2015", 19 December 2016

(23) EU Comm., Commission Staff Working Document, "Annual Public Procurement Implementation Review 2013", SWD (2014) 262 final, 1 August 2014.

*Table 1. CPB procurement volume, share in the relevant procurement markets, and number of contracting authorities in a number of Member States*

Member State	CPB	CPB procurement volume(22) (million euro)	Value of public procurement above EU thresholds(23) (million euro)	CPBs' share of procurement above EU thresholds (%)	Number of contracting authorities(24)
Austria (2015)	BBG	1.400	3.220	43,5	5.600
Croatia (2015)	State office for Central Public Procurement	83	1.660	5,0	1.811
Finland (2015)	Hansel	932	4.930	18,9	540
France (2015)	Ugap	2.714	32.730	8,3	132.652
Germany (2015)	Beescha	1.100	15.930	6,9	30.000
Ireland (2014)	OGP	357	1.800	19,8	3.319
Italy (2014)	Consip	5.600	20.690	27,1	34.000
Lithuania (2012)	CPO	69	850	8,1	7.703
Portugal (2014)	ESPap	538	1.030	52,3	4.467
Spain (2015)	DGRCC	740	11.420	6,5	8.339
Sweden (2016)	National Procurement Service	1.400	9.960	14,1	3.900
UK (2015)	CCS	18.053	66.070	27,3	30.000

The share of public procurement is influenced by various factors, such as the mandate and scope of the sector in which they operate or the existence of one or more CPBs operating at the national level (for instance, in Germany four CPBs operate at the federal level, each covering different areas). The institutional setup of the Member States has a significant impact on the devolution of public

procurement to the different levels of government. Bodies that have been in operation for a longer period of time also seem to record a higher share of the total amount of public procurement above the EU thresholds; in the case of Consip, the data are largely affected by the significant volume of procurement below EU thresholds, which inflates the numerator of the ratio. As a result of these many differences, the resulting share is not meaningful in terms of comparison between them.

Overall, at the EU level, it is estimated that the volume of procurement purchased by national CPBs is around 35 billion euros, *i.e.* approximately 18% of the total value of public procurement above the EU thresholds in the sectors in which those bodies operate; this value is largely concentrated in the activity of the British CPB, the Crown Commercial Service, which makes up almost half of the total.

As can be seen from the table above, in some Member States CPB weight is relevant both in absolute and relative terms and in many cases further aggregation is conducted at the regional or sectoral level. In the next section, we will consider some aspects of the systemic relevance of CPBs. This should however not lead us to forget the importance of how CPBs design their calls<sup>(24)</sup> (mostly framework agreements) and the characteristics of their IT platforms, the measures necessary to ensure that markets remain competitive and open, how to prevent possible malpractices by such pivotal bodies, or how to ensure access to SMEs.

### 3.3. The systemic relevance of CPBs

Centralised procurement is a process wherein one administrative organisation, representing the collective needs of other departments, carries out procurement functions. In most Member States, public procurement is mainly conducted on a highly decentralised basis (*i.e.* at the level of individual spending ministries, local authorities, or other public bodies) by hundreds or sometimes thousands of procuring entities/bodies.

Therefore, the Public Procurement landscape is characterised by high dispersion in all its key dimensions, *i.e.* the number of contracting authorities (estimated at least 350,000 across the EU<sup>(25)</sup>), the amount of tenders above the EU tenders published annually (close to 170,000 in 2015

(24) G.L. ALBANO and C. NICHOLAS, *The Law and Economics of Framework Agreements – Designing Flexible Solutions for Public Procurement*, Cambridge, CUP, 2016; G.L. ALBANO and M. SPARRO, “Flexible Strategies for Centralized Public Procurement”, *Rev. Econ. & Instit.*, 2010, 1(2), Art. 4.

(25) However, this number is only to provide an approximate estimation; there is not a standard way to count a contracting authority; each internal division of the same body (e.g. a Ministry) could be counted individually or the Ministry as one single contracting authority. The difference of scale between the number of contracting authorities in Germany and France (four times the German number) suggests that Member States used a different metric to define contracting authority.

– procurement by utilities and in the defence sector included(26)) and many economic operators which actively participate or could participate in public procurement.

Such fragmentation is highly inefficient:(27) i) it leads to potentially higher prices; ii) the launch and management of a procurement procedure implies significant process costs;(28) iii) small buyers often lack the administrative capacity to deal with complicated cases; in short, professional buyers are also needed to deal with big players; iv) fragmentation deters the rollout of standards in areas like IT, and can be an obstacle to interoperability of solutions in use by different departments of public administration.

Driven by the need for further control over public spending, several Member States have set up CPBs to achieve savings through economies of scale and reduce transaction costs.(29) This is of increasing importance in the context of the severe budgetary constraints experienced by many EU countries.

At the same time, public procurement is increasingly seen as a tool to carry out a wide range of political and economic priorities. In addition to the need to create savings, procure and manage contracts efficiently, procurement handles a number of sensitive, often conflicting policy objectives. The combination of growing demands on the public authorities generates a need to specialise and increasingly professionalise procurement bodies.(30) Most buyers, in particular

(26) If below-threshold procurement is included, the number of procedures run annually escalates significantly. In Italy alone, about 5m procedures are run annually including above- and below-threshold for goods and services alone.

(27) C. COTTARELLI, *La lista della spesa. La verità sulla spesa pubblica italiana e su come si può tagliare*, Milan, Feltrinelli, 2015.

(28) As reported in the study from PWC *et al.*, centralized purchasing requires 30 person-days on average, more than the average for a non centralised procurement (22 person-days). However, when disaggregating the results by the number of individual buyers the contract involves, the average staff time per buyer decreases as the number of buyers involved increases. Therefore, centralized purchasing has significant cost saving. EsPap, the Portuguese CPB estimates that process savings deriving from aggregation count for 8.6% of total savings.

(29) SIGMA, “Organising Central Public Procurement Functions”, Brief 26, Public Procurement, 2013; SIGMA Papers No. 47; OECD, “Centralised Purchasing Systems in the European Union”, 24 April 2011, p. 58; P. HOPKINS, *Building the case for centralisation in public procurement*, CIPSA Australia, 2006; OECD, “Becoming a Central Purchasing Body: communication and change management strategies for an effective implementation. The case of the Greek secretariat General of Commerce (SGC) at the Ministry of Economic Development”, Meeting of the Working Party of the Leading Practitioners on Public Procurement (LPP), Paris, 27-28 April 2015; G.M. RACCA, *Professional buying organisations, sustainability and competition in public procurement performance*, 4th International Public Procurement Conference (IPPC 2010), Seoul, 2010; N. DIMITRI, F. DINI and G. PIGA, “When should procurement be centralised?”, in *Handbook of Public Procurement* (N. DIMITRI, G. PIGA and G. SPAGNOLO eds), Cambridge, CUP, 2006. K. KARJALAINEN, “Estimating the cost effects of purchasing centralisation – Empirical evidence from framework agreements in the public sector”, *J. Purchasing & Supply Management*, 2011, Vol. 17, Iss. 2, pp. 87-97.

(30) OECD, Recommendation of the Council on Public Procurement, Directorate for Public Governance and Territorial Development, 2015. See in particular Recommendation V.

the smaller ones, may lack the necessary capacity and competence to manage these new requirements.

Because of their size, their expertise and their specific role in the public procurement landscape, CPBs can play a significant role in the implementation of policy. Issues such as the professionalization of public buyers, rationalisation of the public procurement system,(31) digitisation or the implementation of strategic procurement can hardly be addressed without involving CPBs.

This is neatly pinned down by the OECD. According to the OECD, “CPBs are increasingly becoming the core knowledge hubs in the country’s public procurement frameworks, not only for consolidated procurement but also for the implementation of e-Procurement, the dissemination of capacity and monitoring of the performance of procurement systems”.(32) CPBs therefore contribute to overcoming fragmentation and lack of any coordination between public buyers, improving the governance of public procurement. Experience has shown that policy coordination in public procurement is weak in many Member States. One emerging trend observed in some cases (e.g. the UK and Ireland) is to integrate procurement policy, advice, and operations – including the CPBs’ buying function – into a single organisation. This development is aimed at strengthening spend analytics, monitoring procurement and generating further savings.

In some countries, CPBs manage an ever-increasing share of public procurement and this has also some downsides. In fact, aggregation of procurement also carries a number of potential risks,(33) such as potentially reduced access for SMEs due to larger contracts, centralisation in procurement decision making, and excessive standardisation. These aspects are to be carefully monitored by the State.

Finally, there is another advantage to CPBs. They work independently of the electoral process, as their decisions do not depend on the mood of the electorate. This is not the case for many individual buyers whose decisions take into account the timing of the next elections (which represents the pay-back period for patronage).

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(31) G.M. RACCA, “Le prospettive dell’aggregazione nell’amministrazione dei contratti pubblici”, *ApertaContrada*, 2014. G.M. RACCA and G.L. ALBANO “Collaborative Public Procurement and Supply Chain; the European Union Experience”, in *The SAGE handbook of strategic supply management* (C. HARLAND, G. NASSIMBENI and E. SCHNELLER eds), Los Angeles, SAGE, 2013.

(32) OECD, “Working Party of the Leading Practitioners on Public Procurement”, Paris, 27-28 April 2015.

(33) G.L. ALBANO and M. SPARRO, “Flexible Strategies for Centralized Public Procurement”, *op. cit.*, p. 53.

### 3.4. The Commission's policy on cooperative procurement

The European Commission services have drafted an Action Plan on cooperative procurement aiming to capture the innovative effects of smart aggregation of public buyers' purchasing power. The main objectives are to maximise the benefits of cooperative procurement by addressing systemic weaknesses, stimulating growth by advancing innovation-oriented practices (including linking innovative SMEs and startups with large buyers), supporting SMEs' access to public procurement through cooperative procurement, and supporting JCBPP.

The actions fit in with the overall objectives of the Commission: achieving best value for money for buyers, greater opportunities for business and SMEs and modernising public administration. The rationale behind this development is the aim of creating more efficient, simple and cost-effective procurement processes, but also addressing potential risks which may derive from the poor implementation of aggregation practices.

## 4. *The digitisation of public procurement*

### 4.1. The phases of the transition to e-procurement

The first significant process innovation introduced by the new public procurement Directives is the transition to e-procurement. The Directives provide for a gradual, mandatory transition to e-procurement in terms of the phases and actors involved, rolling in over time.<sup>(34)</sup>

The impact of this transition will be significant, and, if properly managed, may largely contribute to improving and simplifying the process, re-designing it, and increasing the efficiency and transparency of public procurement. In its Communication on end-to-end e-procurement of 2013, the European Commission stated that "the transition to end-to-end e-procurement can generate significant savings, facilitate structural re-thinking of certain areas of public administration, and constitutes a growth enabler by opening up the Internal Market and by fostering innovation and simplification. It can also facilitate SME participation in public procurement by reducing administrative burden, by increasing transparency over business opportunities, and by lowering participation costs".<sup>(35)</sup>

The initial phases concerned by the transition to e-procurement (*see figure 1*) are as follows:

(34) EU Comm., "A strategy for e-procurement", 20 April 2012, COM (2012) 179 final, 2012.

(35) EU Comm., "End-to-end e-procurement to modernise public administration", 26 June 2013, COM (2013) 453 final, 2013.

- ‘e-notification’ (meaning the electronic transmission of notices<sup>(36)</sup>) as provided by Article 51(2) of Directive 2014/24/EU. Notices should be drawn up and transmitted by electronic means to the Publications Office of the EU for publication in the EU portal Tenders Economic Daily<sup>(37)</sup> (TED). They should be published within 5 days after they are sent;
- ‘e-access’ concerns the electronic availability of procurement documents. The documents should be available in an unrestricted manner and with full direct access free of charge, as set out in Article 53.

The deadline for the completion of these two phases was 18 April 2016, in accordance with the guidance set out in Article 90(1) on transitional measures.

The next phase concerns the electronic submission of tenders (e-submission), including the electronic transmission of requests for participation. The Directive provides for a gradual introduction over time to the bodies involved. The obligation is imposed as a first step to Central Purchasing Bodies (CPBs). According to Article 90(2), Member States can postpone its implementation until 18 April 2017. As pointed out in Recital 72, e-submission is well suited to use by CPBs, whose purchasing practices and tools are, generally speaking, more advanced in implementing e-procurement than traditional contracting authorities. The obligation to use e-submission is then extended to all contracting authorities. According to the transitory provisions, Member States may postpone the obligation to submit tenders online until 18 October 2018. If they decide to do so, bidding would take place by post, fax, electronically or by any of these means combined.

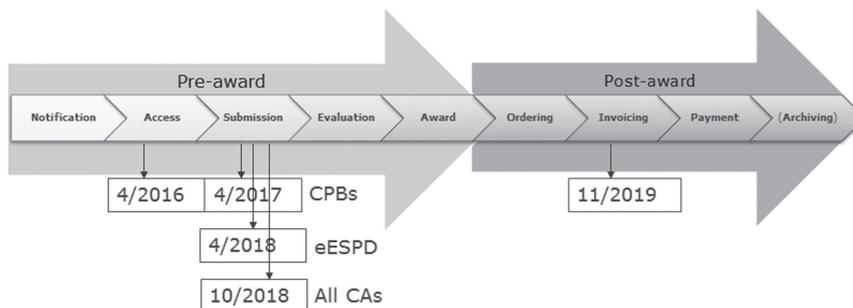
As pointed out in Recital 52, the mandatory use of electronic means of communications does not include the electronic processing of tenders, electronic evaluation or automatic processing. Furthermore, pursuant to this Directive, the provisions of the Directive relating to e-procurement and the obligation to use electronic means of communication cover only the pre-award process: this means, in practice, that the obligation to use electronic means of communication does not refer to any elements of the public procurement process after the award of the contract. Moreover, the internal communications within the contracting authority are, quite reasonably, also outside the scope of the Directive.

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(36) This applies to the prior information notice, the contract notice and the contract award notices provided respectively by Art. 48, 49 and 50 of the Directive.

(37) TED is the online version of the *Supplement to the Official Journal* of the EU, dedicated to European public procurement. It is the EU portal for publication of procedures above the EU thresholds.

*Figure 1 – EU directives milestones and the process life cycle*



To ensure that e-procurement is not used as a means to restrict access to procurement markets, Article 22(1) provides that the tools and devices to be used, as well as their technical characteristics, are non-discriminatory, generally available and interoperable with the ICT products in general use.

In broad terms, similar provisions are included in Utilities Directive 2014/25/EU. Under the Concessions Directive 2014/23/EU, e-submission is voluntary. Under the terms of the Concessions Directive (Art. 29(1)), communication between bidders and the contracting authorities would take place using traditional means such as post, fax and hand delivery. It is left to the discretion of Member States to make e-procurement mandatory. In general terms, the provisions relating to electronic communication are very few and the legislator drafted only a 'light regime' in this area. The provisions (at Art. 29(2)) refer to the general principles, such as openness, general availability and non-discrimination of the systems used, in addition to the preserving the integrity and confidentiality of the communications between the relevant parties.

#### 4.2. Exceptions to the use of electronic communications

In certain cases, the Directive allows the contracting authorities to avoid requiring the use of e-submission. These cases are contemplated in the following six exceptions.

- i) When the use of electronic means requires specialised tools, devices or file formats that are not generally available or supported by generally available applications.
- ii) Regarding IP-related issues, where making the applications or the software available for download would entail a breach of the copyright related to the software by the contracting authority. The relevant provisions illustrate the case explaining that the applications suitable for

the description of the tenders use file formats that cannot be handled by open or generally available applications or are under a proprietary licensing scheme.

- iii) Electronic communications could only be handled using specialised office equipment, such as wide-format printers used in certain works/architectural projects.(38)
- iv) The submission of a physical or scale model which obviously cannot take place electronically. In such a case, the scale model would have to be submitted by post or using other carriers.(39)
- v) When not using such means of communication is necessary in order to protect the particularly sensitive nature of the information.(40) However, to meet the confidentiality requirement, the buyer may use specific or dedicated electronic tools (not generally available to users) allowing the necessary level of protection; in such a case the procedure could still be run electronically.(41)
- vi) Due to a breach in the system in the e-procurement system, as it would put the regularity of the procedure at serious risk.

The first three exceptions are related to technical issues, while the last two concern security issues.

Furthermore, to ensure the openness of the tender, the contracting authorities have to offer alternative means of access in case it is not possible to use electronic means which are not generally available. For instance, a provisional token or password is to be provided to the supplier. While derogating to the use of electronic procurement may be justified in specific cases, in general terms this is not problematic if the contracting authorities avail themselves of the services of an e-procurement services provider. Ugap, the French national CPB, has conducted its procurement procedures solely electronically since 2014 without having to resort to exceptions.

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(38) It would not be proportionate to require the contracting authority to buy a specific printer to be used in only one tender.

(39) This exception would apply to the transmission of the scale model itself, while the rest of the procedure is to be conducted electronically.

(40) The case of sensitive information could apply, for instance, to the contract to the advisor for the privatisation of a company. Such information could affect the market value of the company on the stock market.

(41) For instance, this would be the case where the contracting authority requires the use of a dedicated secure means of communication such as dedicated leased lines not connected to the public telecommunications network.

### 4.3. The procurement of works and e-procurement

Although the provisions of the Directives apply neutrally to all types of procurement (goods, supply or services), in practice, a number of provisions would concern works, or architectural projects, almost exclusively. For instance, this is the case of some of the exceptions outlined above, such the submission of a physical or scale model, and that relating to the use of special equipment (respectively points iii) and iv) in the list in the previous section).

Another issue relating to work projects<sup>(42)</sup> is mentioned in Recital 53. This concerns the possibility for buyers to set out the maximum size of file formats to be submitted. Works project files are often large; setting out a maximum volume is justified by the fact that the larger the size, the greater the risks of delays or cuts during upload; moreover, bigger files occupy greater storage space.<sup>(43)</sup>

Furthermore, Article 22(5) provides that Member States may require the use of specific electronic tools, such as building information electronic modelling (BIM) tools or similar, for work projects or design contests. As the use of such tools is not generally widespread in all Member States, if BIMs are used the contracting authorities should offer alternative means of access to suppliers in order not to restrict their opportunity to access the procedure.

### 4.4. Interoperability of digital solutions across the Single Market and adjustments to technological development

Article 22(7) empowers the Commission to adopt delegated acts in three specific cases, essentially to cater for technological developments (in the first two cases) and to address technological obstacles to the internal market (the last case, covering interoperability).

The first case allows the Commission to amend the technical details and characteristics set out in Annex IV to take account of technical developments. Annex IV is important as it sets the requirements for tools and devices for the receipt of tenders, requests for participation and plans and projects in design contests conducted in an electronic environment. These requirements tie in with many significant issues which – if improperly managed – may affect the impartiality of

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(42) Obviously, this could also be applied to other types of procurement; however, experience shows that it would be more likely to occur with works.

(43) See K. Schwaub, “The Fourth Industrial Revolution”, World Economic Forum, 2016. The cost of storing information electronically is approaching zero (1 GB costs on average less than USD0.03 a year). Moreover, the space occupied by the relevant IT equipment (servers, PCs, etc.) is a fraction of the space occupied by storage for the paper versions of the same documents, as illustrated by a number of contracting authorities which have already completed the transition to e-procurement. It is therefore assumed that the buyer would store the files in electronic format, applying ‘end-to-end e-procurement’.

the procedure, such as the timing for the receipt of tenders, access by authorised persons to the tenders, opening tenders, and traceability of any possible breach of such elements. Traceability represents one significant advantage of electronic procedures compared to paper, since a record of the activity would be available to courts to verify specific situations in case of legal challenges.

The second possibility allows the Commission to amend the first four exceptions and to adjust them in case technological developments render the use of such exceptions inappropriate or, exceptionally, where new exceptions are to be added due to further technological developments.

The last case allows the Commission to set mandatory technical standards to ensure interoperability in a cross-border context. The use of specific standards may be imposed in certain areas such as e-submission, e-catalogues and means for electronic authentication. The threshold for applying this power is rather high. In fact, this would be possible only where technical standards have been thoroughly tested and have proved their usefulness in practice for both buyers and suppliers; stakeholders should be consulted on these points. Before making the use of any technical standard mandatory, the Commission is also asked to carefully consider the costs that this may entail, in particular in terms of adaptations to existing e-procurement solutions, including infrastructure, processes and software. These requirements make the use of such powers rather difficult.

Almost in parallel to the publication of the regulatory framework for public procurement, EU Member States and the European Commission decided to introduce a European Standard for e-invoicing<sup>(44)</sup> to address interoperability issues regarding e-invoices received by buyers, issued as a result of the performance of public procurement contracts.<sup>(45)</sup> This initiative was taken in response to the many e-invoice formats used or being developed across the EU, leading to increasing costs for public buyers and suppliers wishing to carry out cross-border activities. These varied formats cause unnecessary complexity and high costs for businesses and public entities. As a result of the Directive, buyers will have to accept e-invoices that comply with a forthcoming European norm to be developed by the European Committee for Standardisation (CEN), although nationally specific rules will remain valid. In addition, this Directive provides for a gradual transition to allow buyers to prepare for the change. The implementation deadline is set in relation to the publication of the reference of the European standard in the *OJEU* (*i.e.* 18 months afterwards). In order to facilitate the take-up of e-invoicing for local and regional contracting authorities, Member States may postpone the application of this

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(44) Dir. 2014/55/EU of 16 April 2016 on electronic invoicing in public procurement.

(45) The scope of application includes contracts under the classical Directive, the Utilities Directive 2014/25/EU, the Concessions Directive 2014/23/EU, and the Defence Directive 2009/81/EU.

Directive to sub-central contracting authorities and contracting entities for up to 30 months following the publication of the reference indicated above. In practice, this brings the effective implementation of seamless e-invoicing communication across the EU to the end of 2019 or beginning of 2020.

#### 4.5. Security levels and electronic signature

Some considerations are to be made in relation to the use of electronic signatures.<sup>(46)</sup> The Directive assigns Member States the power to specify the level of security required in relation to the use of electronic communications in the various stages of the procurement procedure. Interestingly, the legislator provided that Member States should assess the proportionality between the level of security and the risks attached, which suggests that certain tools may not always be necessary.

Thus, the level of security may change depending on the phase of the procedure and the associated needs. A higher level of security may be required in relation to e-submission, since it is necessary to preserve the integrity of the document or to identify the sender with no ambiguity. On the contrary, a lower level of security would be needed regarding the request for confirmation of the address at which an information meeting is to be held and access to procurement documents, in relation to the resubmission of e-catalogues. In practice, this means that the use of electronic signatures can be considered unnecessary in the cases above, requiring a low level of security.

It is worth pointing out that Member States tend to assess the level of security necessary to the (e-) signature of bids differently. For instance, in Ireland, Finland, Sweden and the UK, bids are not required to be (electronically) signed, while this requirement is in place in other Member States such as France, Greece, Italy and Portugal. It is worth highlighting that in some Member States the requirement of signing bids electronically has been or is being reconsidered with a view to simplifying the procedures for economic operators. As pointed out in the EXEP paper on “Regulatory Aspects and Interpretation”,<sup>(47)</sup> the problem may lie with the use of e-signature for economic operators and in the validation of e-signatures for contracting authorities.

In short, there is no legal requirement stemming from the Directive requiring the use of e-signatures. In this respect, the provisions on the use of advanced electronic signature lay down conditions when such requirement

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(46) eIDAS Regulation (EU) No. 910/2014 of 23 July 2014 on electronic identification and trust services for electronic transactions in the internal market and repealing Directive 1999/93/EC, *OJEU*, L 257 of 28 August 2014, sets out the framework for eID and trust services, including e-signatures, e-seals and electronic time stamps.

(47) EXEP – Multistakeholders Expert Group on electronic procurement – Subgroup report, *Governance and Capacity building – Effective transition to e-procurement. Useful tips*, October 2016.

must be accepted in a cross-border context. The Directive states that buyers should accept advanced electronic signatures supported by a qualified certificate, irrespective of the Member State in which the service provider issuing the qualified certificate and/or the signatory is established, as long as the electronic signature is supported by a certificate issued by a service provider on a trusted list provided by the Commission Decision 2009/767/EC(48) as amended.

#### 4.6. E-procurement:

##### A tool to re-engineer the public procurement process

As stated above, the introduction of ICT is an opportunity to overhaul public procurement processes, in addition to improving efficiency, transparency and traceability and reducing the administrative burden on buyers and suppliers.(49)

As indicated in the EXEP paper on governance and capacity building, “changing from old processes (for example, paper based) in public procurement to digital solutions is much more than an ICT usage matter. It is a matter of reorganizing functions and rethinking ways of carrying out the same activities”.(50)

The shift to e-procurement therefore represents a unique window of opportunity to review process and organisation in public procurement for the following reasons:

- it enables the automation of certain phases of the procedure;
- it enables conducting the procedure remotely (this applies both to the buyer, but especially to the bidder);
- it supports rapid and paperless transactions;
- it increases transparency and traceability of the process;
- it facilitates the modernization of procurement workflow;
- it promotes the use of structured data;
- it enables access to the data in real time.

One example is the creation of a single national portal for the publication of all notices and awarded contracts. Gathering all this information in one place enhances transparency and greatly simplifies economic operators’ access

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(48) EU Comm. Decision of 16 October 2009 “setting out measures facilitating the use of procedures by electronic means through the ‘points of single contact’ under Directive 2006/123/EC of the European Parliament and of the Council on services in the internal market”, *OJEU*, L 299/18 of 14 November 2009.

(49) Moreover, the digitisation of public procurement can also generate significant spillover effects in other areas of public administration. In fact, the digitisation and automation of verification of compliance (e.g. absence of conviction or company data on turnover) are used in other administrative procedures requiring an authorisation from the State – this is for example the case of business mobility.

(50) As explained in the same paper, the governance of digital transformation is key to successful implementation.

to information about procurement markets. Furthermore, interoperability between the portal, TED and the national *Official Journal* allows contracting authorities to enter the data on the procedure only once. This enables states to save time and money, as well as ensuring the reliability of the data generated by different IT systems.

Another example is information exchange. During the tender, it may be necessary to update the tender documents or reply to questions from economic operators. Updates and questions and answers can be posted on the e-procurement platform. The replies and new information will be automatically sent to the economic operators which have expressed an interest in the procedure. This will ensure that all bidders have access to the same information. Moreover, an electronic audit trail can be generated, to help ensure transparency in the procurement process.

Another case concerns the qualification process. Information that is presented in a structured format allows an automated or semi-automated evaluation of bidders' compliance with exclusion or selection criteria. This saves a significant amount of time, reduces typographical errors and cuts out the discretionality of the buyers in the process. As we will see in the next section, the ESPD is the essential element to ensure the implementation of automation in the qualification process.

Finally, the overall objective of digitisation is to achieve 'end-to-end' e-procurement, starting from planning and preparation up until archiving. Achieving such an ambitious objective requires a comprehensive approach, which implies the interconnection of various IT systems composing the 'e-procurement ecosystem,' such as databases of certificates, pre-qualification services, e-procurement services, the portal(s) for the publication of the calls, etc. Therefore, the digitisation should go far beyond the phases of public procurement covered by the Directives and include post award phases such as e-invoicing, e-payment etc. Establishing such a seamless exchange of data is a multidisciplinary challenge. Technical aspects of legal frameworks, and operational issues, must be coordinated to ensure that all systems involved are able to process and reuse the relevant data.

## ***5. The European Single Procurement Document (ESPD)***

An important process innovation introduced by the new Directives on public procurement is the European Single Procurement Document (ESPD), a self-declaration to be regarded as preliminary evidence in replacement of certificates.

The main elements of the ESPD are defined in Article 59 of Directive 2014/24/EU. It was established by the Commission's implementing Regulation 2016/5 (2016) in January 2016<sup>(51)</sup> (hereafter referred as 'the Regulation') which entered into force on 26 January 2016. The entry into force of the ESPD is linked to the transposition of Directive 2014/24/EU into national legislation and, as stated in Article 1 of the Regulation, must take place at the latest by 18 April 2016.

Alongside the classical procurement sectors, the ESPD is to be used by contracting entities subject to Directive 2014/25/EU when applying exclusion and selection criteria provided by Directive 2014/24/EU. With regard to concessions on procedures and procurement whose value is below the EU thresholds, the use of the ESPD is left to the discretion of Member States.

The objective of the ESPD is to reduce the administrative burden on economic operators "deriving from the need to produce a substantial number of certificates or other documents related to exclusion<sup>(52)</sup> and selection criteria".<sup>(53)</sup> Therefore, the ESPD was introduced with the aim of simplifying procedures for both buyers and suppliers and reducing the administrative burden.

In short, the ESPD is a self-declaration of companies' suitability, financial status and abilities, used as preliminary evidence in all public procurement procedures above the EU thresholds. A few general aspects of the ESPD are as follows.

- The ESPD enables participating companies or other economic operators to state that they are not in one of the situations in which they must be excluded or may be excluded from the procedure.
- Only the winner will have to submit certificates or other means of proof requested as evidence by the buyer and this cuts the volume of documents needed in the procedure.
- While self-declaration is deemed to be sufficient a priori, the buyer can request some (or all) of the documents in cases of doubt when selecting candidates, especially in the case of two-stage procedures; this is to avoid contracting authorities inviting candidates which later prove unable to submit their supporting documents at the award stage, depriving otherwise qualified candidates from participation.
- Technical specifications are not part of the ESPD; it covers only the conditions for participation (pre-qualification) in terms of exclusion and selection criteria.

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(51) Commission Implementing Regulation (EU) 2016/7 of 5 January 2016 establishing the standard form for the European Single Procurement Document, *OJEU*, L3 of 6 January 2006.

(52) Examples of exclusion criteria are criminal convictions, grave professional misconduct, etc. Examples of selection criteria are financial, economic and technical capacity.

(53) See Recital 84 of the Directive 2014/24/EU and Recital 1 of the Regulation.

- It can be used for both one- and two-stage procedures (restricted procedures, competitive procedures with negotiation, competitive dialogues and innovation partnerships).
- Bidders can be excluded if the ESPD is not properly filled in, as for any other formal requirement. Buyers may however provide an opportunity to correct minor issues.
- The ESPD is also to be provided by subcontractors so that the verification of the information regarding such entities can be carried out together with and in the same conditions as the verification of the main economic operator.
- The ESPD can be reused in different procedures, in particular in digital format, or updated.

This possibility is linked to the availability of the ESPD in electronic format. The design of the ESPD (structured information) allows automatic processing. Under the Directive, the shift to an entirely electronic solution can be postponed until 18 April 2018.

### 5.1. The ESPD and the “winner only” principle

The use of the ESPD is to be viewed together with the ‘winner only’ principle, whereby the relevant supporting documents (certificates, attestations, declarations on oath etc.) should be requested from the potential winner of the procedure only, *i.e.* the tenderer to which the contracting authority has decided to award the contract. This represents a significant simplification of the process for all parties involved. Indeed, self-declaration was already in use in some Member States (for instance, in the Netherlands, Germany and Spain) while in many others it was a novelty. The objective of the ESPD is to replace the diverging self-declarations in use across the EU, and to introduce it as a common procedure across the EU, which in some cases is a radical shift away from the way the procurement process has been organised heretofore.

This represents a significant change and a potential relief for most suppliers, who will now be able to submit only the offer, without having to take care of looking for and collecting the relevant certificates demonstrating that they meet the relevant exclusion and selection criteria set by the contracting authority. This means process savings for the economic operators, allowing them to focus on the preparation of the technical and financial aspects of the offer. The process simplification is also relevant for the buyers, as they may verify the conformity of the evidence provided by only one operator – the potential winner – instead of all the bidders.

## 5.2. The ESPD and the Single Market dimension

From the perspective of consolidating the internal market, the ESPD represents a significant innovation with the potential of increasing cross-border participation in public procurement procedures. From this perspective, the main innovative aspects of the ESPD are the following:

- It clarifies – by ‘standardising’ them – the exclusion and selection criteria to be used by all buyers across the EU, in an almost exhaustive manner (some national criteria are still allowed.<sup>(54)</sup> This point also has a relevant national dimension, since in many cases different contracting authorities in the same Member State were previously applying non-homogeneous criteria although operating under the same national legislation.
- The ESPD simplifies procedure for both buyers and bidders, as it replaces different and diverging self-declarations with one standard form established at the European level, available in all official EU languages.
- The establishment of a standard self-declaration contributes to increasing legal certainty in the procedure. This is quite relevant since it increases bidders’ confidence on some aspects of the applicable public procurement rule, and may potentially increase business interest in public procurement.
- The ESPD allows for making the ‘winners only principle’ the standard principle to be used in procurement procedures across the EU. This greatly simplifies matters for bidders and public administrations alike taking part in procurement procedures in all the EU.
- The ESPD – being thought to be available in electronic format – allows the presentation of the information requested in structured format, paving the way for automatic verification of data (and paving the way for the so-called ‘once-only’ principle). In this respect, it provides a strong push for the digitisation of public procurement procedures.

As a complement to the creation of the ESPD, the new Directives in Article 61 establish eCertis, an online database enabling mapping the means of proof (certificates, declarations on oath etc.) issued in any EU Member State, to demonstrate compliance with exclusion or selection criteria.<sup>(55)</sup> The Directive requires Member States to keep the information included in eCertis up to date. It is important to stress that eCertis is not only a tool simplifying procedural aspects but it also has multiple functions: as a clearing house, it allows checking the reliability of certificates and attestations provided; it is

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(54) See Part III D of the Regulation which allows the contracting authority (or the contracting entity) to include other exclusion grounds that may be foreseen in its national legislation. An example of such national exclusion grounds is the AntiMafia declaration requested in Italy.

(55) eCertis also includes information on countries from the European Economic Area: Iceland, Liechtenstein and Norway. Other European States are considering joining eCertis.

an information one-stop-shop on means of proof requirements used in public procurement in the EU, and it allows benchmarking of the regulatory practices of Member States in the field of certificates requested for public procurement.

### 5.3. The ESPD as a driver for the introduction of the ‘once-only’ principle

According to Article 59(1) and (5) of the Directive, when the contracting authority can obtain the supporting documents directly by accessing a database, the ESPD should include the relevant information (e.g. the link to the website of the database storing the information and the code necessary to access it) to make this possible. The bidder should not be required to provide the supporting documents insofar as the buyer can access a national database available free of charge in any Member State. These provisions are complemented with the requirement aiming at ensuring that foreign buyers obtain the same conditions of access with regard to the databases.

Therefore, the ESPD is rightly considered a building block in the development of the ‘Once-Only Principle’ (OOP) meaning that suppliers should not be asked (or asked once at the most) to provide information in order to demonstrate that they meet the requirements set out in an administrative procedure, since this information is already available in databases owned by public authorities. Obviously, the implementation of e-procurement is one of the preconditions for the seamless flow of data between the registry or databases containing the certificates and the contracting authority. In this respect, it is to be noted that the suppliers give buyers consent to retrieve the relevant information from the database. This allows addressing data protection requirements<sup>(56)</sup> and the processing of personal data contained in the ESPD relating to natural persons who are members of an administrative, management, or supervisory body of the supplier.

Thus, one significant simplification in the public procurement procedure is to integrate the ESPD with databases and/or a system for the pre-qualification of suppliers. This integration would allow automatic verification of bidders’ compliance with exclusion or selection criteria. The Commission’s recent report on the practical application of the ESPD indicates that two thirds of Member States plan to proceed with such integration, acknowledging the importance of the ESPD as a building block for the digitisation of public administration.

The level of OOP readiness is rather variable in the Member States, as reported by the Commission. A large group of Member States indicated that the databases are not open to access by other parts of the administration for direct consultation or for interconnection. On the other hand, eleven Member

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<sup>(56)</sup> Art. 83(6) and 86(2) of Dir. 2014/24/EU refers to the need to observe data protection rules (both EU rules and national ones). This issue is also addressed by Recital 5 of the ESPD Regulation.

States have reported that all contracting authorities can access national databases to retrieve certificates directly, although this possibility is applicable only to certain types of documents, such as those relating to exclusion grounds. The three Baltic States already have a system in place allowing all buyers to automatically retrieve and verify the compliance of suppliers for certain types of requirements. These Member States plan to link the ESPD to all registries so as to cover all points, allowing for the simplified verification of data.

#### 5.4. Initial implementation of the ESPD

Given the importance and innovative character of the ESPD, the EU legislator provided for the Commission to “review the practical application of the ESPD taking into account the technical development of databases in the Member States and report thereon to the European Parliament and the Council by 18 April 2017”.<sup>(57)</sup> The Report, which included a survey of Member States and a survey of targeted stakeholders, was published on 17 May 2017.<sup>(58)</sup>

In view of the innovative nature of the ESPD and the number of parties involved in the requirement of using the ESPD (all buyers in the EU), the Commission has put in place accompanying measures to support Member States in its implementation, including various IT solutions,<sup>(59)</sup> workshops in the Member States, and funding.

The report referred to above came too early to appreciate in full the practical application of the ESPD. As pointed out by the Commission in its report, some Member States indicated that the number of contracts awarded was still very small, for instance due to budgetary restrictions or due to the still-recent transposition of the Directive at the time of the survey. As reported by the Commission, only two Member States provided a quantitative estimation of the impact on companies: according to Denmark, the benefits accrue to 12 million euros per year, while Croatia reported an 83% reduction of costs in preparing bids with regard to means of proof. This provides only a partial estimation of the benefits since it does not include those benefits deriving from a reduced administrative burden for buyers. It is also true that such a huge change, implying moving from a paper-based transaction to a structured data transaction, is quite difficult to measure and at the same time requires some time for the parties concerned to adjust. Overall, in qualitative terms, the Commission reported that most Member States expressed favourable views on

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<sup>(57)</sup> Art. 59(3). This is 2 full years earlier than the ‘ordinary’ date, 18 April 2019, foreseen for the general review of the Directive pursuant to its Art. 92.

<sup>(58)</sup> EU Comm., “Report to the European Parliament and the Council on the practical application of the European Single Procurement Document”, COM (2017) 242 final, 17 May 2017.

<sup>(59)</sup> The online service developed by the Commission aims at helping Member States in the transition to e-procurement, until they have fully integrated an ESPD. It is therefore a transitional tool.

the ESPD; nonetheless, some of them raised some concerns with regard to the complexity of the document, its wording, and the need to adjust from use of a simpler self-declaration, where in use.

## 6. Conclusions

This paper has briefly illustrated the main innovations in the public procurement process introduced by the Directives on public procurement of 2014. These are the digitisation of procurement, the use of self-declaration via a standard form (the ESPD), joint cross-border procurement (JCBPP) and cooperative procurement via institutional bodies, CPBs.

While some of the innovations are compulsory (the use of the ESPD, as well as the digitisation of certain phases of the procurement procedure), others are voluntary, such as the establishment of CPBs or the use of JCBPP. Regardless of whether or not they are mandatory, these elements also have a significant systemic effect on the organisation of public procurement and its dynamic functioning. To fully exploit the transformative character of these changes, Member States should go beyond what is required by the Directives while respecting their requirements. This will require making policy choices in the setting of the public procurement system, so as to generate efficiencies and savings, which, if translated into tax reduction, could contribute to economic growth.

For instance, this implies using the window of opportunity for the transition to e-procurement provided by the EU rules (which covers e-notification, e-access and online submission) to digitise the full procurement process from planning to archiving.<sup>(60)</sup> Also, it implies using ESPD as leverage to connect with national databases and with a view to automating the verification of compliance with exclusion and selection criteria. At this point in time, it is key for Member States to set the right regulatory conditions (legal and technical) in which the various parties (buyers and bidders, providers of e-procurement solutions, providers of national IT systems such as databases, etc.) operate. This will prevent the creation of an IT legacy which is a significant obstacle to interoperability. Some Member States are taking a comprehensive approach to the transition to e-procurement, demonstrating political will, vision and the administrative capacity to enable digital transformation. The potential impact of e-procurement as a contributor to digital transformation is huge and may result in solutions going beyond what can be anticipated today.

The digital age is about accessing and processing data. To allow this to happen, e-procurement requires ‘datafication’ of information, in order for it to

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(60) Recital 52 of Directive 2014/24/EU states explicitly that “Member States and contracting authorities remain free to go further if they so wish” with regard to the phases to be made electronic.

be tabulated and analysed.(61) Using electronic platforms for the transition to e-procurement is a necessary pre-condition. The requirements on traceability and auditing stemming from the Directive support this view: Annex IV of Directive 2024/24/EU sets out minimum requirements for tools and devices for the electronic receipt of tenders, requests for participation and plans and projects in design contests. The process may be properly audited and traced to meet the requirements of Annex IV only when e-procurement platforms are used. In other words, it is not possible to ensure that these requirements are met by sending bids via e-mail (e.g. with the bid attached) as this may not guarantee sufficiently secure storage of bids and access to their content.

For a policymaking or monitoring body this means being able to assess and control what has been procured, how, and from whom. Contract registers(62) covering the life cycle of the contract(63) are an efficient tool for the promotion of good governance through enhanced transparency.(64) This also means open data made available to non-State actors. Data mining tools enable benchmarking the performance of individual buyers, or spotting anomalous behaviour out of thousands of datasets. Furthermore, the creation of a seamless flow of data also makes it possible to reconcile procurement (purchase orders by individual contracting authorities), payment and accounting data. From the perspective of managing public expenditure this is a significant step forward.

Data analysis helps make sense of the landscape and taking fact-based policy decisions. Further, CPBs gather market intelligence which is produced from a single source. This is not only relevant for operational tasks relating to the calls, but also in relation to demand and supply. This point has led some Member States to integrate procurement policy, strategy and CPBs (including some sectorial ones) in one office with the objective of strengthening spend analytics and data management; and, at the same time, securing savings. As clearly explained by Blomberg,(65) “there is a need to develop national strategies on the development and organisation of the procurement system where the

(61) V. MAYER-SCHÖNBERGER and K. CUKIER, *Big Data. A Revolution That Will Transform How We Live, Work and Think*, Boston, Houghton Mifflin Harcourt, 2013.

(62) EU Comm., “Upgrading the Single Market: More opportunities for people and business”, COM (2015) 550 final, 28 October 2015. As indicated in the EU Commission’s Staff Working Document (SWD [2015] 202 of 28 October 2015) accompanying the Communication on the Upgrading of the Single Market, contract registries store digitalized contracts, their structured summaries as well as full wording, including contract performance conditions, terms of delivery, and subsequent modifications. Ideally, an enforcement mechanism is in place to ensure the publication of the contract (e.g. the contract is void in case it is not published in the register).

(63) OECD, aforesaid, 30. In particular Recommendation II which refers explicitly to transparency in all stage of public procurement cycle.

(64) See BASE <http://www.base.gov.pt/Base/pt/Homepage>

(65) P. BLOMBERG, “Future trends of CPBs and the role of the European Commission”, follow up note to brainstorming meeting, 2015.

goals, visions and priorities, are outlined and communicated to the administrations”. In other words, this calls for steering public procurement, lacking so far in most Member States.

Another relevant aspect – still connected to the above – concerns the mainly dual role of CPBs: platform providers, and organizers of the marketplace for buyers and sellers alike, happy to delegate procurement tasks, responsibility and litigation risk. In practical terms, these roles imply the provision of IT platforms and/or the procedural ‘platform’ for the purchase itself (the framework agreement, a dynamic purchasing system, or an e-catalogue) so as to overcome the fragmentation deriving from infinite individual award procedures to procure similar goods or services. In this respect, data analysis and the new techniques for CPBs complement each other.

Each of the novelties introduced by the new Directives has value on its own; however, the combination of e-procurement and aggregation techniques may result in more than proportional changes. In every field digital platforms have dramatically reduced transaction costs for both buyers and suppliers.<sup>(66)</sup> These platforms match buyers and sellers of a huge variety of products and services and thereby enjoy an increasing return to scale since adding a new product on an e-catalogue has a very low marginal cost.<sup>(67)</sup> At the same time, digital platforms have the potential of harnessing highly competitive markets, which can significantly cut process cost for the contracting authority with lower prices. Consumer habits are changing and public procurement is unlikely to remain indifferent to the effect of technological change on procurement modalities. Thus, it may be argued whether in the future contracting authorities might be tempted to resort to privately-owned platforms operating in business-to-consumer services, or whether the legislation would adjust to allow the development of innovative organisational models, including “outsourcing” IT platforms to private operators.

Obviously procurement will remain essentially a national issue. Nonetheless, JCBPP stands out in terms of process innovation as it creates the conditions for cooperation between administrations in the Single Market; from the buyer’s perspective, JCBPP implies being open to evaluating and even awarding a contract to a foreign bidder, and being ready to accept means of proof delivered by a foreign administration. JCBPP can thus be seen from another perspective: anticipating the possibility of choosing a foreign supplier at the stage of preparation of the procedure (*ex ante*); this differs significantly from the traditional procedure, wherein foreign suppliers might be selected

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(66) K. SCHWAUB, “The Fourth Industrial Revolution”, World Economic Forum, 2016.

(67) The e-catalogue of eSPap include 23.000 products, Ugap and BBG catalogue includes 300.000; Consip’s 8 million.

only after the evaluation (*ex post*) if it offers the best value for money and thus prevails over other localistic considerations.

Public procurement remains a highly regulated activity and at least in the initial phase of implementation JCBBB does not seem sufficient to stimulate competitive dynamics between buyers (*i.e.* public bodies) from different Member States. However, it opens up the possibility of co-operation between large buyers (CPBs or large cities) in areas of mutual interest (for instance, to share the cost and the risk linked to innovation projects) or between buyers located in bordering areas building infrastructure linking the two adjacent territories.

The new standard forms for publication of notices in TED – being implemented in the EU – allow identifying JCBPP projects for both entities (under the Utilities Directive) and contracting authorities (under the Classic one). The 2017 data confirm the interest of buyers in applying this new tool. It can be assumed that the increase of legal certainty produced by the new rules led to an increase of cases; however, this cannot be ascertained definitively due to the lack of data for the previous years.

Results seem to confirm that JCBPP via centralised purchasing is extremely rare; the reasons for this are to be researched (perceived insufficient legal certainty e.g. with regard to applicable law in review procedures, lack of motivation of CPBs, etc.). In most cases the countries concerned share the same border; the geographical nature of the goods or services or works to be procured (e.g. maritime navigation aids, construction of a tunnel or a bridge between two countries, air navigation systems) pushes them to award the contract jointly. In these situations, the need for close coordination between parties from different Member States is a valid reason for implementing JCBPP. The same holds true for projects concerning utilities (purchase of connectors, cables etc.); in addition, those companies operate in a different context than public buyers, with efficiency-driven operations. In some others there is no common border (purchase of electric cars, software) and parties have decided to award jointly the contract. This is likely due to sharing (transaction and purchasing) costs and knowledge and procuring innovative goods or services. In either case the voluntary use of this innovative process looks to be a good deal for the procuring bodies.



## CHAPTER 2

### Cooperative Purchasing: A US Perspective

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#### *1. Introduction to cooperative purchasing*

The 2000 American Bar Association (ABA) Model Procurement Code defines cooperative purchasing (known generally in the European Union as 'Joint and Collaborative Procurement') as a "procurement conducted by, or on behalf of, one or more Public Procurement Units".<sup>(1)</sup> How it comes to be, and how it is evaluated, contracted for, and made available to governmental entities are some of the broader questions that surround cooperative purchasing today. Suffice it to say, cooperative purchasing is on the rise<sup>(2)</sup> and utilized at nearly every level of government, from the federal government to the smallest of local entities. Thus, it becomes important to understand why governmental entities use cooperative purchasing, to what benefit, and at what expense. In order to do so, it is necessary to examine the principles underlining cooperative purchasing, its legal basis, the types of cooperatives in existence today in the United States, the structure and processes that exist within those cooperatives, and the issues, concerns, and practicalities that are associated with cooperative purchasing. It should be noted that discussion herein focuses on the U.S. experience of cooperative purchasing as it exists primarily between U.S. States and does not address transnational procurement or collaboration.

The fundamental principles surrounding cooperative purchasing do not differ from the fundamentals surrounding public procurement in general; or rather, they should not. The requirements to ensure fair and open competition, transparency, and accountability must be met whether one is leading or participating in cooperative purchasing. However, while these principles or requirements are nearly universal in public procurement, their meanings

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(1) American Bar Association (ABA), *The Model Procurement Code for State and Local Governments*, Art. 10, Part A, Definitions, §§ 10-101(1), 2000, p. 79.

(2) National Association of State Procurement Officials (NASPO), "Strength in Numbers – An Introduction to Cooperative Procurements", February, 2006.

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change depending upon the applicable legal requirements and policies. As well, what may seem fair and open to one entity at the city level may not look fair and open to a counterpart at the State level, and vice versa.

### 1.1. Fair and Open Competition, Transparency, and Accountability

Fair and open competition is a key principle underlying the integrity of public procurement and public trust.<sup>(3)</sup> In basic terms, fair and open competition means that the government entity treats everyone fairly and conducts the procurement in a transparent manner. This concept of fair and open competition applies throughout the procurement process, from the drafting of the solicitation to its issuance, the evaluation of responses, and the resulting contracts.

To ensure fair and equal treatment and access in the procurement process, thereby adhering to the principles of fair and open competition, procurement professionals must provide each of the following in a timely manner:<sup>(4)</sup>

- advance public notice of State business opportunities;
- advance disclosure of all mandatory requirements and selection criteria;
- identical information to all interested vendors, presented at the same time;
- a selection of vendors based solely on defined criteria and process; and
- appropriate oversight to prevent organizational conflicts of interest.<sup>(5)</sup>

Each of these requirements presents unique challenges in public procurement, recognizing that each of these unique challenges magnifies when engaging in cooperative purchasing that involves multiple government entities.<sup>(6)</sup> For the latter, participation in the process by governmental entities allows each entity to ensure that its own requirements for fair and open competition and transparency are met. It is essential for any participating government entity to verify that the cooperative purchasing entity has met those said requirements before it engages in cooperative purchasing.

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(3) E. HAYES, “An Introduction to Cooperative Purchasing”, presented periodically to Seminar Class at The George Washington University Law School by Elizabeth Hayes and Justin Kaufman.

(4) *Ibid.*, p. 3.

(5) For additional information on organizational conflicts of interest, see National Association of State Procurement Officials, *State and Local Government Procurement, A Practical Guide*, 2<sup>nd</sup> ed., 2015, p. 242.

(6) For additional information on public procurement in the United States, see D.M. CONWAY, “State and Local Government Procurement”, *American Bar Association Section of State and Local Government Law*, 2012.

## 1.2. The Case for Cooperative Purchasing

A strong justification for participation in cooperative purchasing lies in the notion that buying in large volumes (leveraged spend) leads to several benefits, to include, among others, lower per unit costs, the ability to insist on better terms of service, and overall better value.<sup>(7)</sup> In addition to price competition, there are other efficiencies to be gained through cooperative purchasing. Governmental entities are continually asked to do more with less, *i.e.*, with budget reductions leading to an increased workload and declining resources. Therefore, the ability to engage in cooperative purchasing permits one governmental entity to provide resources and experts, the benefit of which can be enjoyed by all of the entities that are involved. This allows governmental entities with fewer resources to engage in procurements and contracts that may otherwise be cost or resource prohibitive, while giving the government entity that provides the resources and expertise the opportunity to take advantage of its increased purchasing power. Therefore, through cooperative purchasing, these entities are able to share their varied expertise, pool their resources, distribute their workloads, and work as a shared unit.

Another common interest for government entities in cooperative purchasing is the advancement of social interests, where the increased purchasing power provides an ability or potential to steer the market to meet the governments' needs. For example, imagine the impact of a large number of U.S. States requiring all photocopiers to meet federal accessibility requirements in order to be eligible for a contract under a cooperative purchasing effort.<sup>(8)</sup> Would that be sufficient to move the marketplace toward developing and manufacturing more accessible photocopiers? This idea and the veracity of the assumptions that surround it are addressed later from a more rounded perspective. For now, let us continue by examining the legal authority to lead and participate in cooperative purchasing, from a U.S. perspective.

## 2. The Legal Basis

A common theme in public procurement is the notion that in the private sector you can do anything that is not prohibited, whereas in the public sector you can only do what is authorized.<sup>(9)</sup> While perhaps an over-generalization, what this means in practicality is that each State must have the authority to

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(7) National Association of State Procurement Officials, *State and Local Government Procurement: Practical Guide*, *op. cit.*, p. 189.

(8) Federal Acquisition Regulation (FAR), Section 508 of the Rehabilitation Act, 36 CFR Part 1194 (2000) (accessibility requirements).

(9) See J.E. ARNOLD, *Anyone Who Can Be Fired Needs a Fallback Position: Preparing a Contingency Plan for the Worst Case Scenario*, Topeka, Exurba Publishing, 2003, p. 42.

participate in cooperative purchasing set forth within its statutory framework, rather than a mere absence of a prohibition to do so.

To that end, not all States or jurisdictions allow the participation of governmental entities in cooperative purchasing. Some States are permitted to engage in cooperative purchasing but restrict or regulate its scope. The 2009 survey conducted by the National Association of State Procurement Officials (NASPO) found that:<sup>(10)</sup>

- 40 U.S. States had the authority to enter into cooperative purchasing with local governments within their State;
- 44 U.S. States had the authority to enter into cooperative purchasing with other States (each also chose to enter into cooperative purchasing with other States) – NASPO’s 2018 Survey of State Procurement Practices showed an increase to 48 States having authority to enter into cooperative purchasing with other States (out of 48 States that responded to the survey);<sup>(11)</sup>
- 37 U.S. States had the authority to engage in cooperative purchasing with the federal government;
- 6 U.S. States had the authority to engage in cooperative purchasing with other countries;
- 14 U.S. States had the authority to do cooperative purchasing with not-for-profit associations; and
- 1 U.S. State did not have the authority to enter into cooperative purchasing.

In the 2015 NASPO survey, 44 U.S. States indicated the extent of their legal authority to enter into cooperative purchasing.<sup>(12)</sup> The 2015 NASPO survey further delineated the said authority, and addressed the specific actions that the U.S. States must take to meet the requirements for fair and open competition, and transparency. For example:

- 21 of 44 States reported that they must be named as a potential participant in the cooperative’s solicitation;
- 19 of 44 States reported that they must advertise the original solicitation;
- 6 of 44 States reported that they must participate in the evaluation or award decision;
- 9 of 44 States reported that they must review and approve the final contract;
- 17 of 44 States reported that there were ‘other’ requirements; and

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(10) NASPO, *2009 Survey of State Government Purchasing Practices*, 2009.

(11) NASPO, *2018 Survey of State Procurement Practices, Summary Report*, April 2018.

(12) NASPO, *2015 Survey of State Procurement Practices, Summary Report*, September, 2015.

- 10 of 44 States reported that there was no such obligation prior to participation.(13)

The data provided in the 2015 survey is important not only to an understanding of the landscape among the U.S. States, but to identifying the factors that are necessary to ensure fair and open competition, transparency, and accountability. Whether expressly required by law or not, the survey suggests that “being named as a potential participant, advertising the solicitation in their states, participating in the evaluation process, and reviewing and approving the final contract” are some of the best practices for cooperative purchasing. That said, State laws vary dramatically on the requirements and safeguards necessary, including the need for publication and competition, prior to engaging in cooperative purchasing.(14)

## 2.1. ABA Model Procurement Code

To date, the American Bar Association’s (ABA) Model Procurement Code (MPC) has been adopted (either the 1979 or 2000 version) by 26 U.S. States, with complete adoption in only three States.(15) In addition, hundreds of local jurisdictions across the U.S. have adopted some sections of the MPC in their procurement codes or regulations.(16) The ABA 2000 Model Procurement Code contains language not only authorizing Public Procurement Units to engage in cooperative purchasing, but also encouraging such participation.(17) Definitional changes were also made in the ABA 2000 MPC which expanded the term ‘Public Procurement Unit’ to include “local governments, other State governments, local governments in other States, federal agencies of the United States”, and certain not-for-profit entities.(18)

Section § 10-201(1) of the code authorizes cooperative purchasing, stating in part:

“Any Public Procurement Unit may either participate in, sponsor, conduct, or administer a Cooperative Purchasing agreement for the procurement of any supplies, services, or construction with one or more Public Procurement Units in accordance with an agreement entered into between the participants [...]”.(19)

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(13) *Ibid.*, p. 12.

(14) For a more complete analysis, see E.P. ROBERSON, “No Compete Contracting in Cooperative Purchasing? Proposed Solutions to Resolve Gaps in Competition, Transparency, and Socioeconomic Policy at the State and Local Level”, *Pub. Cont. L.J.*, 2017, p. 753.

(15) NASPO, *2018 Survey of State Procurement Practices, Summary Report, op. cit.*, p. 11.

(16) NASPO, *2016 Survey of State Procurement Practices, Summary Report*, September, 2016.

(17) *Ibid.*, p. 16.

(18) *Ibid.*

(19) *Ibid.*, pp. 16, 80 and ff.

Section §10-201(2) clarifies, as a requirement, that “[a]ll Cooperative Purchasing conducted under this Article shall be through contracts awarded through full and open competition, including use of source selection methods substantially equivalent to those specified in Article 3 (Source Selection and Contract Formation) of this Code”.(20) Not surprisingly, the sourcing requirements in the model code are aligned with the restrictions that are identified in the 2015 NASPO survey, including the requirements for fair and open competition discussed above.

## 2.2. A State Example: Minnesota Law

The State of Minnesota traces back its authority for the ‘joint exercise of powers’ to an act that was introduced and approved by the Minnesota legislature in 1943.(21) Under the current Minnesota law, the authority to conduct and participate in cooperative purchasing is contained in a tapestry of statutes. The State of Minnesota derives its general authority to conduct its own cooperative purchasing program from two sources:

(1) Minnesota Statutes § 16C.03, which provides the authority “to enter into a cooperative purchasing agreement for the provision of goods, services, construction, and utilities,” and sets forth a list of entities that are authorized by law to enter into cooperative agreements with Minnesota;(22) and

(2) Minnesota Statutes § 471.59, which provides a broad authority for the State to participate in cooperative purchasing, stating in part that “[t]wo or more governmental units, by agreement entered into through action of their governing bodies, may jointly or cooperatively exercise any power common to the contracting parties or any similar powers, including those which are the same except for the territorial limits within which they may be exercised. The agreement may provide for the exercise of such powers by one or more of the participating governmental units on behalf of the other participating units”.(23)

Through this authority, Minnesota may forgo its own competitive process when it utilizes a cooperative agreement that is provided by another governmental entity.(24) It is worth noting that Minnesota Statutes §§ 16C.03 and

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(20) *Ibid.*, p. 19.

(21) Minnesota Statutes, § 471.59, created in 1943 under Chapter 557, House File 721, Approved 22 April 1943.

(22) Minnesota Statutes, § 16C.03, Subd. 10.

(23) Minnesota Statutes, § 471.59, aforesaid, p. 21.

(24) Minnesota Statutes, § 16C.10, Subd. 4, which states: “The solicitation process described in this chapter is not required for cooperative agreements. The commissioner may enter into contracts or accept prices effective for sales to any governmental unit as defined in section 471.59, through a cooperative agreement as defined in section 471.59”.

471.59 not only authorize Minnesota to participate in cooperative purchasing, but also provide the State with the authority to create its own cooperative purchasing program, which is currently known as the “Cooperative Purchasing Venture (CPV)” program. Aside from the benefits of an aggregated spend for the State of Minnesota, the CPV program is also established for the benefit of local governments, and must be at least considered for use by local governments under certain circumstances. For example, pursuant to the Minnesota Statutes § 471.345, Subd. 15, “[f]or a contract estimated to exceed \$25,000, a municipality (*a type of local government*) must consider the availability, price and quality of supplies, materials, or equipment available through the State’s cooperative purchasing venture before purchasing through another source”.(25)

### 3. Common Types of Cooperatives

Cooperative purchasing entities (a group of governmental entities engaged in cooperative purchasing) often attempt to distinguish themselves based on their core participants, the products and services offered, and their alignment with other organizations. While these are all quantifiable characteristics to be considered, the cooperatives also differentiate themselves on the basis of a number of characteristics unique to cooperative purchasing, *i.e.*, labels or categories that governments colloquially, if not formally, assign to cooperative ventures. To that end, cooperative purchasing is commonly divided into three categories: formal cooperatives, piggyback contracts, and third-party aggregators.(26)

#### 3.1. Formal Cooperatives

Formal Cooperatives (sometimes called ‘true’ or ‘pure’ cooperatives) involve public sector organizations that work together from the inception of an idea through the processes of solicitation, evaluation and award. There is typically a formality to the organization, including the creation of a board, membership, voting rights, bylaws, and other means and measures of documenting the cooperative.(27)

The key hallmark of a ‘true’ or ‘pure’ cooperative is collaboration by the participating governmental entities. With a formal cooperative, one governmental entity typically serves as the “lead” entity, which issues the solicitation

(25) Minnesota Statutes, § 471.345, Subd. 15 (emphasis added).

(26) C. MUSE, CPPO, Director, Department of Purchasing and Supply Management, County of Fairfax Virginia, “Incorporating Cooperative Purchasing into Your Agency”, National Institute for Government Purchasing (NIGP) webinar.

(27) *Ibid.*, p. 26.

for bids or proposals in accordance with its own procurement laws.(28) This does not occur in a vacuum, but in collaboration with other members and participants which provide guidance and ensure that their own procurement laws are also being met in the solicitation.

Formal cooperatives are generally rule-driven entities, in which members' individual legal requirements, typically set forth in statute, must be met in order for the members to participate in the cooperative, and the cooperatives' processes accordingly are designed to ensure fair and open competition and transparency.(29) Formal cooperatives therefore generally require a high level of participation by their members, significant documentation to ensure transparency, and solicitation and evaluation processes designed to meet the needs of a wide range of governmental entities. While formal cooperatives entail a high level of effort and process on the part of those participating in cooperative purchasing, they also provide for the greatest deference to the key principles of public procurement, transparency and competition.

### 3.2. Piggybacking

Piggybacking occurs when one or more organizations issue a solicitation, and another unplanned governmental entity elects to 'piggyback' or uses the resulting procurement process as a shortcut to meeting its own requirements.(30) The piggybacking governmental entity may rely on a previously issued solicitation by another entity, and may issue its own purchase order, establish its own separate contract, or join a cooperative contract as a means of accessing the contract after the procurement is completed. The piggybacking entity determines its own ability to piggyback, and is responsible for verifying that its procurement laws have been followed by the lead entity, and that it has the authority to piggyback on the contract. The vendors under a contract to sell goods or services to the lead governmental entity are unlikely to refuse a request from a piggybacking entity. Further, a lead entity may not be aware of the piggybacking, or may be aware but have little ability to control the actions of another governmental (piggybacking) entity. While piggybacking offers convenience for governmental entities, it also poses risks to the requirements for fair and open competition by both the piggybacking entity and the lead entity.(31) As a lead governmental entity may have little ability to control the piggybacking, or may wish to permit piggybacking only to take advan-

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(28) National Association of State Procurement Officials, *State and Local Government Procurement: Practical Guide*, *op. cit.*, pp. 7, 195.

(29) *Ibid.*, pp. 7, 189.

(30) C. MUSE, "Incorporating Cooperative Purchasing into Your Agency", *op. cit.*, p. 26.

(31) For example, *see* D. HINDMAN and R. PARKER, "Piggyback Contracts: The Benefits and the Limits of Shared Purchasing", *PSG Proc. L.*, Spring 2014, p. 16.

tage of the combined purchasing power, a lead entity's solicitation may use general language notifying vendors of the potential for piggybacking under a subsequent contract.

### 3.3. Third-Party Aggregators

Third-Party Aggregators are organizations that create and market cooperative contract opportunities to governmental entities, with contracts that may have been competitively solicited or directly negotiated without regard to fair and open competition, in the strictest sense.<sup>(32)</sup> Third Party Aggregators often bring together multiple organizations to represent their requirements, and manage the resulting contracts or contractors. While in formal cooperatives and piggybacking arrangements the original solicitation is for the benefit of the lead governmental entity, this may not be the case with a third-party aggregator.

## 4. From Types to Characteristics

While the terms 'formal', 'piggybacking', and 'third-party aggregation' provide us with a general framework for understanding the cooperatives that are currently present in the marketplace, these defining terms can also be used on a spectrum as factors to better understand the nature of cooperatives and how they operate. Consider the notion of a cooperative as formal or informal, piggy-backing on a range of permissibility, and aggregation in the sense of whether the resulting contract is intended primarily for the use of the lead or for its members.

### 4.1. Formality as a factor

While a formal cooperative may entail agreements between the members, a board of directors, and other formalities, an informal cooperative may be (for example) a simple agreement between two schools to combine their resources to make a purchase. In this instance there may simply be a collaboration to obtain a low bid for some larger amount of product, with the two schools combining their demand for solicitation and bidding on a solicitation that will ultimately result in two independent purchases. Formality as a factor is a matter of identifying the organizational structure behind the cooperative purchasing, and determining if a formal cooperative exists or if the arrangement is just a simple agreement to collaborate.

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(32) C. MUSE, "Incorporating Cooperative Purchasing into Your Agency", *op. cit.*, p. 26.

## 4.2. Piggy-backing as a factor

In the context of cooperative purchasing, nothing seems to draw concern quite like the invocation of the term ‘piggybacking’. Nonetheless, piggybacking occurs, at some level, in nearly every formal cooperative. We know of at least 21 U.S. States that permit the participation of other States in a cooperative, even if those participating States were not listed as participants when the original solicitation was issued.<sup>(33)</sup> To take this one step further, local governmental units that are able to access a State-led cooperative via their respective State agreements are typically not listed as participants, because listing every local government as potentially eligible would be impractical. The question then become the extent to which the solicitation and its resulting contract will be structured to accommodate piggybacking, and the efforts that will be made by the cooperative purchasing entity (the customer) to balance the ready availability of this option with legal requirements for fair and open competition. In other words, will the lead contract support piggy-backing, and will a customer agency not abuse piggy-backing to avoid normal requirements for transparency and competition.

## 4.3. Third-Party Aggregation as a Factor

Another way to organize this taxonomy is to look to the purpose of the master agreement underlying the cooperative: is the primary purpose of the cooperative for the use by the lead entity, or is it intended for the use of its members? The arrangement is more of a ‘formal’ cooperative when the lead entity intends to use the contract, but acknowledges that it will obtain an advantage by allowing piggybacking. Conversely, when the lead entity has little or no need for the contract, but executes the contract primarily for the benefit of its members rather than its own use, then it is more likely that we have what is known as ‘third-party aggregation’.

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In the following sections, we will begin introducing a number of U.S. cooperatives, and discuss the unique nature and structure of each. Each of these cooperatives sits on a spectrum of formality, piggybacking, and third-party aggregation.

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(33) NASPO, *2015 Survey of State Procurement Practices, Summary Report, op. cit.*, p. 12.

## 5. A Sample of U.S. Federal and State Cooperatives

The list of existing U.S. cooperatives is extensive, from the federal General Services Administration's Multiple Award Schedule (MAS) contracts, to State-led cooperatives, to those arrangements led and managed by cities, counties, schools, and cooperative authorities. These cooperatives often work from the top down. For example, cities may use State-led cooperatives, or cities and States may use federal price schedules, but it is less likely that the federal government would use State-led or city-led cooperatives. Use tends to flow down-stream (lower-level governmental entities) or cross-stream (similarly situated government entities) from the cooperative, with less use up-stream (higher-level governmental entities). This may be due to the more stringent requirements for fair and open competition that exist at the State and federal levels – requirements which may simply not be met by contracting arrangements launched at a local level. For the purpose of comparison, we will focus on the federal MAS contracts, and on two large State-led cooperatives, NASPO ValuePoint and the Minnesota Multistate Contracting Alliance for Pharmacy (MMCAP).

### 5.1. Federal Cooperative Purchasing Program and State Equivalents

The General Services Administration (GSA) within the U.S. federal government “establishes long-term government wide contracts” (known as ‘Multiple Award Schedule’ or ‘MAS’ contracts) “with commercial firms to provide access to millions of commercial products and services at volume discount pricing”.<sup>(34)</sup> Certain of those MAS contracts (for information technology, for example) are made available to State, local and tribal governments, among others, under what is referred to as the Cooperative Purchasing Program. These MAS contracts are entered into under standard federal requirements for purchasing supplies and services.<sup>(35)</sup> Under these contracts, State and local governments have access to a wide array of products and services, including information technology<sup>(36)</sup> and law enforcement equipment.<sup>(37)</sup> However, purchases under GSA contracts (specifically Schedules 70 and 84) were only made available to State and local governments in 2002, following a study that showed inconclusive results on whether use of the GSA schedules would impact

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(34) Government Services Administration Schedules, last reviewed February 14, 2017.

(35) See Federal Acquisition Regulation (FAR), Subpart 8.4, available at [www.acquisition.gov/far/html/Subpart%208\\_4.html](http://www.acquisition.gov/far/html/Subpart%208_4.html), and FAR, Part 38.

(36) Government Services Administration, Schedule 70.

(37) Government Services Administration, Schedule 84.

small businesses' ability to compete for contracts.(38) This question will be addressed later in the general framework of the impact cooperative purchasing presents to small businesses and social interests.

Despite concerns related to small business impact, the use of the GSA contracts appears common at the State and local levels because the contracts are relatively easy to use and their use is generally permitted by law. For example, in the State of Minnesota, pursuant to statute the State may "instead of soliciting bids, contract for purchases with suppliers who have published schedules of prices effective for sales to any federal agency of the United States".(39) These contracts may be used, regardless of the amount of the purchase price, so long as the use of the MAS contract is deemed advantageous and the prices do not exceed those set forth in the federal schedule.(40) However, it should be noted that when using GSA's Cooperative Purchasing Program, the State of Minnesota uses only the price schedule, not the underlying federal contract, and enters into negotiations with the federal supplier for a direct contract using the federal prices. (Notably, while States have access to the federal GSA contracts, it does not appear at this time that the federal government is availing itself of the use of any State or local cooperative agreements.)

As previously described, the use of the GSA contracts and their price schedules is a relatively 'informal' process, and strictly voluntary.(41) Their use generally is limited only by the legal restrictions of the customer State and local entities. Unlike some 'formal' cooperatives, there is no organization to join, no membership applications to complete or annual meetings to attend, and, certainly, there are no boards of directors. Furthermore, the GSA contracts and price schedules are sourced by the federal government, and available for use if permitted by the purchasing entity and allowed by the vendor under the terms of its federal contract.(42)

The GSA Cooperative Purchasing Program resists ready categorization, in part because it is a relatively small part of federal MAS contracting overall. While it seems inappropriate to characterize cooperative use of the GSA MAS contracts as 'third-party aggregation', since the federal government remains the primary user of the GSA contracts available under the Cooperative Purchasing Program, it is less clear whether we should characterize the use of the GSA MAS contracts by other governmental entities as

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(38) "State and Local Governments: Ditch the GSA Schedule and Do It Yourself", *Pub. Cont. L.J.*, 2015, pp. 573, 581-582.

(39) Minnesota Statutes, § 16C.10, Subd. 3.

(40) Minnesota Statutes, § 16C.10, *op. cit.*, p. 39.

(41) Government Services Administration, "Cooperative Purchasing FAQs".

(42) *Ibid.*, p. 41.

‘piggybacking’. For the sake of argument, consider for a moment whether a solicitation that is issued by the federal government and advertised as available for use by all States and local entities is sufficient to alleviate the concerns normally associated with piggybacking (*i.e.*, extent of its use and the need for fair and open competition). This question remains unanswered for now.

### 5.2. Federal – State Equivalents

A number of States manage programs very similar to the federal MAS Cooperative Purchasing Program for use by their local governmental units. For example, the Minnesota Cooperative Purchasing Venture (CPV) program makes many of the contracts held by the State of Minnesota available for the use of local governments in Minnesota, as well as non-Minnesota local governments, and other States. However, Minnesota’s CPV process is slightly more formal than the federal program. While there are no annual meetings and no board of directors, there is a basic membership application, and an agreement which requires the entities utilizing the program to generally hold the State harmless in the event that the use of the contract leads to any injury. The agreement also sets forth a handful of other legal terms and conditions, such as a limitation of liability, intellectual property rights, warranties and disclaimers, termination for convenience, and requirements for performance bonds.<sup>(43)</sup> There are more than 800 Minnesota State contracts that are available, including contracts for computer hardware and software, cleaning supplies, vehicles, cell phones, copiers, furniture, fuel, paint, paper, road salt, hazardous waste recycling, digital imaging, translation, IT services, and more.<sup>(44)</sup>

### 5.3. NASPO ValuePoint

Unlike the Minnesota CPV arrangements, the cooperative purchasing arrangements sponsored by the National Association of State Procurement Officials (NASPO) are more formal. NASPO was founded in 1947 at a meeting of State purchasing officials held in Chicago.<sup>(45)</sup> Originally, the meeting was held to discuss how States could secure surplus war property from the federal government. One attendee, George J. Cronin, from Massachusetts, “urged the

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(43) R. PENNINGTON, “Comparative Review of State IT Procurement Practices”, prepared for the NASPO IT Procurement Work Group, 2010.

(44) Welcome to Minnesota’s Office of State Procurement Cooperative Purchasing Opportunities, [www.mmd.admin.state.mn.us/coop.htm](http://www.mmd.admin.state.mn.us/coop.htm). For additional examples of State-led cooperatives, *see also* [comptroller.texas.gov/purchasing/programs/co-op/](http://comptroller.texas.gov/purchasing/programs/co-op/).

(45) *History of the Cronin Awards*. <https://www.naspo.org/NASPO-Awards/Cronin-Award-for-Procurement-Excellence>.

formation of an ongoing, formal organization of State purchasing officials as an effective vehicle to address specific public procurement issues and provide a network for resolving problems". The other participants agreed, and elected Cronin to be the president of the new organization.(46)

Seventy years later, NASPO identifies itself as "a non-profit association dedicated to advancing public procurement through leadership, excellence, and integrity".(47) NASPO's leadership is comprised of the directors of the central purchasing offices from each of its members, which include the 50 U.S. States, the District of Columbia, and the territories of the United States.(48)

In 1993, a group of 15 States came together to form the Western States Contracting Alliance (WSCA)(49) to function as a cooperative purchasing program under the banner of the National Association of State Procurement Officials (NASPO). While other regional cooperative purchasing programs were formed under NASPO, none were as prevalent or prolific as WSCA. In 2006, NASPO merged the Eastern, Southern, and Midwest regional cooperatives into the new NASPO Cooperative. Finally, in 2013, as WSCA became more successful and cooperative efforts grew, NASPO consolidated its two remaining cooperatives (WSCA and the NASPO Cooperative) under a non-profit, limited liability company named 'NASPO ValuePoint'.(50)

The NASPO ValuePoint Cooperative Purchasing Organization LLC is a nonprofit, wholly owned subsidiary of the National Association of State Procurement Officials (NASPO).(51) It is led by a 21-member Management Board comprised of State procurement officials appointed by NASPO, its parent organization. Each board member represents one of four original geographic regions that were established by NASPO for cooperative purchasing (e.g., the Western States and the Western States Contracting Alliance).(52) The NASPO ValuePoint Board oversees the strategic direction, operations, and activities of the organization, and does so with the assistance of a contractor hired to facilitate and support the entity and its programs.(53) In fact, NASPO ValuePoint itself awards no contracts, but rather assists States in their collaboration on solicitations and resulting contracts, using a 'Lead State' model.

(46) *History of the Cronin Awards, op. cit.*, p. 45.

(47) "Who We Are", [www.naspo.org](http://www.naspo.org).

(48) "NASPO Membership", [www.naspo.org](http://www.naspo.org).

(49) For a more complete history of WSCA, see J.E. NELSON and J.A. LoBosco, "Understanding the WSCA-NASPO Cooperative Purchasing Organization: It's Time to Invite the Elephant Out of the Corner", 44 *Public Contract L.J.*, 2014, p. 113.

(50) "Who We Are", aforesaid, p. 47.

(51) *Ibid.*

(52) *Ibid.*

(53) "How NASPO ValuePoint Works", [www.naspovaluepoint.org/about](http://www.naspovaluepoint.org/about).

When determining which contracts to pursue as part of the NASPO ValuePoint cooperative, ideas begin at the State level among its members. The ideas are then presented to the NASPO ValuePoint board, which may elect to move the idea forward into a solicitation, to decline the idea, or in some cases, to issue a survey to better understand the needs of the cooperative's members as they relate to the proposed new contract.(54) Once a need is identified, a Lead State is selected (or volunteers), and the lead State begins the process of preparing for the issuance of a solicitation.(55) The lead State will first gather its own staff and experts, and then create a sourcing team composed of subject matter experts from other States. In the lead State model, one State leads the procurement, issues the solicitation, and awards the master contract based on that State's legal and policy requirements. The lead State relies heavily on sourcing teams to provide the needed guidance and to identify customer demand to ensure a successful new cooperative contract(s). Together with the sourcing team, the lead State develops the solicitation for publication, which includes the requirements and evaluation criteria, and then publishes that solicitation in accordance with its own rules, but also taking into account other States' requirements (for longer periods of publication, for example), to make it possible for other States to participate in the resulting contract.(56) Significant effort goes into this process, which is supported by NASPO ValuePoint's general counsel.(57)

Once responses are received from eligible vendors, the sourcing team continues to work with the lead State, in most cases, to evaluate those responses, and ultimately to select the vendors that will be awarded a Master Contract.(58) The Master Contract will be held by the lead State, and serves as the overarching contractual document for all purchases arising from the solicitation.(59) Each State that wishes to participate in the Master Contract, including the lead State, will then issue a Participating Addendum (PA) that will, if agreed to by the awardee Contractors, bind the joining Contractors to each State's specific requirements. The Participating Addendum is a direct agreement between the Contractor and a participating governmental entity that incorporates the terms and conditions included in the original solicitation, the terms and conditions in the Master Contract, and any other additional specific language or other requirements of that

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(54) NASPO, *State and Local Government Procurement: Practical Guide*, *op. cit.*, pp. 7, 195-196 and ff.

(55) *Ibid.*, p. 54.

(56) *Ibid.*

(57) Richard Pennington has served as the General Counsel of NASPO since 2003, and has been instrumental in working to align legal terms and create boilerplate language for use by all lead States.

(58) NASPO, *State and Local Government Procurement: Practical Guide*, *op. cit.*, pp. 54, 195 and ff.

(59) *Ibid.*, p. 58.

State or local entity (a participating entity), generally including an order of precedence.(60) It should also be noted that the participating entities have the flexibility of negotiating additional terms and conditions to meet the unique needs of their States. The results of the negotiations – the special terms – that are incorporated in a Participating Addendum are between the participating entity and the contractor, and do not impact the terms of the Master Contract.

A main purpose of a Participating Addendum is to create privity of contract between each participating entity and each vendor, thereby creating protections in the event of performance issues or should legal liabilities occur. It is worth noting that a Master Contract is signed by the lead State with each vendor under the program; and a Participating Addendum is signed by each State (and some local entities) with one or more vendors under the program. For example, in NASPO's contract for computer equipment, peripherals, and related services, where the Master Contract is held by the State of Minnesota, there was a single solicitation that resulted in the issuance of a Master Contract to 30 vendors, and resulted in over 600 Participating Addenda between the vendors and participating governmental entities.(61) In most cases, a Participating Addendum on the part of a U.S. State is approved by the State's Chief Procurement Officer, or equivalent, at which point the officer may determine that the Participating Addendum is only eligible for State use, or may permit the participation by all eligible local entities within the State. Where the State has not entered into a Participating Addendum, the local entities may enter into their own Participating Addenda, but may (in the case of NASPO ValuePoint) need a prior approval from the State's Chief Procurement Officer.

NASPO ValuePoint currently maintains 67 Contract Portfolios (contracts covering 67 areas) ranging from Auto Parts to Computer Equipment, to infant formula, to Wireless Communication & Equipment.(62) These contract portfolios translate to master contracts with 358 contractors to provide the goods and services.(63) The contracts are established for the use and benefit of the State members and the lead State, and not for the purpose of third-party aggregation. From the standpoint of piggy-backing, these contracts (like the GSA MAS contracts) can be made available to local entities which were not involved in the solicitation and award of the master contracts, but which were broadly identified as potential downstream users.

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(60) "How NASPO ValuePoint Works", aforesaid, p. 53.

(61) "Computer Equipment, Peripherals & Related Services 2015-2020", [www.naspovaluepoint.org/portfolios](http://www.naspovaluepoint.org/portfolios).

(62) "Contract Portfolios", [www.naspovaluepoint.org/portfolios](http://www.naspovaluepoint.org/portfolios).

(63) "Current Portfolios, Contractors", [www.naspovaluepoint.org/contractors](http://www.naspovaluepoint.org/contractors).

To fund its operation, NASPO ValuePoint does not currently charge membership fees.<sup>(64)</sup> Rather, it collects an administrative fee from its contractors when they make a sale through the cooperative's contract. These fees, set by the NASPO ValuePoint Board, fund NASPO ValuePoint and National Association of State Procurement Officials (NASPO) operations, are used to reimburse approved costs of the State leading the cooperative procurement, and provide for training and education of NASPO members.<sup>(65)</sup> The contractor collects the administrative fee at the point of sale, and remits it to NASPO ValuePoint, and not to the lead State.<sup>(66)</sup> Generally the administrative fee paid by the contractors is *de minimis* and has little impact on the pricing that is charged to the purchasing organization. In December 18, 2014 the State of Utah's Office of the Legislative Auditor General reported, "[t]he WSCA-NASPO administrative fee included on most of the organization's contracts does not appear to affect the final price of goods".<sup>(67)</sup>

#### 5.4. Minnesota Multistate Contracting Alliance for Pharmacy (MMCAP Infuse)

The Minnesota Multistate Contracting Alliance for Pharmacy (MMCAP, pronounced 'em-cap') recently re-branded as "MMCAP Infuse", was established in 1985 as a cooperative between the States of Minnesota and Wisconsin. While eligible as a Group Purchasing Organization (GPO) under the federal safe harbor provisions,<sup>(68)</sup> MMCAP is not a non-profit organization, but rather a purchasing cooperative within the State of Minnesota's Office of State Procurement.

MMCAP is a free and voluntary cooperative, with a membership that includes 49 States, and serves thousands of counties, cities, school districts, correctional facilities, and public higher education facilities in all 50 US States.<sup>(69)</sup> While similar to NASPO ValuePoint in many ways, MMCAP is a government program and does not have a management board in the same manner as NASPO ValuePoint. Rather, MMCAP is managed under the purview of the State's chief procurement officer and an advisory board that consists of a chairperson and eight other member representatives from among its members.<sup>(70)</sup> Four representatives are State purchasing agents and the

(64) "How NASPO ValuePoint Works", aforesaid, p. 53.

(65) *Ibid.*

(66) *A Review of Allegations Concerning Utah's Purchasing Interaction with WSCA-NASPO*, Report to the Utah Legislature, No. 2014-11, December 2014.

(67) *A Review of Allegations Concerning Utah's Purchasing Interaction with WSCA-NASPO*, *op. cit.*, p. 66.

(68) 42 CFR, § 1001, "Program Integrity – Medicare and State Health Care Programs".

(69) "What is MMCAP?", [www.infuse-mn.gov/about](http://www.infuse-mn.gov/about).

(70) *Ibid.*, p. 69.

remaining four representatives are pharmacists selected from the main practice areas participating in MMCAP.(71) The Advisory Board is elected by MMCAP members, and meets monthly to provide recommendations to MMCAP on the strategic direction of the program.(72)

Upon joining MMCAP, each State designates its contacts (one purchasing representative and one pharmacy representative) who are responsible to:

- act as liaisons between MMCAP and its members;
- provide their State a voice in MMCAP operations;
- review the membership applications and eligibility;
- assist with the solicitation strategy, content, evaluation and response (e.g., pharmaceuticals, wholesalers, and other products and programs);
- manage the State participation requirements (e.g., RFP notifications, contract awards, etc.); and
- evaluate the pharmaceutical proposals for contract awards at a National Member Conference.(73)

Unlike NASPO ValuePoint, MMCAP maintains a staff of roughly thirty individuals, including procurement experts, pharmacists, medical supply specialists, specialists in other subject matter areas, and additional staff to support its outreach and marketing efforts. All solicitations and sourcing events issued by MMCAP are pursuant to requirements under Minnesota law, but MMCAP staff work with its members to address the issues that may be unique to or required by a member in order to participate. Similar to NASPO, MMCAP uses the lead State and sourcing team models, with the State of Minnesota always serving as the lead State.

While NASPO ValuePoint is an association with State members, MMCAP is part of the State of Minnesota and formalizes its relationships with its Member States via a joint powers agreement, under the authority of Minnesota Statutes §471.59, which sets forth the nature of the obligations of the parties. Unlike the NASPO ValuePoint model where the States establish their own direct contracts with suppliers, a single contract is held by MMCAP with each vendor (wholesalers, manufacturers, and other providers) under the MMCAP model. Each MMCAP master contract is then modified to add the needed State member requirements, similar to those that might have been added to a Participating Addendum under the NASPO model.(74) The practicality of this model means fewer variations and a simpler process for vendors, but increased

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(71) *Ibid.*

(72) "Advisory Board", [www.infuse-mn.gov/networks/advisory-board](http://www.infuse-mn.gov/networks/advisory-board).

(73) "MMCAP Government Serving Government presentation" (November 2014), [www.infuse-mn.gov](http://www.infuse-mn.gov).

(74) "Membership Application", [www.infuse-mn.gov/membershipapp](http://www.infuse-mn.gov/membershipapp).

work for the cooperative entity. This model is successful largely because of the MMCAP's staff hands-on management of the contracts, which allows for the needed level of interaction and oversight.

Finally, in order to comply with federal safe harbor provisions, something unique to the pharmaceutical industry, MMCAP requires each facility that purchases from its contracts to complete an application and enter into a member participation agreement (MPA), which among other items, notifies the facilities of the administrative fee funding model used by MMCAP.<sup>(75)</sup>

To fund its operation, MMCAP does not receive funding directly from the State of Minnesota or from any government source and does not collect a membership fee. Rather, MMCAP collects an administrative fee from the manufacturers and wholesalers that provide the products to their members, in much the same manner as NASPO ValuePoint.<sup>(76)</sup> However, as a governmental entity, MMCAP uses the collected administrative fees to fund its operations, and returns unused vendor fees to its members' facilities, on a proportional basis to the amount spent by each, in the form of a wholesaler credit.<sup>(77)</sup>

### 5.5. Common Characteristics and Ranges

There are a number of common characteristics among the previously discussed cooperatives. First, the participation in these cooperatives is voluntary; that is, the participating entities may choose to purchase from an available cooperative contract, elect to purchase from their own contracts or conduct their own solicitations, or may seek to purchase from another cooperative. They have the ability to look to multiple contracts for the best pricing and terms, a choice sometimes called 'cherry-picking'.

Second, each cooperative presents a model where time and resources are traded for the benefit of consolidated buying power, taxpayer savings, and simplicity for down-stream entities. For example, in the lead State model presented by NASPO ValuePoint, there is less effort on the part of the participants (entering into a participating agreement) and significant work for the lead State (solicitation, evaluation, contracting and a participating *addendum*). Each of these cooperatives also sits on the spectrum of formality, piggy-backing, and third-party aggregation, as discussed above. If we look at each of these factors on a spectrum, as a means of comparison, we find that the GSA Cooperative Purchasing Program placed low on the spectrum for formality, while the MMCAP and NASPO models both placed relatively high on the same formality spectrum.

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(75) Safe Harbor Regulations, 42 CFR, § 1001.952, 2011.

(76) "MMCAP Government Serving Government presentation", aforesaid, p. 73.

(77) *Ibid.*

While formality is relatively easy to quantify and chart, piggy-backing and third-party aggregation are more difficult to quantify. We can analyze piggy-backing on the basis of whether it is permissible, permissible but limited, silent, or prohibited. The difficulty, however, is in determining which level of transparency, advertising, and solicitation notice is sufficient to qualify in each category. Third-party aggregation is more binary, turning on the basis of whether the contracts are for primary use by the contracting party, or primarily for the use of the members of the cooperative; that said, some grey area may exist, and some cooperative arrangements that are nominally ‘formal’ or ‘pure’ in practice may be heavily used by third parties.

### ***6. Deciding to Participate in Cooperative Purchasing***

In a 2016 survey, NASPO reported an across-the-board increase in the use of cooperative contracting, as compared to its use in 2015,(78) e.g., the number of States actively using a NASPO ValuePoint contract increased during this time period from 33 to 46, and GSA MAS contract use increased from 19 States to 29 States).(79) The 2018 NASPO Survey showed that cooperative purchasing is becoming ‘increasingly popular’ (*i.e.*, the number of participating States actively using NASPO ValuePoint contracts were increased to 48, including Member States and the District of Columbia) with an overwhelming increase on the use of NASPO ValuePoint Cooperative contracts (100%), MMCAP (23%), and other cooperative purchasing organization contracts such as the National Joint Powers Alliance (NJPA) (1%) and U.S. Communities (10%) compared to the 2016 result.(80) Interestingly, however, the same is not true on the State use of GSA schedules (*i.e.*, with a 10% decrease on State use from 79% in 2016 to 69% in 2018).(81) Nonetheless, these advances appear to speak to the staying power of and increased reliance on cooperative purchasing. While cooperative purchasing continues to grow, at nearly all levels of government, it does so with an increased visibility, which may also lead to an increased criticism.

Ease of use is a primary appeal for cooperative purchasing at all levels of government and is often cited as a reason for using a contract available through a cooperative. In addition to ease of use, cooperative purchasing participants also value fair and open competition, contract monitoring, aggressive negotiations, ability to participate in the process, and the capacity to include their specific legal terms and conditions. Public entities also look to the pooling of

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(78) NASPO, *2016 Survey of State Procurement Practices*, *op. cit.*, p. 14.

(79) *Ibid.*

(80) NASPO, *2018 Survey of State Procurement Practices, Executive Summary*, *op. cit.*, p. 11.

(81) *Ibid.*

resources, avoidance of redundancy, and improved services to contract users. Conversely, there is a concern raised by some that cooperatives cannot be used effectively for indefinite quantity contracts, and are too permissive of piggy-backing, which may allow users to bypass best practices on fair and open competition and transparency. This is by no means a complete list of the pros and cons of cooperative purchasing, but merely a starting point for discussion.

### 6.1. Moving forward with cooperative purchasing

A meaningful consideration of the benefits and detriments of cooperative purchasing is necessary for any governmental entity prior to engagement; this process should occur before a need arises to access a cooperative contract, so as to not blur the criticality of the need with the judgment of whether to proceed. Indeed, a number of aspects should be evaluated in considering whether cooperative purchasing is the proper path for a governmental entity.

#### 6.1.1. Quantity and pricing considerations

In the realm of public procurement, there are things that we solicit for use based on a more immediate need, and things we solicit based on a future need. A procurement office may solicit for supplies, knowing the typical need and identifying a date range for ordering and delivery for what is, at the time of contract award, a still indefinite quantity of supplies. These are known as ‘framework agreements’ or ‘catalogue contracts’ internationally. The U.S. federal government refers to these as indefinite delivery/indefinite quantity (IDIQ) contracts.<sup>(82)</sup> In this instance, the procuring entity may not know the quantity of goods or service that it may need, or when they are likely to be needed, nonetheless, it establishes a master contract to ensure the availability of a contracting vehicle for purchase once the need is identified.

Problematically, as any seller of goods and services will tell you, “one in the hand is worth two in the bush”. In practice, this means that pricing of an item for sale, when based on an actual sale, arguably will result in better pricing than that provided in response to an IDIQ solicitation with no promise of purchase. This issue can be mitigated by providing in the solicitation typical spend volumes for the participating entities. However, this does not take into account piggy-backing, which may drive up the overall volume, and which may be difficult for the seller to account for in setting prices. Conversely, as the use of a cooperative vehicle is typically voluntary and governmental entities are free to cherry-pick (select to purchase goods from a number of sources depending on which provided the best price for each product line),

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(82) Federal Acquisition Regulation (FAR), 48 CFR, § 16.504(a).

vendors may be hesitant to rely on past volumes as an indication of future opportunity.

Nonetheless, governmental entities, particularly those leading the cooperative vehicle for the goods or services at issue, have the ability to conduct objective price comparisons, comparing (on either a product-specific or an overall offering basis) what is otherwise available in the marketplace. Users can at the very least conduct a comparison to determine whether the pricing is competitive, whatever the basis is for that pricing. In this same vein, lead States are able to standardize product lines, driving spend to a particular product or manufacturer as opposed to providing options and watering down volume. For example, purchasing 100 widgets from one manufacturer is apt to result in better pricing than that offered by one of four manufacturers each selling 25 widgets.

#### 6.1.2. Meeting fair and open competition requirements

The procurement process as a whole is often viewed with skepticism, in part because the public sees only the solicitation and then the result, but not the process under which the decisions are reached. To that end, and as a means of quelling public skepticism within its borders, a governmental entity's participation in the cooperative purchasing process, specifically in the solicitation and evaluation process, is the best assurance. In the absence of that participation, and in order to ensure that its own legal requirements for fair and open competition are met, the governmental entity that plans to use a cooperative vehicle must evaluate how broadly the solicitation was posted and advertised, and whether that entity's other legal requirements are met. It should also be noted, from a transparency and accountability perspective, that nearly all data collected (including solicitations, vendor responses, cost, and evaluations) should become public no later than the time of contract award, to allow those that would wish to challenge the outcome to do so. Another question then to be resolved is whether the transparency practices of the lead entity are sufficient to meet the requirements of the participating entity.

As discussed earlier, potential participating governmental entities ideally should be named in the solicitation, the solicitation should be published in their States, they should participate in the evaluation process, and they should (if possible) review and approve the final contract. The absence of one or more of these safeguards, without regard for whether they are legally required, is a common concern among those critical of cooperative purchasing and the widespread use of permitted piggy-backing. As each State has its own set of requirements, the perceived lack of transparency and fair and open competition when

engaging in piggy-backing can lead to procurement protests and legal challenges to the governmental entity's legal authority.(83)

### 6.1.3. Legal compliance

Among the numerous complexities related to procurement and contracting endeavors involving multiple States and local government,(84) one of the most significant issues stems from the differences found in the procurement laws of the participating entities. These differences cut across not only geographic State boundaries, but are found among the various levels of government within each State. Suffice it to say, the publication and notice requirements may vary greatly, not only on a state-by-state basis, but also between State and local governments. For example, in the State of Minnesota, while the State must competitively bid all contracts over \$5,000, this is not the case at the city level where competitive bidding typically is not required unless the contract exceeds \$100,000.(85) This raises a potential concern regarding whether the procurement requirements of one governmental entity are sufficient for use by another governmental entity, particularly between governmental entities at different levels, in the context of cooperative purchasing. While the lead State in a cooperative purchase works diligently to ensure that the needs of those identified for participation are met, the entities that will later join via piggy-backing are not necessarily represented, and cannot be guaranteed that the cooperative contract meets their legal and procurement requirements absent adequate due diligence.

These variations create complexity not only at the time of sourcing, but also when contracting and managing contracts. The difficulty in managing cooperative contracts can be seen through the differing approaches of NASPO ValuePoint and MMCAP, as discussed prior. The complexity in each variation turns on the number of governmental entities involved, the diversity and sheer number of vendors, and the terms that apply uniquely to each vendor and governmental entity through a participating addendum or amendment to the master contract. While formality of process, proper support, and communication are some of the keys to address this challenge, still, the larger the cooperative and the more entities are involved, the greater the challenge.

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(83) For an example, *see* "In Re New Jersey State Contract", 28 A.3d 816, 2011.

(84) For an example, *see* P. THOMPSON, "Municipal Cooperative Purchasing Arrangements in Home Rule States: The Maine Example", *American Bar Association, 54-Fall Procurement Law*, 8, 2018. (Home rule, *i.e.*, the degree of autonomy municipalities, has been granted by the State constitution or the legislature to enact laws and policies to govern their local affairs, has made it more difficult for the nearly 500 municipalities and towns in the State of Maine to implement cooperative purchasing to control the cost of local government services.)

(85) League of Minnesota Cities, "Information Memo on Competitive Bidding Requirements in Cities", 2015.

#### 6.1.4. Equality and sustainability – A case for balance

How a government chooses to spend its money often takes into account more considerations than need, want, and cost. The ability of a government to promote social objectives, e.g., small business, minority-owned business opportunities, environmental considerations, and accessibility, is often done through public procurement, with the spending of the governmental entity ostensibly used to promote social change. When leveraging social interests, (e.g. environmental sustainability in a cooperative purchasing solicitation and resulting contracts), the impact felt reaches far beyond that of the lead State. Particularly, where the governmental entity leading the procurement alone has insufficient power to move the market to meet its goals, its leadership in a cooperative's solicitation permits that entity to speak for the buying power of the cooperative as a whole. This is likely to continue, as we see an increasing trend in sustainability in State contracts, green purchasing policies, and executive orders mandating sustainability initiatives.<sup>(86)</sup>

While we can look at the positive attributes of aligning social goals, leveraging buying power, and other benefits that stem from cooperative purchasing, we should also look at its potential costs. One primary cost is cooperative purchasing's potential negative impact on local vendors and markets, which can be at odds with requirements for local and small business participation, including (among others) the participation of minority, women, persons with disabilities, and veteran-owned businesses. Those engaged in cooperative purchasing must balance their interests in social outcomes and local businesses, against the need for low prices and efficiency. Conversely, however, cooperative purchasing also can make it possible to purchase sustainable products directly, from a more diverse vendor base.

### 6.2. Keys to success

With the balancing of interests in mind, successful cooperative purchasing begins with the selection of an appropriate commodity or service.<sup>(87)</sup> The subject of the solicitation must have a wide geographic availability and an adequate distribution channels to meet the needs of the members of the cooperative. The selection of goods or services that are too specific or lack proper distribution channels results in lower use and diminishing returns from the cooperative contract. This is where the cooperative entity must listen and pay heed to its members, and give them a meaningful voice to ensure that the cooperative reflects the needs and requirements of its members.

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(86) NASPO, *2018 Survey of State Procurement Practices, Summary Report*, *op. cit.*, p. 11.

(87) E. HAYES, "An Introduction to Cooperative Purchasing", *op. cit.*, p. 3.

Assuming that an appropriate commodity or service is selected by the cooperative entity, the next step is ensuring that the lead entity can allocate sufficient resources to the program, both in terms of labor force and expertise.<sup>(88)</sup> This ties back to one of the requirements in the selection of the goods or services; that is, whatever is selected as the subject of the contracts, it is necessary that the team that is assigned to implement the contract has the proper expertise on the nature of the goods or services to be procured, and the most advantageous means of soliciting, evaluating, and contracting for those goods or services. Assuming that the proper resources and expertise have been committed, a critical next step for those resources is obtaining vendor acquiescence to the proposed acquisition strategy.<sup>(89)</sup> This is often challenging in the context of fair and open competition, as procurement professionals must avoid any appearance of preference or collusion when discussing their needs with vendors in a pre-solicitation context. However, a solicitation which deters vendors from replying, or a situation in which potential vendors do not understand the nature of the cooperative, may result in a poor outcome for all involved; arguably, less competition results in a decreased ability to obtain competitive pricing and terms.

Finally, once the contract is in place, proactive and aggressive contract management, not only by the lead State but also by the participating entities, is critical.<sup>(90)</sup> The failure to manage a large cooperative contract(s) and to provide the needed levels of oversight give the vendors a burden to self-regulate. Without suggesting any negative or malicious intent, the vendors should not be allowed in a public procurement arena to act without the proper oversight by those responsible for the expenditure of public funds. To assist the participating entities in this needed oversight, the process for contracting and contracting management must be simplified to the greatest extent possible. There must be a direct access by each participating entity to manage its day-to-day interactions with the vendor, in concert with the ability of the lead State to step in and escalate at a master contract level when needed.

### 6.3. Additional considerations

Cooperative purchasing presents a complex tapestry of issues, from legal compliance to fair and open competition, from pricing to piggy-backing, and from local to federal levels. Again, we return to the notions of fair and open competition, transparency, and accountability. Acknowledging the concerns related to local vendors and cooperative purchasing, buyers within the

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(88) *Ibid.*

(89) *Ibid.*

(90) *Ibid.*

governmental entity purchasing from a cooperative contract must evaluate the prevalence of local and regional vendors and their ability to compete with cooperative vendors to meet the needs of the purchasing entity. One suggestion that has been put forward is the issuance of a secondary solicitation as a means of promoting fair and open competition within a cooperative purchasing context.<sup>(91)</sup> This type of issuance could result in the creation of additional competition at the time of purchasing. This idea can also be broadened by opening the secondary solicitation to quotes from non-cooperative contracts, regional and local vendors, and others, with the purpose of establishing best value (or perhaps low cost). This would allow the governmental entity to make its purchase knowing that it has achieved the best value or lowest cost available at that point in time, be it from the cooperative vehicle or elsewhere. A secondary solicitation could also alleviate many of the concerns related to local and small businesses, Indefinite Delivery, Indefinite Quantity (IDIQ)<sup>(92)</sup> contracts and their lack of competitive pricing, and bolster transparency in the purchasing process. However, the issuance of a secondary solicitation, with all of the benefits, adds time, expense, and complexity to the process of purchasing from a Master Contract, which are the very things a cooperative purchasing Master Contract seeks to reduce for the purchasing entity. How then should we navigate these competing interests to achieve the proverbial best of both worlds?

An often uncited, unrecognized key to fair and open competition is the nature and composition of the public procurement staff. Where dedication to fair and open competition and transparency in the process is part of the cultural landscape, and supported by leadership despite political considerations, public procurement thrives. That is to say, when the right people do the right things, the process works. Problematically, when a key factor is discretion, there is also a great opportunity for things to go astray. There is no magic to the decision of whether or not to engage a secondary solicitation. The first step, however, is to examine the extent to which price negotiations were conducted, and prices were determined to be competitive in the marketplace. When in doubt, a secondary solicitation (which adds a layer of competition) may provide for greater confidence. In the absence of a secondary solicitation, publication of the governmental entity's desire to purchase from a cooperative contract may, at the least, provide for greater transparency. The application of these strategies must be considered and evaluated in the context of the overall needs and resources of the governmental entity.

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(91) J.E. NELSON and J.A. LoBosco, "Understanding the WSCA-NASPO Cooperative Purchasing Organization: It's Time to Invite the Elephant Out of the Corner", *op. cit.*, p. 49.

(92) General Services Administration, "Indefinite Delivery, Indefinite Quantity Contracts", in [www.gsa.gov](http://www.gsa.gov).

## ***7. Conclusion***

Cooperative purchasing provides opportunities for federal, State, and local governments, from the very large to the very small, to consolidate spend, and reduce the overall effort, which should result in enormous benefits not only for the government but also for its selected vendors. At the same time, the governmental entities that are engaged in cooperative purchasing must balance their interests with those of the public and the broader vendor communities. This is a tall order that the cooperative purchasing entities must not take lightly. When done well, cooperative purchasing provides for an efficient, considerate, and legally defensible means of purchasing goods and services. As a caveat, with the use of cooperative purchasing continuing to grow, dedication to the principles of fair and open competition, transparency, and accountability will be increasingly critical not only to its degree of success, but also to its literal survival.



## CHAPTER 3

### European Joint Cross-border Procurement and Innovation

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#### *1. The Challenges for Cross-border Procurement*

Arguably, European integration in the procurement sector is still a challenge. More than forty years of Procurement Directives have not yet succeeded in opening the internal procurement market. Many of the reasons are well-known: the initially limited scope of the Directives, and the varied implementations in different national procurement systems, which raise legal barriers and exacerbate language barriers. Integrity issues must also be addressed.<sup>(1)</sup> All these factors help explain the reluctance of suppliers to cross the national borders, and buyers' inclination to maintain their nationally based supply chains.

The Directives seem to have done better at opening national markets compared to even more fragmented markets at regional and local levels. The development of electronic means for a fully digital transition has also logged behind. Nonetheless, significant changes are coming rapidly and the developments across the Atlantic make the trajectory of those changes clearer. Technologies and joint procurement have radically changed the procurement sector as we know it. The burdens of a traditional paper based award of a single contract for a single procuring entity seem to be rapidly receding.

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(1) R. CAVALLO PERIN and G. M. RACCA, "Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process", in *The Changing Administrative Law* (D. SORACE and L. FERRARA eds.), Giappichelli, Springer, 2019, forthcoming; Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally (G. M. RACCA and C. R. YUKINS eds), in *Droit Administratif/Administrative Law Collection* (J.-B. Auby dir.), Bruylant, Bruxelles, 2014.

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Public purchasing power seems to have become a lever of industrial policy as Europe moves to support integration through the growth of SMEs, sustainability and innovation. From the other side of the Atlantic, more pragmatically procurement is used as a lever for gaining more efficiency and savings, including across borders, but without Europe's market integration goals.

From this perspective it is easier to understand the differing approaches to joint cross-border procurement in the EU and in the United States.

Given the integration imperative in the European Union, it is important to highlight the critical issues that have emerged in the European experience. Administrative cooperation seems to be a strategic necessity for the ongoing European integration to develop shared knowledge and capacities on a voluntary basis of shared public interest. This will also allow European governments to pursue increasingly efficient, innovative, and high quality goods and services. An analysis of different ways to set agreements to reconcile differing goals and provisions may also provide useful ideas to share across the Atlantic.

Developing transparent and efficient procurement systems appears to be a shared goal. Nonetheless, the real challenge is implementing them through the most advanced technologies so as to ensure that public purchasing power is steered toward benefiting citizens across the EU Member States.

## **2. The European Administrative Cooperation among Public Administrations**

Over the last decades the relationships among the EU Member States' administrations have been favored by the application of some key principles, such as those of sincere cooperation and of mutual recognition.<sup>(2)</sup> Yet, a prominent role has also been played by more recent provisions on administrative cooperation.<sup>(3)</sup> Administrative cooperation represents a significant

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(2) K. A. ARMSTRONG, 'Mutual recognition', in C. BARNARD and J. SCOTT, *The Law of the Single European Market: Unpacking the premises*, Hart Publishing, Oxford and Portland, Oregon, 2002, 231; M. LOTTINI, 'From 'Administrative Cooperation' in the Application of European Union Law to 'Administrative Cooperation' in the Protection of European Rights and Liberties', in *European Review of Public Law*, 2012, 131; D. U. GALETTA, 'Coamministrazione, reti di amministrazioni, Verwaltungsverbund: modelli organizzativi nuovi o alternative semantiche alla nozione di 'cooperazione amministrativa' dell'art. 10 TCE, per definire il fenomeno dell'amministrazione intrecciata?', in *L'interesse pubblico tra politica e amministrazione* (A. CONTIERI, F. FRANCIOSI, M. IMMORDINO, and A. ZITO eds), ESI, 2010, I, 191. E.C.J. 10 February 2000, FTS, C-202/97, *Fitzwilliam Executive Search Ltd v. Bestuur van het Landelijk instituut sociale verzekeringen*; E.C.J. Presidential ordinance, 19 April 2005, C-521/2004, *Tillack v. EC Commission*.

(3) Arts. 6, 74-76 and 197, Treaty on the Functioning of the European Union (hereinafter also referred to as 'TFEU'); M. P. CHITI, 'Introduzione. Lo spazio amministrativo europeo', in *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds), Il Mulino, Bologna, 2012, 19.

challenge for European public administrations.(4) That is because it is one of the recent areas of competence of the European Union, together with protection and improvement of human health, industry, culture, tourism, education, vocational training, youth and sport.(5) Such competences are defined as ‘supporting competences’ related to areas where the European Union has already intervened by means of cross-cutting policies.

The European Union's general competence on administrative cooperation ‘shall [...] be without prejudice to other provisions of the Treaties providing for administrative cooperation among Member States, and also between Member States and the Union’.(6) That objective envisages customs cooperation.(7) It also envisages coordination and cooperation between police, judicial and other competent authorities as well as the recognition of judgments in criminal matters.(8) Also in the scope of administrative cooperation is the creation of an area of freedom, security and justice with respect for fundamental rights. All this, however, safeguarding the peculiarities of the different jurisdictions and different legal traditions of the Member States.(9)

In these areas, national laws are not required to be harmonized. Nonetheless, supporting Member States’ direct actions in such areas become essential to support, develop, and ultimately coordinate an integrated network of the national public administrations among the Union.

A lack of professionalism and capacity causes shortcomings in correctly performing public activities, though.(10) Professionalism arguably is the essential prerequisite for a structural reorganization and allocation of functions, including cooperation among European administrations.(11) Indeed, the development of professionalism is needed to prevent that the ‘substantial

(4) Arts. 6 and 197, TFEU.

(5) Art. 6, TFEU.

(6) Art. 197(3), TFEU.

(7) Art. 33, TFEU: ‘Within the scope of application of the Treaties, the European Parliament and the Council, acting in accordance with the ordinary legislative procedure, shall take measures in order to strengthen customs cooperation between Member States and between the latter and the Commission’.

(8) Art. 82, TFEU. See E. SELVAGGI, *Rapporti per la cooperazione penale fra Stati, Osservazioni a CGUE, 16 luglio 2015, n. 237*, in *Cass. Pen.*, 2015, 3800B; F. SPIEZIA, *La proposta di regolamento del 17 luglio 2013 per la creazione dell'agenzia dell'unione europea per la cooperazione giudiziaria penale. Lo stato dei negoziati e le prospettive per il futuro di Eurojust*, in *Cass. Pen.*, 2015, 1614C.

(9) Art. 67, TFEU. See also art. 87 TFEU, where it is affirmed that ‘The Union shall establish police cooperation involving all the Member States’ competent authorities, including police, customs and other specialised law enforcement services in relation to the prevention, detection and investigation of criminal offences’. F. LAFARGE, *Administrative Cooperation between Member States and Implementation of EU Law*, in *European Public Law*, 2010, p. 600 et seq.; *The Internal Market after 1992. Meeting the Challenge. Report to the EEC Commission by the High Level Group on the Operation of the Internal Market*, op. cit.

(10) In Italy the principle of adequacy is set out in the Constitution, art. 118(1).

(11) See: EU Commission, *Making Public Procurement work in and for Europe*, COM(2017) 572 final, October 2017; ID. *Europe 2020 A strategy for smart, sustainable and inclusive growth*, COM(2010) 2020 final, March 2010. See: P. T. MCKEEN, ‘The importance of a professionally educated public procurement workforce: lessons learned from the U.S. experience’, in *Integrity and Efficiency in Sustainable Public*

ineffectiveness – even if not formal – of European law’ may result in inefficiencies within administrative structures, which would result in ‘asymmetry’ in the implementation of the European law.(12)

Arguably, professionally adequate organizations, capable of pursuing public interests and ensuring the effectiveness of public authorities, are therefore needed.(13)

The introduction of new European institutions and new levels of governance requires a redefinition in the competences of the different institutions at all levels in the ‘European administrative space’.(14) The objectives are, notably, to support ‘integration between national administrations and with the EU institutions which, while respecting national autonomy’, pursue integrated administration models ‘having the effect of defining common principles’, while also favoring the possible convergence of organizational models.(15)

An ‘open, efficient and independent’ European administration, which is gradually going to be established, should progress in ensuring the right to good administration enshrined in the Charter of Fundamental Rights, also in order to foster the idea of ‘administrative citizenship’.(16)

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*Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (G. M. RACCA and C. R. YUKINS eds), *op. cit.*, 319.

(12) D. SORACE, ‘Una nuova base costituzionale europea per la pubblica amministrazione’, in *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona*, (M. P. CHITI and A. NATALINI eds.) *cit.*, 82.

(13) On the forms of cooperation allowing the application of the EU law and related policies see H. C. H. HOFMANN, *Mapping the European administrative space*, in *West European Politics*, 2008, 31. On the public procurement sector, see G. M. RACCA, ‘Collaborative procurement and contract performance in the Italian healthcare sector: illustration of a common problem in European procurement’, in *Public Procurement Law Review*, 3, 2010, 119-133.

(14) R. CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, *cit.* See also M. P. CHITI, *Lo spazio amministrativo europeo*, in *Studi in Onore di Alberto Romano*, Editrice Scientifica, Napoli, 2011, 163; *Id.*, *Introduzione. Lo Spazio amministrativo europeo*, in *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds.), *cit.*, 19.

(15) See A. H. TURK, ‘Judicial Review of Integrated Administration in the Eu’, in *Legal Challenges in Eu Administrative Law* (H.C.H. HOFMANN and A.H. TURK eds.), Cheltenham, Edward Elgar, 2009), 218. See also D. DEIRDRE CURTIN, ‘Holding (Quasi-)Autonomous EU Administrative Actors to Public Account’, in *European Law Journal*, Vol. 13, 4, July 2007, 523-541.

(16) R. CAVALLO PERIN, ‘La configurazione della cittadinanza amministrativa’, in *Dir. Amm.*, 2004, 201-208; J. SCHWARZE, ‘European Administrative Law in the Light of the Treaty of Lisbon’, in *European Public Law*, 2012, 297-298; EU Parliament, *Towards an EU Regulation on Administrative Procedure?*, 2010. Art. 41, Charter of Fundamental Rights of the European Union, codifies the principle of good administration (J. SCHWARZE, *ibidem*, 298). According to the jurisprudence of the European Court of Justice (hereinafter referred as to ‘ECJ’) the right to a good administration ‘is one of the general principles of the rule of law common to the constitutional traditions of the Member States [and in which they find expression rights such as the] right of diligent and impartial treatment of a complaint’ (ECJ, 30 January 2002, case T-54/99 *Max.Mobil v. Commission* *Racc.* II-313, par. 48 and 49). Those rights are enshrined in the law even before the entry into force of the Charter (ECJ, 18 September 1992, T-24/90, *Automec v. Commission*, *Racc.* II-2223, § 79, 15 September 1998, T-95/96, *Gestevisión Telecinco v. Commission*, *Racc.* II-3407, § 53). See also ECJ, 22 February 2005,

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Direct interventions in the European Union on administrative cooperation were traditionally limited by the principles of subsidiarity and proportionality.<sup>(17)</sup> Administrative cooperation may advance through European interventions to support Member States' administrations in order to increase the 'administrative capacity to implement Union law' for specific purposes.<sup>(18)</sup> Its effectiveness becomes a matter of public interest.<sup>(19)</sup> Administrative cooperation thus becomes an essential tool for the proper functioning of the European Union to the benefit of EU citizens.<sup>(20)</sup>

Strengthening 'cooperation' amongst public administrations is essential to ensure the effectiveness of European Union law and its national

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C-141/02, *Commission v. Max.Mobil*, Racc. I-1283, par. 72; E. NIETO-GARRIDO, I. M. DELGADO, *European Administrative Law in the Constitutional Treaty*, Oxford 2007, 26; K. LENAERTS, "In the Union we trust": Trust-enhancing principles of Community law', in *Common Market Law Review*, Issue 2, 2004, 317 – 343; I. RABINOVICI, *The Right to Be Heard in the Charter of Fundamental Rights of the European Union*, in *European Public Law* 18, n. 1, 2012, 149; M. TRIMARCHI, 'L'art. 41 della Carta europea dei Diritti Fondamentali e la disciplina dell'attività amministrativa in Italia', in *Dir. Amm.*, 2011, 537; J. PONCE SOLÈ, EU Law, 'Global Law and the Right to Good Administration', in *Global Administrative Law and EU Administrative Law. Relationships, Legal Issues and Comparison* (E. CHITI and B. G. MATTARELLA eds.), 2011, Part 2, 133; M. CARTABIA, 'I diritti fondamentali in Europa dopo Lisbona: verso nuovi equilibri?', in *Giorn. Dir. Amm.*, no. 3/2010, 221; D.U. GALETTA, 'Diritto ad una buona amministrazione e ruolo del nostro giudice amministrativo dopo l'entrata in vigore del trattato di Lisbona', in *Dir. amm.*, 2010, 601; F. TRIMARCHI BANFI, 'Il diritto ad una buona amministrazione', in *Trattato di diritto amministrativo europeo* (M. P. CHITI and G. GRECO eds.), Milano, 2007, I, 49 - 86; E. CHITI, 'Il principio di buona amministrazione', in *Diritto amministrativo europeo – Casi e materiali* (E. CHITI, C. FRANCHINI, M. GNES, M. SAVINO, and M. VERONELLI eds), Milano, 2005, 3940; F. NICOLETTI, 'Il principio di "buona amministrazione" nell'Unione europea tra garanzia ed efficienza', in *Il diritto dell'economia*, n. 4/2006, 776.

(17) Treaty on European Union (hereinafter referred to as 'TEU'), art. 5; Treaty of Lisbon, annex protocol 2.

(18) Arts. 6 and 197, TFEU. See F. LAFARGE, 'Administrative Cooperation between Member States and Implementation of EU Law', in *European Review of Public Law*, 2010, 597-616, qualifies administrative cooperation as an essential element for the proper functioning of EU policies and related European legislation, particularly with regard to matters related to the internal market. Administrative cooperation is the instrument to ensure free movement of goods, persons, services and capital, and to reduce barriers between the public administrations of the States. In this context, the transition from the concept of a common market to that of the single market implies a higher level of cooperation. See Directive 2006/123/EC, 12 December 2006, on services in the internal market, which states that 'administrative cooperation is essential to make the internal market in services function properly. Lack of cooperation between Member States results in proliferation of rules applicable to service providers or duplication of controls for cross-border activities, and can also be used by rogue traders to avoid supervision or to circumvent applicable national rules on services. It is, therefore, essential to provide for clear, legally binding obligations for Member States to cooperate effectively'. See *The Internal Market after 1992. Meeting the Challenge. Report to the EEC Commission by the High Level Group on the Operation of the Internal Market*, 28 October 1992.

(19) TEU, art. 4: 'The Member States shall take any appropriate measure, general or particular, to ensure the fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the European Union'.

(20) See arts. 6 and 197, TFEU. F. CORTESE, *Il coordinamento amministrativo. Dinamiche e interpretazioni*, Milano 2011, 140; E. CHITI, 'Il Trattato di Lisbona', in *Giorn. Dir. amm.*, 2010, 221, where it is stated that art. 197 TFEU seems to be posing a new 'constitutional' attention to the issue regarding national public administrations' capacity, qualifying the effectiveness of enforcement as a question of common interest and acknowledging that it should be ensured by a system of cooperation at the EU level.

implementation, thus favoring integration among public administrations and different national legal systems.<sup>(21)</sup> Administrative cooperation, either as vertical cooperation between the European and national levels or horizontal collaboration among national administrations, is being developed as a new way of acting of the European Union. That does not limit the responsibility of the Member States. Rather, an EU internal policy requires actions being taken to ‘support, coordinate or supplement the actions of the Member States’.<sup>(22)</sup> That policy applies without prejudice to the Member States’ obligation to implement the EU law. The same can be said as far as the prerogatives and duties of the EU Commission.<sup>(23)</sup> The latter should thus support the efforts of Member States in the exercise of their functions without necessarily requiring a harmonization of the provisions among the different legal systems of Member States.<sup>(24)</sup> The aim of such a cooperation can be the creation of an integrated system of public administrations, whether national or European, aimed at promoting the wellbeing of European citizens and the enhancement of social cohesion.<sup>(25)</sup>

The “European administrative space” has developed in different sectors by identifying suitable administrative cooperation tools to define ‘integrated

(21) M. LOTTINI, ‘From “Administrative Cooperation” in the Application of European Union Law to “Administrative Cooperation” in the Protection of European Rights and Liberties’, in *European public law*, 2012, 127-147, where cooperation is considered as an integration tool, which aims to ensure the proper application of EU law and the protection provided by the ECJ.

(22) Art. 6, TFEU: ‘The Union shall have competence to carry out actions to support, coordinate or supplement the actions of the Member States. The areas of such action shall, at European level, be (a) protection and improvement of human health; (b) industry; (c) culture;(d) tourism; (e) education, vocational training, youth and sport; (f) civil protection; (g) administrative cooperation’. EU Commission, *Commission staff working paper concerning the application of EU public procurement law to relations between contracting authorities (‘public-public cooperation’)*, 4 October 2011, SEC(2011) 1169 final. See J. WIGGEN, ‘Public Procurement Law and Public-Public cooperation: reduced flexibility but greater legal certainty ahead? A note on the Commission’s Staff Working Paper on the application of EU public procurement law to relations between contracting authorities and proposal for a new directive’, in *Public Procurement Law Review*, 2012, 225-233.

(23) See art. 197(3), TFEU.

(24) F. CORTESE, ‘Gli strumenti per la cooperazione amministrativa verticale’, in Astrid Rassegna, n. 150/2012; *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds), cit., 168; J. SCHWARZE, ‘European Administrative Law in the Light of the Treaty of Lisbon’, in *European public law*, 2012, 287.

(25) M. P. CHITI, *Introduzione. Lo Spazio amministrativo europeo, Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds), cit., 19. See EU Parliament, *European administrative law in the light of the Treaty of Lisbon: introductory remarks*, 2011; ID., *Towards an EU Regulation on Administrative Procedure?*, 2010, where the convergences between the evolution of European administrative law and of the national administrative laws are highlighted. From the beginning the legal traditions of the Member States have influenced the ECJ case law in the formulation of general principles in the matter of ‘circular motion’; then, the principles of law established by the ECJ have influenced the administrative law of the Member States and, increasingly, the European legislation and secondary sources, at times pushing Member States to change their internal administrative laws in compliance with European standards even in areas outside the Union’s competence.

administrations' models.(26) These can favour the effectiveness of the internal market and competition among economic operators, both of which are fundamental goals (in view of a European administrative citizenship), particularly in the public contracts and services sectors.(27)

The wording 'to supplement the actions of the Member States' can be interpreted as an effort to create a system of reciprocal interaction among administrations within a European framework that may develop common experiences and principles in the implementation of EU provisions in different sectors. The same applies to procurement related to works, goods and services.(28) Indeed, further provisions for the development of such cooperation have been introduced in the last EU Directives on public procurement.(29) Such cooperation might significantly innovate organizational models pursuing the most efficient solutions in the procurement sector.(30) As the integration process is notably asymmetric, it should be observed that such differences are inevitable and that only more advanced experiences may drive future changes in the long run.(31)

Such forms of cooperation are of 'common interest' to the Member States for the purpose of adapting the peculiarities of the national legal systems to the common goals of development and enlarging participation in the public

(26) H. C. H. HOFMANN, *Mapping the European administrative space*, in *West European Politics*, cit., 665 - 668.

(27) A. ROMANO TASSONE, 'I "diritti" tra ordinamento interno ed ordinamento comunitario', in *Diritto e processo amministrativo*, 2008, 112. J. SCHWARZE, *European Administrative Law in the Light of the Treaty of Lisbon*, cit., 298 - 299, where it is clarified that the choice of founding 'European administrative law' on the concept of rule of law has made it possible to define the development of the protection of fundamental rights, including the right to good administration (Charter of Fundamental Rights of the European Union, art. 41) and the right of access to documents (Charter of fundamental rights of the European Union, art. 42). F. BASSANINI, 'Prefazione', in *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds), cit., 16.

(28) Art. 6, TFEU; in addition to arts. 114-117 TFEU.

(29) Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts; 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 (hereinafter collectively referred to as 'Procurement Directives'; for clarity purposes, the terms 'Procurement Directive' and 'Directive' refers only to Directive 2014/24/EU).

(30) Art. 298, TFEU: '1. In carrying out their missions, the institutions, bodies, offices and agencies of the Union shall have the support of an open, efficient and independent European administration.2. In compliance with the Staff Regulations and the Conditions of Employment adopted on the basis of Article 336, the European Parliament and the Council, acting by means of regulations in accordance with the ordinary legislative procedure, shall establish provisions to that end'. P. CRAIG, *A General Law on Administrative Procedure, Legislative Competence and Judicial Competence*, *European Review of Public Law*, 2013, 503, where the legitimacy of the European institutions to adopt a general regulation on administrative procedure is brought back to the rules of the Treaty, which expressly confers the regulatory power in certain sectors: telecommunications, waste management, and protection of competition.

(31) R. CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, cit.

procurement market.<sup>(32)</sup> That is particularly true considering that the competitiveness of European countries also depends on the performance of their public administrations and the quality of the services they assure to citizens and companies. Therefore, the intervention of the European institutions should be aimed at completing national actions so as to ensure 'European quality services' to citizens, with the aim of fulfilling the social goals of the Treaties.<sup>(33)</sup>

Another area of interest might be the special provisions of the TFEU on cooperation in tax and civil matters.<sup>(34)</sup> These provisions may in fact favour the harmonization of national legislations in order to guarantee 'the establishment and functioning of the internal market and to avoid distortions of competition'<sup>(35)</sup>, especially in the procurement sector, from the definition of needs to the award and execution of public contracts. Cooperation among contracting authorities may become an effective tool to spur the single market of public procurement so as to develop new award and execution procedures, which will inevitably tend to integrate and harmonize the practice and acts of the administrations involved. Effects of such harmonization may be also viewed from the supply-side perspective, as simplification of the participation of EU suppliers, including SMEs, award procedures, which might lead to further growth and quality of procurement.

The Treaty fosters actions aimed at promoting 'the exchange of information and public officials' while 'supporting training programs' to overcome inadequate systems that are inefficient and unable to properly implement the

(32) D. U. GALETTA, 'Coamministrazione, reti di amministrazioni, Verwaltungsverbund: modelli organizzativi nuovi o alternative semantiche alla nozione di «cooperazione amministrativa» dell'art. 10 Tee, per definire il fenomeno dell'amministrazione intrecciata?', in *Riv. it. dir. pubbl. com.*, 2009, 1689; M. P. CHITI, *A rigid Constitution for a flexible Administration*, in *European Review of Public Law*, 2004, 175.

(33) D. U. GALETTA, *L'autonomia procedurale degli Stati membri dell'Unione europea: «Paradise Lost?»*, Torino, Giappichelli, 2009; M. P. CHITI, 'Lo spazio amministrativo europeo. Introduzione', in *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds), cit., 26 - 27. See: J. SCHWARZE, *European Administrative Law in the Light of the Treaty of Lisbon*, in *European Public Law*, 2012, 294, where the 'voluntary' nature of cooperation is highlighted, as governed by art. 197 TFEU where the European Union action is used to support the Member States in order to 'improve their administrative capacity to implement Union law' (TFEU art. 197(2)) helping to ensure their effectiveness.

(34) Arts. 113 and 115, TFEU; Directive 2011/16/EU, 15 February 2011, on the obligations of national authorities to send information to the competent authorities of the other Member States. Art. 81, TFEU, where it is provided that 'The Union shall develop judicial cooperation in civil matters having cross-border implications, based on the principle of mutual recognition of judgments and of decisions in extrajudicial cases. Such cooperation may include the adoption of measures for the approximation of the laws and regulations of the Member States'.

(35) Art. 113, TFEU. F. LAFARGE, *Administrative Cooperation between Member States and Implementation of EU Law*, cit., 602 - 611, where a distinction is made between the duties of cooperation provided for by the EU legal framework (art. 33, TFEU, in the field of customs cooperation; art. 46(a), TFEU, in the field of free movement of workers; art. 74, TFEU, in the field of an area of freedom, security and justice; art. 81, TFEU, in the field of judicial cooperation on civil matters) and optional tools aimed to favour cooperation.

EU law and to meet the needs of the communities.(36) The EU Cooperation in public officials' training leads to the dissemination of best practices and information for the pursuit of the effectiveness of European law as a common goal.(37) All this is beyond, even, the effects of legislative harmonization.(38)

Cooperation and networking strategies among European public administrations involve an inevitable comparison among the services rendered by national administrations (benchmarking) and the circulation of best procurement strategies and practices. Thus, it may be possible to develop qualitative performance standards (minimum and uniform), supranational parameters and the definition of European indicators, levels of performance, and the accountability of public administrations in the implementation of 'the right to good administration'.(39)

Cooperation provides a balance between the exercise of economic freedom and the principle of solidarity, with an effective implementation of social rights, already recognized in the Member States legal orders. As a result, it pursues an effective social and economic cohesion. In addition to that, it may encourage the development of European public services, mainly through horizontal cooperation among public administrations. The implementation of the European administrative space may bring a progressive overlap with the organizational, administrative, and judicial autonomy of legal entities, as defined by national legislation. From this perspective, horizontal cooperation

(36) Art. 197(2), TFEU, with regulations approved by the Parliament and Council.

(37) See, by way of example, the Austrian Public Procurement Excellence Programme (PPE), which is the first European training program dedicated to CPBs professionals only. It is an EU-funded specialised training programme to provide public procurement practitioners with the core knowledge, skills and methods of modern public procurement. Among the forms of cooperation in the training of public officials in Europe, we should note the European Institute of Public Administration (EIPA) which, through a network among public administrations (European, national and local), offers integrated training with activities of research and applied consultancy. Another example is the European Public Administration Network (EUPAN), which is a type of informal cooperation among the public administration ministers of the Member States, the EU Commission and possible observers, carrying out its activities at the political, managerial and technical levels (including through special groups of work): Common Assessment Framework, 2013. S. PONZIO, *La valutazione della qualità delle amministrazioni pubbliche*, Nel Diritto editore, Roma, 2012, 22; D. U. GALETTA, *Coamministrazione, reti di amministrazioni, Verwaltungsverband: modelli organizzativi nuovi o alternative semantiche alla nozione di «cooperazione amministrativa» dell'art. 10 Tce, per definire il fenomeno dell'amministrazione intrecciata?*, cit., 1689.

(38) C. FRANCHINI, 'Les notions d'administration indirecte et de coadministration', in *Droit administratif européen* (J.B. AUBY and J. DUTHEIL DE LA ROCHÈRE eds.), II ed., Brussels, 2014; S. CASSESE, 'Concentrazione e dispersione dei poteri pubblici', in *Studi in onore di Biscaretti di Ruffia*, Milano, Giuffrè, 1987, I, p. 155; ID., 'Global administrative law: The state of the art', in *International Journal of Constitutional Law* 13(2), April 2015; ID. *Research Handbook on Global Administrative Law*, Edward Elgar Publishing, 2016.

(39) Charter of Fundamental Rights of the European Union, art. 41. See: F. BASSANINI, 'Prefazione', in *Lo spazio amministrativo europeo. Le pubbliche amministrazioni dopo il Trattato di Lisbona* (M. P. CHITI and A. NATALINI eds), cit., 15 - 16, concerning the creation of a 'Maastricht public administration' and to the possible setting in the Treaty of 'quality standards and minimum efficiency while respecting the diversity of the choices made by each country with regard to the institutional and organizational models and the status of civil servants'.

among professional organizations, such as central purchasing bodies (CPBs) through joint cross-border procurement, might genuinely promote innovation, growth, and sustainable development in specific sectors.

Administrative cooperation, enhanced by the increasing use of technology, may develop a number of European networks able to improve the quality of administrative action at European and national levels.<sup>(40)</sup> The development of ‘smart contracts’ through new technology may also favor new forms of cooperation with collaborative agreements among suppliers and public administration aiming at a shared goal, *i.e.*, the correct and prompt execution of public contracts.<sup>(41)</sup>

### ***3. Cooperation Agreements involving Contracting Authorities from Different Member States***

As mentioned earlier, implementing administrative cooperation among public administrations from different Member States’ in the procurement sector might result in increasing the participation of tenderers. It would also enhance the quality of the selection process to the benefit of the final stakeholders of any procurement system, the citizens.

Any cooperation among procurement entities, both of the same country or cross-border, can turn into a benefit for the stakeholders, whenever the goals and the strategies are correctly and intelligently defined.

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(40) Tools that can be used to exploit the full potential of these means include the exchange of information between institutions, agencies and national public administrations, the so-called IDABC Interoperable Delivery of pan-European eGovernment Services to Public Administrations, Business and Citizens whose objective is the development of e-government services to public authorities, economic operators and citizens; and the Internal Market Information System, which is the European cooperation tool aimed at facilitating the exchange of information among public administrations of EU States. In addition, the EU Commission has unified in one program – the Interoperability Solutions for European Public Administrations (ISA) – forty actions related to activities carried out in previously EU-funded projects aimed at interoperability of information of public administrations and standardization of content in which a special interest has been taken in those specifically aimed at simplifying the formalities relating to public contracts, especially of cross-border and transnational character. As part of the ISA program on interoperability tools for public administrations on public contracts, a mention goes to the action called ‘Greater clarity of evidence requirements in the EU public procurement’ – aimed at developing computer tools (e-Certis) to facilitate participation in the selection procedures for a contractor, including for SMEs – and to the European Single Procurement Document (ESPD). *See*: F. LAFARGE, *Administrative Cooperation between Member States and Implementation of EU Law*, cit., 612 - 614, on the forms of administrative cooperation developed in Europe since the mid-1990’s through the use of databases.

(41) *See* G.M. DI GIUDA and G.M. RACCA, *From Works Contracts to Collaborative Contracts: The Challenges of Building Information Modeling (BIM) in public procurement*, Chapter 8 in this book; S. VALAGUZZA, ‘Governare per contratto. Come creare valore attraverso i contratti pubblici’, Editoriale scientifica, Napoli, 2018; G. M. RACCA, *I contratti pubblici collaborativi e le prospettive innovative della modellazione digitale (il Building Information Modeling)*, in *La prossima città* (G. F. FERRARI eds), II ed. (Smart cities 2), Nemesis, forthcoming.

Cooperation depends on the market in which the contracting entities operate, and on the goals that they decide to pursue – for instance, setting industrial policy targets at National, regional or local level within the framework of a coordinated and agreed cross-border strategy.

The Procurement Directives encourage that kind of cooperation, including cross-border cooperation. They also grant the contracting entities freedom to opt for it, and pursue shared goals.<sup>(42)</sup> The provision that ‘member States shall not prohibit’ cross-border procurement implies that forms of cross border cooperation should enjoy support from the EU. That probably is due to the very limited cross-border participation in undertakings for the procurement of different Member States<sup>(43)</sup>. European policymakers are also likely to stand for, and provide funds to cooperation projects of that kind in a design to promote cooperation and integration through the sharing of knowledge and experience.

The cross-border cooperation might apply to different phases of procurement, from the definition of needs to contract execution and management, and therefore contribute to meeting the common public objectives defined in the cooperation agreements.

Cooperation aimed at creating an aggregate ‘public demand side’, in fact, may contribute to achieving many of the objectives of the EU public procurement policies. It may also trigger economic operators’ responsiveness to specific joint procurement strategies on a case-by-case basis.

Relevant tools and strategies should be adapted so as to reach goals of interest to the contracting entities involved, for instance by sharing risks arising from buying innovation, and also promoting the participation of SMEs. Pursuing such an objective may require adopting a specific strategy which calls for contract splitting into lots, and bids limited to a maximum of one or two lots so as to encourage the participation of economic operators from different Member States, and market penetration as well.

It can even be assumed that suppliers will be encouraged to collaborate in order to create an aggregate ‘supply side’ (e.g. temporary partnerships) which would allow them to keep having a competitive position while meeting the aggregate ‘public demand side’ requirements – something that has not happened frequently so far. Cooperation on the demand side in relevant sectors

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(42) ECJ, 7 October 2004, Case C-247/02, where the Court declared void a national provision which restricted contracting authorities to choose a single criterion for the award of public contracts, thereby depriving them of the possibility of taking into consideration the nature and specific characteristics of such contracts, and of choosing the criterion most likely to ensure free competition and thus the best tender. *See* also Advocate General’s Opinion delivered on 27 November 2007 in the Joined Cases C-147/06 and C-148/06, footnote no. 39

(43) Art. 39(2), Dir. 2014/24/EU.

may increase the purchasing power and help reduce contract fragmentation in highly concentrated oligopolistic markets, which would result in significant savings.(44) The strategies and goals of such forms of cooperation may vary in different markets and European economic areas based on the industrial policy objectives to be pursued.

It should be added that systematic cooperation through a network of competences can open the way to the development of legal systems capable of overcoming administrative nationalism, thus favoring case-by-case harmonization.(45) Indeed, cross-border cooperation in the public demand side can help overcome legal barriers arising from ‘conflicts between different national provisions’.(46) The same applies to practical obstacles linked to language barriers.(47) These have actually limited cooperation agreements between public contracting authorities.(48)

Yet, such cooperation has already been envisaged, although implicitly, in the Directive 2004/18/EC on public procurement.(49) Not only does the

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(44) I. LOCATELLI, *Public Contracting and innovations: lessons across borders*; Chapter 1 in this book. For the U.S. experience see: J. B. KAUFMAN, *Cooperative Purchasing: A US Perspective*, Chapter 2 in this book.

(45) R. CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, cit.

(46) Directive 2014/24/EU, recital no. 73: ‘Joint awarding of public contracts by contracting authorities from different Member States currently encounters specific legal difficulties concerning conflicts of national laws. Despite the fact that Directive 2004/18/EC implicitly allowed for cross-border joint public procurement, contracting authorities are still facing considerable legal and practical difficulties in purchasing from central purchasing bodies in other Member States or jointly awarding public contracts. In order to allow contracting authorities to derive maximum benefit from the potential of the internal market in terms of economies of scale and risk-benefit sharing, not least for innovative projects involving a greater amount of risk than reasonably bearable by a single contracting authority, those difficulties should be remedied. Therefore, new rules on cross-border joint procurement should be established in order to facilitate cooperation between contracting authorities and enhancing the benefits of the internal market by creating cross-border business opportunities for suppliers and service providers’; EU Commission, *Making Public Procurement work in and for Europe*, COM(2017) 572 final, cit.

(47) See the Commission’s announcement: ‘To increase transparency in public procurement opportunities, an online machine translation service will be available, free of charge, for all public procurement notices published in Tenders Electronic Daily (TED) from 15 January 2016’. This service is available from and to all 24 EU official languages and is subject to prior registration on the TED (Tenders Electronic Daily) platform, which is the online version of the Supplement to the Official Journal of the EU, dedicated to European public procurement.

(48) The EU Commission supports the strategic implementation of integrated networks of contracting authorities from different Member States by the creation of transnational networks: ‘Enprotex’, to stimulate innovation in textile protection products; ‘Sci-Network’ to promote the restructuring of existing buildings with innovative and sustainable materials, the analysis and the use of life-cycle analysis (LCA) and life-cycle costing (LCC); ‘Leb – Healthcare’ with the purpose of creating innovative solutions with low emissions for the health sector. F. LAFARGE, *Administrative Cooperation between Member States and Implementation of EU Law*, cit., 600, on the so-called Sutherland report (cit.) for the establishment of a general system of administrative cooperation.

(49) Recital no. 73, Dir. 2014/24/EU, highlights: ‘specific legal difficulties concerning conflicts of national laws’ in case of ‘Joint awarding of public contracts by contracting authorities from different Member States’. It also reports that ‘Despite the fact that Directive 2004/18/EC implicitly allowed for cross-border joint public procurement, contracting authorities are still facing considerable legal and

Procurement Directive explicitly allow contracting authorities to develop participation procedures that are accessible to the authorities of other Member States, but also forbids Member States to prohibit such an opportunity.<sup>(50)</sup> This implies supporting cooperation as well as the aggregation of public demand, thus favoring the achievement of the goals of the European internal market of public procurement.<sup>(51)</sup>

It should be noted that the aforementioned provisions recall the Italian legislation which, since the early years of the last century, has exempted public administrations establishing consortia from the obligation to tender for the establishment of public purchasing groups.<sup>(52)</sup>

Most forms of cooperation among public entities are grounded in national legal traditions envisaging administrative agreements among public entities. The European Court of Justice validated such a principle.<sup>(53)</sup> In fact, it excluded the obligation to tender for consortia constitutive agreements.<sup>(54)</sup> It can be argued, therefore, that traditional forms of administrative cooperation anticipated the provisions set forth in the recent EU Procurement Directive, aimed at fostering an institutional public administration culture that many countries in continental Europe have in common.<sup>(55)</sup> All this has been reaffirmed in the EU legal framework while recalling the legal orders of the Member States.<sup>(56)</sup>

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practical difficulties in purchasing from central purchasing bodies in other Member States or jointly awarding public contracts', implicitly admitting this possibility. Similar programs are: the Competitiveness and Innovation Framework Programme (CIP – Competitiveness and Innovation Framework Programme; Programme for the Competitiveness of enterprises and SMEs (COSME) 2014-2020 and the Framework Programme for Research and Technological Development (FP7). Among the most advanced testing of innovative joint procurement across borders, a mention goes to the project HAPPI (Healthy Ageing – Public Procurement of Innovations), which aimed to favour product innovation and enabled a significant change in the contractor selection process, being carried out with a joint framework agreement among several Member States and open to accession by others, anticipating solutions now covered by the new directive on public procurement. See art. 69, Dir. 2014/24/EU.

(50) Arts 37 – 39, Dir. 2014/24/EU.

(51) Recital no. 71, Dir. 2014/24/EU. R. CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, cit.

(52) S. CIVITARESE, Art. 31, in *Commentario breve al testo unico sulle autonomie locali* (R. CAVALLO PERIN and A. ROMANO eds.), Breviaria Iuris, CEDAM, Padua, 2006, 182.

(53) ECJ, C-480/06, *Commission v. Federal Republic of Germany* (the so called 'Hamburg case), excluded the obligation to tender for the establishment of a public purchasing group. See R. CAVALLO PERIN, 'I servizi pubblici locali: modelli gestionali e destino delle utilities' in *L'integrazione degli ordinamenti giuridici in Europa* (P. L. PORTALURI eds), Edizioni Scientifiche Italiane, Napoli, 2014, 23-40.

(54) R. CAVALLO PERIN – G. M. RACCA, *La cooperazione amministrativa europea nei contratti e nei servizi pubblici*, in *Rivista Italiana di Diritto Pubblico Comunitario*, 2016, 1464.

(55) Art. 12, Dir. 2014/24/EU.

(56) R. CAVALLO PERIN, *Concluding remarks, Conference Proceedings: Appalti pubblici: innovazione e razionalizzazione. Le strategie di aggregazione e cooperazione europea nelle nuove direttive*, State Council, Rome, 14 May 2014, *Ius Publicum Network Review*, 38. See amplius: R. CAVALLO PERIN, *I servizi pubblici locali: modelli gestionali e destino delle utilities*, cit., 23-40.

In the absence of any explicit prohibition, various forms of cross-border administrative cooperation for joint procurement were initially established on the basis of applicable National and European principles and rules. Legal difficulties arose in terms of conflict between national laws, though. The Procurement Directive recalls existing legal and practical difficulties in purchasing from central purchasing bodies in other Member States, and even jointly awarding public contracts. Yet, it also remarks that the aforementioned type of cooperation was already possible under the previous EU Directive on public procurement.<sup>(57)</sup>

Indeed, cooperation among contracting authorities from different Member States for meeting public needs was first foreseen in the Green Paper for the Modernization of the EU public procurement, issued by the European Commission in 2011. That document acknowledged that ‘cross-border cooperation between contracting authorities from different Member States could help us integrate procurement markets further, and also encourage the defragmentation of European markets across national borders’.<sup>(58)</sup> Indeed, the Procurement Directive reinforced those aims by stating that ‘[a] Member State shall not prohibit its contracting authorities from using centralized purchasing activities offered by central purchasing bodies located in another Member State’. It is therefore clear that the European principle aimed at promoting a single market while protecting competition among private actors does change the way in which EU countries and public authorities may procure.<sup>(59)</sup>

The Procurement Directive explicitly bars Member States from prohibiting their contracting authorities to use central purchasing bodies from other Member States.<sup>(60)</sup> As such, any National law in contrast with that provision should be considered inapplicable as breaching the said directive.

As already mentioned, national rules on cooperation are based on common national traditions in many EU Member States. In Austria provisions allowing cross-border cooperation in the procurement sector were already in force before 2014, and have probably been taken as a reference model for the Procurement Directive. Those provisions, however, had not been particularly successful as far as actual cooperation was concerned, especially with Germany. Besides, cross-border procurement was explicitly forbidden in Finland, where, as a

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(57) Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.

(58) EU Commission (2011), *Green Paper on the Modernisation of EU Public Procurement Policy: Towards a More Efficient European Procurement Market*.

(59) I. LOCATELLI, *Public Contracting and innovations: lessons across borders*, Chapter 1 in this book.

(60) Art. 39(2) and (4), Dir. 2014/24/EU.

consequence, participation in joint cross border procurement projects was not possible. In the Italian legal system, the legal basis for joint cross border procurement can be found in the agreements among public authorities covered by the general law on administrative procedure and, at the local level, in conventions among municipalities.(61)

As far as the Belgian law and the law of Grand-Duchy of Luxembourg are concerned, the legal basis for the forms of cooperation in question can be found in their procurement law.(62)

In such a multifaceted European context, further clarification from the EU institutions to foster cooperation was therefore necessary: although already available as an option, in practice cooperation was a complex issue because of “specific legal difficulties concerning conflicts of national laws”.(63)

Some pilot projects aimed at testing joint cross-border procurement, in fact, brought to the fore evidence of the criticalities in the development of its models.(64)

Pilot projects had to overcome many challenges, but their outcomes may lead to further improvement, especially because the implementation of the Procurement Directives has demonstrated that joint cross-border public procurement is the key to strengthening the single market.(65)

The EU Commission and, more recently, the European Parliament, have observed that the internal market could be shaped so as to develop innovative methodologies, products, works or services which do not yet exist.(66) In this

(61) See Art. 11, Law of 7 August 1990, no. 241 (*‘Norme in materia di procedimento amministrativo e di diritto di accesso ai documenti amministrativi’*). See also art. 30, Legislative Decree of 18 August 2000, no. 267 (*‘Testo unico delle leggi sull’ordinamento degli enti locali’*).

(62) Under the Belgian Law, the opportunity to establish a central purchasing body was made possible pursuant articles 24, 31 and 32 of the Act of 15 June 2006 on public procurement, and also articles 136, 137 and 138 of the Royal Decree of 15 July 2011. The Public Procurement Act of 17 June 2016 replaced the former Act of 15 June 2006 as it transposed the Public Procurement Directives 2014/24/EU and 2014/25/EU. Under the law of the Grand-Duchy of Luxembourg, central purchasing bodies are governed by articles 3, paragraph 9, and 25, paragraph 2, of the Law of 25 June 2009 on public procurement, while framework agreements are provided for by articles 3, paragraph 5, 5, paragraphs 2 and 3, and 46 of the same law on public procurement. On 20 April 2018, the new law on public procurement of 8th of April 2018 (*‘Loi sur les marchés publics du 8 avril 2018’*) became effective.

(63) Recital no. 73, Dir. 2014/24/EU.

(64) See below, the HAPPI case. On the 28 March 2019, the European Commission announced that 15 Member States and the Commission had signed framework contracts, on the basis of Article 5 of Decision 1082/2013/EU. EU Commission, *Making Public Procurement work in and for Europe*, cit.

(65) BBG-SKI, *Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, December 2016. See the criticalities evidenced by A. SANCHEZ-GRAELLS, *Is Joint Cross-Border Public Procurement Legally Feasible or Simply Commercially Tolerated? – A Critical Assessment of the BBG-SKI JCBPP Feasibility Study*, in *European Procurement & Public Private Partnership Law Review*, 12, 2017, p. 97.

(66) EU Parliament, *Resolution of 4 October 2018 on the public procurement strategy package* (2017/2278(INI)), October 2018, 5. EU Commission, *Making Public Procurement work in and for Europe*, COM(2017) 572 final, cit.

view, the role of aggregation acquires greater importance when combined with adequate techniques, for instance contract splitting into lots, in a design to favour the participation of SMEs.(67) Arguably, more Member States should thus take advantage of the CPBs and aggregation of public purchasing to enhance expertise, best practices, and innovation.

Public-public cooperation, which does not necessarily mean huge contracts of unmanageable complexity, nonetheless requires a sophisticated and constantly revised procurement strategy.

Purchasing on a cross-border basis is not just aimed at minimizing what the economists define as ‘market failures’. Nor is it meant to allow enterprises and SMEs to pursue mere commercial interests in the common market. Administrative cooperation aims to implement fundamental rights effectively while meeting commonly shared transnational needs and interests.

#### ***4. The European Territorial Cooperation Grouping and other Joint Entities***

The Procurement Directives recalled the establishment of European Groupings of Territorial Cooperation (EGTCs) and other entities established under the EU law, as a means for cross-border cooperation.(68) In particular, mentioned in the Directive are ‘European Groupings of territorial cooperation under Regulation (EC) No 1082/2006 of the European Parliament and Council’ as joint entities which ‘contracting authorities from different Member States’ can establish to pursue cross-border procurement. In that event ‘the participating contracting authorities shall, upon decision of the competent body of the joint entity, agree on the applicable national procurement rules of one of the Member States by choosing either (a) the national provisions of the Member State where the joint entity has its registered office or (b) the national provisions of the Member State where the joint entity is carrying out its activities’. According to the European Union law, the EGTC is a subject with legal personality set up to promote cross-border cooperation at a transnational or interregional level(69).

(67) EU Commission, *Commission Notice Guidance on Innovation Procurement*, Brussels, May 2018 C(2018) 3051 final, 7.

(68) Art. 39(5), Dir. 2014/24/EU.

(69) All approval authorities adopted the original EGTC regulation (EC) 1082/2006/CE of 5 July 2006; but only 23 of the 54 approval authorities would have adopted the EGTC Regulation as amended by the Regulation (EU) 1302/2013 by December 2017. Since the introduction of the EGTC in 2006, 69 EGTCs were founded in the EU with various local, regional and national authorities as well as other members. Currently there are 68 EGTCs as one closed in 2017. *See*: European EU Commission, Assessment of the application of EGTC regulation, Final report, April 2018, p. 2; EU Commission, European Territorial Cooperation. Building Bridges Between People, 2011; L. LANZONI, ‘Le forme della democrazia partecipativa nell’ambito della cooperazione transfrontaliera’, in *Riv. it. dir. pubbl. comunit.*,

It should be noted that the reference to an entity conceived as a means for joint procurement, offers a new perspective on implementation.

Territorial cooperation was regarded as a priority objective in the 2014-2020 programming period of the European Structural Investment (ESI) Funds, which fostered networking and the exchange of experience while enabling public administrations to identify suitable legal tools for implementing the European cohesion policy.<sup>(70)</sup> Administrative integration at transnational territorial levels has been hindered by the complexity of national legal frameworks applicable to the establishment of, and participation in EGTCs.<sup>(71)</sup> Adding to that is the Member States' tendency to maintain sovereignty on territorial policies.<sup>(72)</sup> In the light of all this, it seems clear that the recent European Union regulation was specifically aimed at simplifying the rules for the establishment and functioning of the aforementioned legal entities.<sup>(73)</sup>

The preamble to the Regulation states different objectives, namely facilitating the establishment and operation of EGTCs, clarifying relevant provisions and allowing for a more extensive use of EGTCs so as to improve policy coherence while pursuing cooperation between public bodies without creating an additional burden on national or Union administrations.<sup>(74)</sup> Nevertheless, territorial and linguistic challenges in the implementation of the Regulation have led to the creation of heterogeneous national and regional frameworks. In that respect, the degree of detail in national implementation rules, including the latest amendments, differs considerably. As reported by a recent analysis of the European Commission, some include extremely technical guidance

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2011, 503; V. COCUCCI, 'Nuove forme di cooperazione territoriale transfrontaliera: il Gruppo Europeo di Cooperazione Territoriale', in *Riv. it. dir. pubbl. comunit.*, 2008, 89; L. SOVERINO, 'I servizi pubblici nell'Euroregione: nuove prospettive di diritto comunitario per la cooperazione transfrontaliera, tra Consiglio d'Europa e potere estero delle Regioni', in *Riv. it. dir. pubbl. comunit.*, 2009, 17; R. DICKMANN, 'Il gruppo europeo cooperazione territoriale (geet)', in *Foro amm. CDS*, 2006, 2901.

(70) EU Commission, *European Structural and Investment Funds 2014 - 2020: Official texts and commentaries*, April 2015. The objectives of cohesion policy are, namely: 'Investment for growth and employment', with the national and regional programs being funded through the ERDF (European Regional Development Fund), the ESF (European Social Fund) and the Cohesion Fund, aiming at cross-border and transnational cooperation programs, also inter-financed by the ERDF. See Regulation 1303/2013/EU of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Fund for Maritime Affairs and Fisheries, and general provisions on the European regional development Fund, the European social Fund, the cohesion Fund and the European Fund for Maritime Affairs and Fisheries, and repealing Regulation (EC) No. 1083/2006 of the Council.

(71) European Parliament, *European Grouping of Territorial Cooperation as an Instrument for Promotion and Improvement of Territorial Cooperation in Europe*, July 2015; Committee of the Regions, *Conclusions of the Committee of the Regions about the Joint Consultation. The Review of Regulation (EC) 1083/2006 on the European Grouping of Territorial Cooperation*, 2010.

(72) They may be based on national legal forms (e.g. associations) formed by partners from different countries, or through a valid bilateral regional agreement.

(73) Regulation (EU) No 1302/2013 of the European Parliament and Council of 17 December 2013 amending Regulation (EC) No 1082/2006 on a European grouping of territorial cooperation (EGTC).

(74) Regulation (EU) No 1302/2013.

such as task descriptions, approval procedures and provisions for the EGTC staff, and/or registration procedures in Member States. Other provisions focus on selective criteria to help EGTCs set-up in the territory of the approval authority. Although the amendment to the original EGTC regulation has considerably facilitated EGTCs, there is still room for further clarification and legal certainty of applicable rules.(75)

As typically seeking a decrease in administrative costs and burden while demanding speedier and less complicated arrangements, simplification helps joint cross-border procurement as well. Hence, the new regulatory framework provides for tacit consent, after six months, to the establishment of an EGCT from the competent national authorities excepting the Member State where the EGTC's seat is located, as in that case formal approval is required.(76) The six-month period is interrupted when the Member State requests more information and the prospective members of the EGTC do not provide that information after ten days.(77) EGTCs can be set up by public administrations (National and local), public enterprises, bodies governed by public law, and enterprises entrusted with the operation of services of general economic interest.(78) In principle, therefore, private entities are excluded from participation unless they meet the criteria applicable to bodies governed by public law.(79)

The possibility of creating an EGTC among bodies governed by public law might fit, in particular, cooperation among contracting entities from different member States for the purpose of joint cross-border procurement. Even more challenging might be the cooperation, not only among traditional contracting entities, but instead among European central purchasing bodies, as provided in the aforementioned Procurement Directives.

It is also worth noting that, in addition to what was provided for in the previous legislation, the national and central authorities of the Member States may become EGTC members, alone or together with sub-national authorities or bodies. The rationale behind the new EGTC regulation is reaching

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(75) EU Commission, *Assessment of the application of EGTC regulation*, cit., 10.

(76) See Regulation 1302/2013/EU, art. 4, par. 3, providing that at least the Member State where the registered office of the EGTC is to be located formally approves the Convention.

(77) The extension from three to six months is justified by the fact that the previous period was rarely respected as it worked as an obstacle to the creation of new EGTCs.

(78) Regulation 1082/2006/EC, art. 3, as amended by EU Regulation 1302/2013. The approval of the participation in an EGTC by the competent authorities at the national level requires the submission of a proposal for the EGCT Convention to the competent national authorities. In Italy, the Community Law of 2008 (Law of July 7, 2009, no. 88, *Provisions for the fulfilment of obligations deriving from Italy to the European Communities – Community Law 2008*) provides for rules on the participation of the national authorization procedure in an EGCT, which has to be adapted in light of the renewed European framework of the EGCT by a new Regulation.

(79) E.g. a private association, or a public company solely composed of public members and financed by public funds is to be seen as a body governed by public law and may therefore participate in an EGTC.

beyond regional and territorial boundaries, and limiting agreements that envisage cross-border cooperation exclusively between neighboring territorial areas (regions, departments, etc.).<sup>(80)</sup> All this may ultimately enable bodies governed by public law to pursue common interests and structural cooperation while developing networks across the European Union's geographical boundaries.<sup>(81)</sup>

The establishment of an EGTC has to be based on a cooperation agreement between Member States setting out the objectives, duration, term and termination, and the methods to be adopted for carrying out a given activity.<sup>(82)</sup> The agreement may envisage the realization of programs that are co-financed by the EU, and also cross-border cooperation projects that may be transnational or interregional and not funded by the EU, including cooperation agreements for contract or public service undertakings.<sup>(83)</sup> To be specified in the agreement is the applicable law, which must be that of one of the Member States where the registered office of the EGTC is located or where the activity is performed.<sup>(84)</sup>

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<sup>(80)</sup> Examples of such agreements are the Karlsruhe agreement (1997), Mainz agreement (1998), Isselburg-Anholt agreement (1991) and the Benelux agreement (1986).

<sup>(81)</sup> For example the EGTCs located on the borders between the six founding EU Member States (i.e. the Benelux countries, France and Germany) and Nordic countries. A large number of CPSPs can also be observed on the German-Swiss, French-Swiss, Czech-German borders. See also ESPON EGTC, *Cross-border Public Services (CPS)*, Final report, January 2019.

<sup>(82)</sup> Regulation 1082/2006/EC, art. 8 as modified by Regulation 1302/2013/EU. The agreement must specify: the name of the EGTC and its registered office; the extent of the territory in which the EGTC may carry out its duties; the goal and the tasks of the EGTC; the duration of the EGTC and the conditions for its dissolution; the list of the EGTC's members; the list of the EGTC's organs and their competencies; the applicable Union law and the law of the Member State in which the national EGTC has its registered office regarding the interpretation and application of the Convention; the applicable Union law and that of the Member State in which the national organs of the EGTC operate; the arrangements for the participation of members from third countries or the OCT, where appropriate including the identification of the applicable law where the EGTC carries out tasks in third countries or in the OCT; the applicable Union and national law directly relevant to the grouping's activities conducted in accordance with the tasks specified in the agreement; the rules applicable to the EGTC's staff as well as the principles governing the arrangements concerning personnel management and recruitment procedures; the provisions regarding the liability of the EGTC and of its members; the appropriate provisions on mutual recognition, including with regard to the financial control of the management of public funds; the procedures for adopting the statutes and amending the convention. The tasks of the EGTC are defined by the convention agreed by its members. Their boundaries, a delicate point of balance between the aspirations of the Regions and the integrity of sovereignty and state control, are specified by a number of factors but remain flexible for extended cooperation and progressive processes. The members may decide by unanimity to empower the execution of tasks to one of its members. See European EU Commission, *Assessment of the application of EGTC regulation*, cit., p. 21; S. CARREA, 'The discipline of the European Grouping of Territorial Cooperation (EGTC) between European Union law, statutory autonomy and private international law: an attempt at synthesis', in *Dir. comm. internaz.*, 2012, 611.

<sup>(83)</sup> EU Commission, *Note for guidance on the funding of joint EDF-ERDF projects 2014-2020*, November 2014. See: Recital no. 7, Regulation 1082/2006/EC.

<sup>(84)</sup> Within ten working days from the registration or publication of the convention and statutes of the country where the EGTC has its registered office, the EGTC shall notify the Committee of the Regions (CoR), which maintains a register of EGTCs. The CoR then transmits the information to the Office of the European Union, which publishes a notice announcing the establishment of the EGTC.

Within the framework of territorial cooperation supported by the European Union it is possible to distinguish between EGTCs that deal with specific programs having a broad cross-border content and EGTCs pursuing cooperation projects having one, specifically identified, goal.(85)

Further distinctions can be made in respect to the EGTCs' legal form of establishment, applicable law (public or private), and the liability system (limited or unlimited).(86)

Initially, EGTCs were mainly aimed at achieving cooperation in limited geographical areas and in some sectors.(87) Administrative cooperation was pursued to achieve different goals, including tourism, sustainable development in agriculture, integration between urban and rural areas, economic and social development, cross-border transport system management, cross-border project development, the construction of infrastructures or the creation of hospitals, yet always ensuring the exchange of experience and good practices.(88)

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The internal organization and functioning of the EGTC is governed by its Statute. *See* EC Regulation 1082/2006, art. 9 as amended by EU Regulation 1302/2013. The Statutes of each EGTC governing the internal organization identifies: the tasks of the organs and how they work; decision-making procedures and language; the methods of operation and employment contracts; financial contributions, the rules on accounting and financial statements. The statutes specify a minimum for: the operating mode of its organs and powers of these bodies, as well as the number of representatives of the members in the relevant organs; its decision-making procedures; its language or its working languages; the arrangements for its operation; the procedures concerning the management and staff recruitment; the provisions concerning the financial contribution of its members; the applicable rules of accounting and budget for its members; the appointment of an independent external auditor of the accounts; the amendment of its articles of association procedures. The statutes set up an assembly composed of representatives of each EGTC member and a director who represents the EGTC itself, and establish an annual budget based on the legislation of the country where it has its registered office. The statutes also characterize any other organs by defining their competencies: Regulation 1082/2006/EC, art. 11 as amended by Regulation 1302/2013/EU. The preparation of accounts including the annual report accompanying them, and the auditing and publication of those accounts shall be governed by the national law of the Member State where the EGTC has its registered office. The budget is divided into a component of operating costs and, if necessary, an operational component.

(85) With regard to the object of cooperation, the EGTC Regulation is relatively generic with reference to 'actions' of general cooperation without distinguishing between issues of cross-cutting interest and a long period, or by activities.

(86) European Parliament, *European Grouping of Territorial Cooperation as an Instrument for Promotion and Improvement of Territorial Cooperation in Europe*, cit., 53. Committee of the Regions, EGTC Monitoring Report 2012. 2013, where it is reported that most of the EGTCs are legal entities of public law. Regulation 1082/2006/EC, art. 12, as amended by Regulation 1302/2013/EU. An EGTC shall be liable for its debts. In the event of insolvency, the members are responsible depending on their contribution (fixed in the statutes). It can, however, impose a 'limited EGTC' (including the phrase in their name), provided that at least one of its members is a limited liability entity.

(87) Example: Hungary and France. *See* European Parliament, *European Grouping of Territorial Cooperation as an Instrument for Promotion and Improvement of Territorial Cooperation in Europe*, cit. 24. EGTCs established with specific thematic focus: Big Région EGTC was established to manage a cross-border project; EGTC TATRY Ltd. as an agency for the management of the Small Project Fund (SPF). *See* also the EGTC: Secrétariat du Sommet de la Grande Région, European Park / Parc Européen Maritime Alps – Mercantour and Hospital de la Cerdanya.

(88) Examples of administrative cooperation in tourism: EGTC Pirineus – Cerdanya; EGTC ArchiMed; EGTC TRITIA Ltd.; ZASNET EGTC; Territorio dei comuni: Comune di Gorizia, Mestna

In general, the possibility of providing public services at a cross-borders level (through a Central Purchasing System, CPS) is a key factor for boosting territorial cohesion and the European internal market development. It contributes to reducing negative border effects, for example by fostering cultural integration, and increases understanding of shared issues or needs. By increasing the accessibility and scope of services, the quality of the services can be improved because knowledge and resources from both sides of a border can be used effectively.<sup>(89)</sup> It is worth highlighting how such a tool can be used for the 'joint management of public services', particularly insofar as services of general economic interest are concerned. All this may lead to in-house companies establishing EGTCs to develop innovative forms of cooperation in the field of public services and, as a result, strengthen the economic, social, and territorial cohesion of the European Union.<sup>(90)</sup>

Although the EGTC has a limited role in the public procurement sector at present, such a model is regarded as having the potential to promote cooperation between traditional contracting authorities (State and local authorities), and also between bodies governed by public law (central purchasing bodies). Indeed, it may ensure innovative developments in the procuring function through institutionalized forms of cooperation between contracting authorities from different Member States.<sup>(91)</sup> EGTCs formed by several public procurers from different countries, meeting minimum requirements, and having a mandate to procure, can purchase on behalf of them. That means minimizing

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Občina; Nova Gorica e Občina Šempeter-Vrtojba; EGTC 'Espacio Portalet'; EGTC Spoločný region Ltd.; EGTC 'Euregio Senza Confini r.l. – Euregio Ohne Grenzen; mbH'; Karst-Bodva EGTC; ABAŮJ-ABAŮJBAN EGTC Ltd.; EGTC Pons Danubii; Rába-Duna-Vág EGTC Ltd.; EGTC Gate to Europe Ltd.; BODROGKŐZI EGTC Ltd.; Eurocity of Chaves-Verín EGTC; EGTC Parc européen/Parco europeo Alpi Marittime; Mercantour; in the agricultural sector: EGTC Euroregion Aquitaine-Euskadi; EGTC 'Euregio Senza Confini r.l. – Euregio Ohne Grenzen mbH'; Banat Triplex Confinium Ltd. EGTC; Rába-Duna -Vag EGTC Ltd; in urban and rural areas: EGTC TRITIA Ltd.; EGTC TATRY Ltd.; EGTC Spoločný region Ltd.; EGTC Karst-Bodva; Pons Danubii EGTC; for building infrastructures for economic and social development: EGTC TRITIA Ltd.; EGTC Hospital de la Cerdanya – Karst-Bodva EGTC; Territorio dei comuni: Comune di Gorizia, Mestna Občina Nova Gorica e Občina Šempeter-Vrtojba; EGTC 'Espacio Portalet'; Arrabona EGTC Ltd.; Bánát-Triplex Confinium Ltd. EGTC; Douero-Douro EGTC; EGTC Parc européen/Parco europeo Alpi Marittime and also for the creation of hospitals. It is the case of the Agrupació Europea de Cooperació Territorial Hospital de Cerdanya (HC), which is, at currently, the first cross-border healthcare project at European Level, aiming to ensure the availability of proper and multi-profile healthcare to the local (French and Spanish) population. See on this topic: European Parliament, *European Grouping of Territorial Cooperation as an Instrument for Promotion and Improvement of Territorial Cooperation in Europe*, cit.

(89) See also ESPON EGTC, *Cross-border Public Services (CPS)*, Final report, cit. 13.

(90) G. M. RACCA, 'Joint Procurement Challenges in the Future Implementation of the New Directives', (F. LICHÈRE, R. CARANTA and S. TREUMER eds.) *Modernising Public Procurement: the New Directive*, Copenhagen, cit., 225-254.

(91) Art. 39(5), Dir. 2014/24/EU.

transaction costs, which would be higher in the event of separate tenders, and pursuing common goals of public interest.<sup>(92)</sup>

Still, the possibility of carrying activities beyond national and regional borders requires further clarification in the interpretation of the national rules for establishing an EGTC to achieve aggregated and collaborative European procurement.<sup>(93)</sup> As the term ‘cooperative procurement’ encompasses various modes of cooperation between public buyers, establishing (or mandating) dedicated entities – such as the European Grouping of Territorial Cooperation (EGTCs) to perform joint procurement on a regular basis – might be the most structured means of cooperation.<sup>(94)</sup> As mentioned earlier, the Procurement Directives specifically indicate the EGTCs (or other joint subjects covered by Union law) as a means to implement administrative cooperation in public contract award and execution.<sup>(95)</sup>

The EGTC agreement from which the joint entity originates may also define the rules and strategies to use within the sector in which the EGTC operates, the procedure to be followed in the procurement phase (mainly framework agreements), and address contract management and contract execution.

As far as the procurement phase is concerned, the applicable law can either be that of the Member State where the EGTC’s registered office is or that of the Member State where the activity in question is performed. The legal framework set out thereby can remain unchanged for an indefinite period of time (if so envisaged by constitution) or only for limited period (as with certain types of contracts for single or occasional joint procedures). Supplementing that legislation are the European rules on conflicts of laws, and rules allowing for the choice of a different law to be applied in the execution phase of a contract. Aside from European directives, those rules promote integration among legal systems and prompt ‘competition’ when it comes to choosing the applicable national law, and allowing case-by-case harmonization under the more effective rule.<sup>(96)</sup>

(92) *See*, by way of example, the ‘Hospital de la Cerdanya’ case. This EGTC was established under Spanish Law; under the statutes, common legal provisions will, in case of conflict, prevail; citizens from both countries have the explicit right to file their complaints against the members of the EGTC, while procurement and employment is subject to Spanish and Catalan legislation. The statutes foresee that the winding-up of the EGTC might not disrupt the provision of health services; in that case, a specific decision by the partners must be taken accordingly.

(93) This possibility is expressly provided by the Regulation 1302/2013/EU. *See*: EU Commission, *Assessment of the application of EGTC regulation*, cit., 21.

(94) EU Commission, *Commission notice Guidance on Innovation Procurement*, cit., 18; Exploring collaborative public procurement practices (A. PATRUCCO, J. LYNCH, J. HARLAND, J. TELGEN, T. TATRAI eds), 2018; EU Commission, *Public procurement – a study on administrative capacity in the EU*, 2016.

(95) Recital no. 24, Regulation 1302/2013/EU: ‘The convention should also list the applicable Union and national law directly relevant to the EGTC’s activities carried out under the tasks specified in the convention, including where the EGTC is managing public services of general interest or infrastructure’.

(96) Recital no. 73, Dir. 2014/24/EU.

The administrative cooperation model provided by the ETGC regulation might open way to the development of other 'second level' horizontal cooperation forms that may enter agreements and establish networks that may join central purchasing bodies through an EGTC.<sup>(97)</sup> Also, joint strategies for the implementation of the European administrative scope of action in the public contracts area may be developed so as to ensure efficiency, quality, and integrity to European citizens while sharing risks arising from innovation.

As it has become easier to establish them, more and more joint entities operating under National or EU laws can now experience joint cross-border procurement. EU pilot projects have often envisaged coordinated procurement being awarded by different contracting authorities, which cannot be regarded as joint procurement in its own right. Those projects, however, were easier to start and allowed authorities to define common technical specifications for buying innovation.<sup>(98)</sup>

Occasional joint-cross border procurement funded by European projects may also establish an Association, operating under National law, open to forms of voluntary cooperation among contracting authorities from different Members States (e.g. central purchasing bodies). That is the case, for example, of the European Public Procurement Alliance (EHPPA). As a French law association, EHPPA is an alliance of non-profit Group Procurement Organizations which aims to pool expertise, leverage performance and provide its members with a strategic position in the European health procurement market.<sup>(99)</sup> At present, the EHPPA activities are aimed at favouring the cooperation and exchange of information among members willing to improve their own procurement performance, and also at facilitating the use of innovative procurement in healthcare. Establishing a framework for joint procurement to be carried by the EHPPA's Members, taking advantage of the previous project 'HAPPI (Healthy Ageing – Public Procurement of Innovations)' is another praiseworthy objective. The EHPPA was an associated member of the a pre-existing consortium funded by an EU project aimed at encouraging joint cross-border procurement. That led to the creation of a joint framework agreement among several central purchasing bodies from different Member States which was open to accession by hospitals normally served by the CPBs, and

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(97) See recital no. 5, Regulation no. 1302/2013/EU: 'Under Regulation (EC) No 1082/2006 EGTCs have in each Member State the most extensive legal capacity accorded to legal persons under that Member State's national law, including the possibility of concluding agreements with other EGTCs, or other legal entities, for the purposes of carrying out joint cooperation projects to, inter alia, provide for more efficient operation of macro-regional strategies'.

(98) See: P. VALCARCEL FERNANDEZ, *The Relevance of Promoting Collaborative and Joint Cross Border Procurement for Buying Innovative Solutions*, Chapter 4 in this book.

(99) EHPPA (European Health Public Procurement Alliance) is an association governed by the French law of July 1st, 1901 and the decree of August 16th, 1901.

also others, thus anticipating solutions that are now covered by the Procurement Directive.(100)

The public healthcare sector has experienced the potential benefits of innovative instruments for the joint procurement of medical countermeasures against cross-border health threats.(101) Joint Procurement Agreements, although established on the basis of the Financial Regulation, have shown their potential in improving the health system efficiency through collaboration at a European level aimed at granting supply safety, cost saving, reduction in administrative burdens, and the creation of professional networks. All this may be particularly appealing to smaller Member States.(102)

Another example of trans-border collaboration across the EU which took place before the entry into force of the Procurement Directive was the collaboration between the banks of the European system under the European Central Bank.(103)

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(100) HAPPI is one of the first cross-border joint public procurements founded by the European Commission and a consortium of European partners consisting of procurement organizations (CPBs) in the health sector, by experts in the field of public procurement, by innovation agencies and academic institutions. See: G. M. RACCA, *Joint Cross-Border Procurement of Innovative Solutions in the Healthcare Sector. The HAPPI project experience*, Turin University Press, 2019, forthcoming. See also: EU Commission, *Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, December 2016, 62 (BBG-SKY); EU Commission, *Making Public Procurement work in and for Europe*, COM(2017) 572 final, cit.

(101) Art. 168(5) TFEU and art. 5 of Decision 1082/2013/EU on serious cross-border threats to health provided the legal basis for the establishment of the joint mechanism: ‘*The institutions of the Union and any Member States which so desire may engage in a joint procurement procedure [...] with a view to the advance purchase of medical countermeasures for serious cross-border threats to health*’. As the referenced memorandum recalls, Botulinum anti-toxin was the first procurement procedure successfully concluded in 2016. Apart from the joint procurement on pandemic influenza vaccines, for the future, EU Member States have expressed interest in joint procurement procedures for diphtheria anti-toxin, Tuberculin and BCG vaccines, and Personal Protective Equipment, all of which are currently in the preparatory phase. See on this topic: N. AZZOPARDI-MUSCATA and P. SCHRODER-BÄCK, H. BRAND, *The European Union Joint Procurement Agreement for cross-border health threats: What is the potential for this new mechanism of health system collaboration?* In *Health Economics, Policy and Law*, Cambridge University Press, 2017, 12(1), 43-59.

(102) The JPA, which was adopted by the Commission on 10 April 2014, is based on the Commission Delegated Regulation (EU) No 1268/2012 of 29 October 2012 on the rules of application of Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union. The JPA is an agreement between the Commission and the participating Member States which implements a provision of a legislative act, namely, Article 5 of Decision 1082/2013/EU. As the JPA was concluded pursuant to the Financial Regulation, it can be considered as a budgetary implementing measure of Decision 1082/2013/EU. The joint procurement procedure was preceded by a Joint Procurement Agreement (JPA) between the mentioned entities determining the practical arrangements governing that procedure, and the decision-making process with regard to the choice of the procedure, the assessment of the tenders and the award of the contract. On 28 March 2019, the European Commission announced that 15 Member States and the Commission signed framework contracts with a pharmaceutical firm for the supply of pandemic influenza vaccines to 30 national contracting authorities, which represented the first “umbrella” joint procurement agreement for influenza pandemic.

(103) EU Commission, *Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, cit. See: European Economic and Social Committee, *Europe’s cooperative banking models*, 2018.

An International agreement was signed for the Italian-Austrian Brenner Tunnel (BTT) collaboration.<sup>(104)</sup> The first phase of the procurement concerned the tender for a geological assessment to be carried out in both Austrian and Italian territory. The tender was organized as an open procedure to award a contract to a single economic operator (or consortium) using bilingual Italian and German documents. Governed by the Italian public procurement law, that agreement stated that the Italian courts would have jurisdiction in the event of litigation arising therefrom.<sup>(105)</sup>

Public-public cooperation, especially cross-border cooperation, can strengthen the ability of public administrations to pursue public interests (in specific areas and sectors). Public-public cooperation can also establish a ‘positive collusion’ strengthening the ability of public entities to pursue public interest and shared industrial policy goals to the benefit of growth, innovation and the integrity of European Union.<sup>(106)</sup> Asymmetric integration through administrative cooperation may offer ways of taking steps forward to achieve European integration effectively.<sup>(107)</sup>

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(104) The first phase (1999-2003) consisted of the preliminary project and assessment; in the second phase (2003-2010) the project was finalized, and the EIA carried out; the second part of phase II (2007-2013) was the exploratory portion; with the building phase starting in 2011. The construction work and the railway outfitting of the Brenner Base Tunnel should be completed by 2025. After that, there will be a year of test operations. The tunnel will become fully operational in December of 2026. See: EU Commission, *Study on permitting and facilitating the preparation of TEN-T core network projects Annex 4 – Case studies*, September 2016, 19. ID., *Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, December 2016, 62.

(105) EU Commission, *Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, cit.

(106) G. M. RACCA and R. CAVALLO PERIN, ‘Corruption as a violation of fundamental rights: reputation risk as a deterrent against the lack of loyalty’, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (G. M. RACCA and C. R. YUKINS eds.), *op. cit.*, 23; A. SÁNCHEZ GRAELLS, ‘Prevention and deterrence of bid rigging: a look from the new EU directive on public procurement’, *ivi*, 171; A. LÓPEZ MIÑO and P. VALCARCEL FERNANDEZ, ‘Contracting authorities’ inability to fight bid rigging in public procurement: reasons and remedies’, *ivi*, 199. G. M. RACCA and R. CAVALLO PERIN – G. L. ALBANO, ‘Public Contracts and International Public Policy Against Corruption’, in *Transnational law of Public Contracts* (M. AUDIT and S. W. SCHILL eds.), Bruylant, Bruxelles, 2016, 845. See also: CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, cit.

(107) R. CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, cit.

### **5. The Different models of Cross-border Joint Procurement: Joint award or Use of Offered Centralised Purchasing Activities**

As mentioned earlier, the EU Procurement Directive envisages forms of joint cross-border cooperation through the establishment of joint entities, or EGTC's, operating under European or national laws.(108)

Joint procurement strategies may be implemented relying on joint award procedures or centralized activities offered by a central purchasing body from a different Member State.

The Directive prevents a distorted use of cooperation as a way as to avoid 'the application of mandatory public law provisions', provided that those 'mandatory public law provisions' are 'in compliance with the EU law to which they are subject in their Member State'.(109)

The first part of the provision seems to warn against the intentional distorted use of national rules implementing the EU Directive in different Member States.(110) Such a risk could be avoided by requiring a specific choice to be made with regard to national provisions applicable to procurement procedures, and perhaps also introducing further clauses that meet all national implementation requirements, especially on transparency. The cooperation agreement might establish the same set of rules applicable in each country on mandatory exclusion grounds, thus enhancing harmonization and striving for stricter qualifications, perhaps through self-declarations according to the ESPD. Choosing the provisions of one Member State does not prevent adding further provisions (in view of the cooperation) governing selection and

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(108) Recitals nos. 71 and 73, Dir. 2014/24/EU. See EU Commission, *Staff Working Paper concerning the application of EU public procurement law to relations between contracting authorities (public-public cooperation)*, Brussels, SEC(2011) 1169 final, October 2011, 12. A distinction is made therein between cooperation for the performance of tasks of public interest in the proper sense, and assigned activities that would require a competitive tendering within the market.

(109) Art. 39(1) e (4), Dir. 2014/24/EU. A. SANCHEZ-GRAELLS, *Is joint cross-border public procurement legally feasible or simply commercially tolerated? A critical Assessment of the BBG-SKI JCBPP Feasibility Study*, cit., p. 16.

(110) The ECJ's case-law has repeatedly ruled against any distorting or elusive use of the European Union's provisions: on the principle of prohibiting abusive practices in taxation see: ECJ, 21 February 2006, case C-255/02, Halifax plc, Leeds Permanent Development Services Ltd, County Wide Property Investments Ltd v. Commissioners of Customs & Excise, § 69: '[t]he application of Community legislation cannot be extended to cover abusive practices by economic operators, that is to say transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by Community law'. See also: ECJ, 5 July 2007, case C-321/05, Hans Markus Kofoed v. Skatteministeriet, § 38: '[i]ndividuals must not improperly or fraudulently take advantage of provisions of Community law. The application of Community legislation cannot be extended to cover abusive practices, that is to say, transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by Community law'.

award, according to the legal system in which the contract shall be executed (e.g. the *Anti-mafia* certificate which is required only by Italian legislation). The rationale of the aforesaid European provision is avoiding an intentional misuse of cooperation with a view to allowing the participation of suppliers which, according to national provisions only, would not be able to participate. Should all this be proved, it might be a case of intentionally avoiding mandatory public law provisions.

The U.S. experience of setting a 'Participating Addendum' to joint framework agreements for each Member State involved, although taking the local legal requirements into account, might offer a useful solution to be adopted for European purposes.<sup>(111)</sup> Under this approach, the master framework agreement with vendors is subordinate to the 'Participating Addendum' entered into between those vendors and the participating state and local governments.

In many other cases national implementation may be irrelevant as transparency, required as a principle for any cooperative initiative, should ensure that the selection process is conducted fairly.

Other issues stem from national implementation of the remedy Directives and the national legal regimen on the challenges of award procedures. Yet, a very clear and transparent cooperation agreement, and relevant contract notice, can call for an 'innovative' application of harmonized provisions and clauses that may spur the development of more effective templates for future contracts. That can be the case for innovative framework agreements, which may define a specific procurement strategy for the master contract, with a limited possibility to call off from it directly and the provision of subsequent mini-competitions for the award of higher value contracts. The remedies to be applied to the mini-competition might be the ones of the Member State concerned, thus verifying the full compliance to mandatory rules (as provided in the cooperation agreement).

Such sophisticated models of cooperation, as already noted, work on an exclusively voluntary base and require an ability to meet specific shared strategies. Since cross-border procurement covers contracting entities from different Member States and local agencies, it requires procurement professionals to be able to manage their own procurement systems, respectively, and also any applicable practices of the countries involved in the cross-border procurement agreement. Indeed, cross-border procurement poses challenges in addressing significant issues arising from variations in procurement regulations and practices and requires support to develop capacity to work out such administrative cooperation.<sup>(112)</sup>

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(111) See J. B. KAUFMAN, *Cooperative Purchasing: A US Perspective*, Chapter 2 in this book.

(112) *Ibid.*; EU Commission, *Public procurement – a study on administrative capacity in the EU*, cit.

The effectiveness of joint procurement requires an agreement stating how responsibilities shall be distributed, and also setting out provisions for the selection of participants, contract award, and contract execution.

Using the centralized purchasing activities of a different Member State is also an option. That model requires the purchasing entity to publish a contract notice stating that it is possible (but not necessarily mandatory) for contracting authorities from different Member States to call-off from a lot, either directly or after a mini-competition. In those circumstances, the central purchasing body in question could act as an intermediary. Indeed, having the central purchasing body fulfilling that role and coordinating the procurement process may be the easiest way to succeed in cooperation.

In other cases the purchasing entity may act as a wholesaler, thus resell goods and services to contracting entities from different Member States. Few central purchasing bodies in the EU have been acting that way so far.(113)

A recent ECJ decision stated that when a framework agreement is to be awarded, the tender documents should clearly specify which contracting authorities may benefit from the agreement and the maximum amount of purchases to be covered by the subsequent contracts.(114) Although the case in question focused on the provisions of the former Directive 2004/18, it is likely that the ECJ's conclusion would be the same under the Directive 2014/24, which has repealed and replaced Directive 2004/18 starting from April 2016, that includes similar yet more detailed provisions on framework agreements.

The horizontal public-public cooperation among contracting authorities from different Member States might serve as a legal basis for establishing a system of joint cross-border procurement superseding the individual award procedure of any contracting authority acting alone.

Administrative cooperation can be developed through occasional joint procurement initiatives even though they do not qualify as systematic and institutionalized acquisition systems like central purchasing bodies.(115) That is because they would allow two or more contracting authorities to 'perform jointly certain specific procurements', the need of which results from a shared interest in innovative projects.(116)

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(113) See I. LOCATELLI, *Process innovation under the new Public Procurement Directives*, Chapter 1 in this book.

(114) ECJ, 19 December 2018, Case C-216/17, *Antitrust and Coopservice Soc. coop. arl v. ASST Sebino et al.* The case involved a request for a preliminary ruling under Article 267 TFEU concerning the decision of a regional healthcare authority to accede to a contract for environmental services (classified as a 'framework agreement' within the meaning of EU law on public procurement) concluded by another healthcare authority without a new public tendering procedure; see G.M. RACCA and S. PONZIO, 'La scelta del contraente come funzione pubblica: i modelli organizzativi per l'aggregazione dei contratti pubblici', in *Dir. Amm.*, 2019, 33.

(115) Recital no. 71, Dir. 2014/24/EU.

(116) Art. 38, Dir. 2014/24/EU.

The joint implementation of an award procedure (either on behalf of the administrations involved, or executed by a CPB on behalf of other contracting entities) entails the joint duty to fulfill all obligations prescribed by the EU Directives and principles. Conversely, the contracting entity will be held responsible for any part of a procedure that has not been implemented jointly.<sup>(117)</sup>

On one hand, the rationale behind the aforesaid provisions on joint and cross-border purchasing stems from EU principles concerning the development of the internal market and the protection of competition through the demand side aggregation. On the other hand, it ties in with public interest in cooperation among central purchasing bodies (or individual contracting authorities) for overcoming the territorial, linguistic, and legal limits existing at national levels.<sup>(118)</sup>

As already mentioned, cooperation among contracting authorities may well enhance the procuring entities' potential, in terms of human resources and technology while favouring the harmonization of tender documents, procedures, contract clauses, and conditions of execution, all of which should encourage more enterprises to bid. All of this is expected to boost development and innovation in the internal market.<sup>(119)</sup>

(117) Recital no. 71, Dir. 2014/24/EU: 'Each contracting authority should be solely responsible in respect of procedures or parts of procedures it conducts on its own, such as the awarding of a contract, the conclusion of a framework agreement, the operation of a dynamic purchasing system, the reopening of competition under a framework agreement or the determination of which of the economic operators party to a framework agreement shall perform a given task'.

(118) Recital no. 73, Dir. 2014/24/EU. See EU Commission, *Staff Working Paper concerning the application of EU public procurement law to relations between contracting authorities (public-public cooperation)*, cit. 21. See also R. CAVALLO PERIN and D. CASALINI, 'Control over In-house Providing Organisations', in *Public Procurement Law Review*, 2009, 227-241; N. BASSI, 'Appalti pubblici comunitari (gli accordi internazionali in materia di)', in *Trattato di diritto amministrativo europeo* (M. P. CHITI, G. F. CARTEI and G. GRECO eds.), Milano, Giuffrè, 2007, 551; T. TATRAI, 'Joint Public Procurement', in *Journal of the Academy of European Law*, 2015; G. M. RACCA, 'Joint Procurement Challenges in the Future Implementation of the New Directives', in *Modernising Public Procurement: the New Directive* (F. LICHÈRE, R. CARANTA, and S. TREUMER eds.), DJØF Publishing, Copenhagen, 2014, 234-235. The use of a central purchasing body is a form of public-public cooperation, with reference to which the EU Court of Justice has already ruled on the risks that may result from collusion among public entities. See ECJ, 14 October 2004, *EC Commission v. Kingdom of the Netherlands*, in Case C-113/02, excluding in some cases: CGCE, 11 July 2006, *Federación Española de Empresas de Tecnología Sanitaria (FENIN) v. EC Commission*, C-205/03, § 26; ECJ, 26 March 2009, *Selex v. EC Commission – Eurocontrol*, in C-113/07 P, § 102. In these cases, the Court held that 'in order to assess the nature of that purchasing activity, we should not separate the activity of purchasing goods from the subsequent use made of them, and that the economic or not next use of the income of the product purchased necessarily determine the character of purchase'. On this aspect see A. SÁNCHEZ GRAELLS, *Public Procurement and the EU Competition Rules*, Hart Publishing, 2011, 150-151 and 165-166.

(119) R. CAVALLO PERIN, *Relazione Conclusiva in Atti del Convegno: Appalti pubblici: innovazione e razionalizzazione. Le strategie di aggregazione e cooperazione europea nelle nuove direttive*, cit., 37. See also G. L. ALBANO, F. DINI, and G. SPAGNOLO, 'Strumenti a Sostegno della Qualità negli Acquisti Pubblici', in *Quaderni Consip*, 2008, I, 3; L. FIORENTINO, 'Introduzione', in *Gli acquisti delle amministrazioni pubbliche nella repubblica federale* (L. FIORENTINO eds), Il Mulino, Bologna, 2011, 18; *Gli acquisti delle amministrazioni pubbliche nella repubblica federale* (L. FIORENTINO eds), Il Mulino, Bologna, 53; G. RACCA

Successful cooperation among contracting authorities requires a prior assessment of the appropriate scope and sector of aggregation. For instance, if purchasing at local levels is hampered by significant price differences caused by failures in competition (such as horizontal agreements among economic operators, other agreements, or cartels), a solution could be devised on a transnational basis and among contracting entities from different Member States.

The Directive provides that, unless international bilateral agreements between Member States have already been established, all necessary elements underpinning their legal relationship shall be set out within an agreement between the contracting authorities.<sup>(120)</sup> Similarly, the procurement strategy should be defined according to the cooperation goals, the relevant market, the territory, and the public administrations involved.

The establishment of joint-cross border public procurement requires a deep analysis of the existing regulatory models in order to identify the most suitable cooperation agreement as well as the best procurement strategy and means that the central administrations of each country involved can adopt. Third countries whose public administrations are not directly covered by the cooperation agreement may also be involved in the process.

It is worth remarking that national central purchasing bodies already manage important shares of the public procurement markets. Therefore, they may well play a decisive role in sharing domestic best practices and strategic approaches with their counterparts in joint procurement projects. These can increase the leverage of public purchasers, which is essential in certain markets dominated by a small number of market operators.<sup>(121)</sup>

Cooperation agreements define each party's responsibilities as well as relevant national provisions on the internal organisation of the procurement procedure, including key aspects of contract award and execution, the allocation of responsibilities, and the applicable EU and/or national laws. Aside from the assignment of competencies and responsibilities as appropriate, therefore, cooperation agreements thus take into account both the contract award and the administration phases. Addressing all these aspects means foreseeing competition between different legal system frameworks, and fostering European integration by harmonising tender documents and contract clauses in a design to implement tender procedures jointly and

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and R. CAVALLO PERIN, 'Organizzazioni sanitarie e contratti pubblici in Europa: modelli organizzativi per la qualità in un sistema di concorrenza', in *I servizi sanitari: organizzazione, riforme e sostenibilità. Una prospettiva comparata* (A. PIOGGIA, S. CIVITARESE MATTEUCCI, G. M. RACCA, and M. DUGATO eds), Maggioli Editore, Rimini, 2011, 197.

(120) Art. 39(4), Dir. 2014/24/EU; art. 57(4), Dir. 2014/24/EU; art. 114 TFEU.

(121) EU Commission, *Making Public Procurement work in and for Europe*, cit., 12.

outline ‘terms and conditions’ running parallel with contract execution according to national laws.

Cooperation agreements may also envisage forms of cooperation at different procedural stages – from issuing technical specifications to selecting economic operators. All this can be achieved by finding the least common denominator for the different countries involved. Another way to reduce burdens and increase participation is devising a procedure within which some requirements are mandatory only in certain legal systems.

Aside from the consortium-based model engaging central purchasing bodies from several countries, as discussed above, it is also possible to opt for a joint cross-border ‘Evaluation Team’ with experts from the different countries involved in the evaluation of offers, who could make recommendations about contract award to competent officers, or committees.<sup>(122)</sup> A more thorough evaluation could thus be made by complementing the inputs received with the opinions of experts from different countries. For example, a procurement strategy could envisage identifying different territorial lots or functional lots, based on what is set out in the cooperation agreement of interest.

In the process of harmonization of the tender documents and contract clauses, several differences to address may concern performance conditions such as invoicing, delivery of the ordered goods, and payment terms. Contract management may therefore need to be handled by each contracting entity separately in order to ensure compliance with the specific terms and conditions called for by their national laws, respectively.

Clearly, joint cross-border procurement requires a sophisticated organisational and contractual design to coordinate effectively the different procurement regimes at stake. Each central purchasing body involved in this model is expected to contribute to drafting of tender documents, and also to provide relevant information about its national legislation.<sup>(123)</sup>

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(122) Such was the case with the project PAPIRUS (‘Public Administration Procurement Innovation to Reach Ultimate Sustainability/Innovation in Hiring Public Administration to Achieve Maximum Sustainability’) which led to a ‘Joint Cross-Border Evaluation Team’ (JCBET) responsible in the formulation of technical specifications and the award criteria, wherein each PAPIRUS partner promoted and awarded its own contract, with its documentation, publication and respective award. See the chapter in this book: P. VALCÁRCEL FERNÁNDEZ, *The Relevance of Promoting Collaborative and Joint Cross Border Procurement for Buying Innovative Solutions*; A. SANCHEZ-GRAELLS, *Is joint cross-border public procurement legally feasible or simply commercially tolerated? A critical Assessment of the BBG-SKI JCBPP Feasibility Study*, cit., p. 8.

(123) A similar model of “joint evaluation team” has been implemented in the HAPPI project, which provided an example of a cross-border joint public procurement founded by the European Commission and a consortium of European partners consisting of procurement organizations (CPBs) in the health sector, by experts in the field of public procurement, by innovation agencies and academic institutions. HAPPI brings together partners from France (Réseau des Acheteurs Hospitaliers d’Ile-de-France, Ecole des Hautes Etudes en Santé Publique (EHESP), BPIFRANCE), the United Kingdom (NHS Commercial Solutions, BITECIC Ltd), Germany (ICLEI – Local Governments for Sustainability),

Choosing cross-border procurement to buy innovation means taking many challenges, which compels contracting entities to have well developed organizational skills. Managing such a major project, in fact, requires undertaking an extensive market analysis in order to identify the options available in a particular sector of interest. It also implies defining, with the aid of a committee appointed *ad hoc*, the subject matter of the contract/s to award, and the legal relationships binding the parties involved in contract award and execution within the framework of joint public procurement at EU and national level.

The EU Directive allows Member States to choose which kind of centralised purchasing activity contracting entities may opt for, for instance the centralised activities of a CPB acting either as a wholesaler or as an intermediary. Surprisingly enough, it seems that all Member States except Italy have implemented the Directive with a broader scope, so as to allow either approach.

Italy, in fact, allows its contracting entities to use the purchasing activities of a CPB from another Member State only when the CPB acts as wholesaler.<sup>(124)</sup> Such a restrictive implementation does not exclude agreements for joint cross border cooperation, but limits the options available when buying under framework agreements with Member States. Consequently, a reciprocal basis principle could limit cross-border cooperation opportunities.

The execution of purchasing activities by a central purchasing body located in another Member State shall be conducted in accordance with the legal provisions of that same country, including substantive rules and remedy rules.<sup>(125)</sup>

The fact that joint procurement has to be carried out complying with the rules of the CPB's home country makes joint procurement a strategy going beyond the scope of maximising the economic benefits of centralised procurement. Indeed, it opens the way to different forms of wider participation and competition among economic operators, which the aggregation of public demand might foster as a logical-legal antecedent to tenders.<sup>(126)</sup>

Public-public cooperation allows contracting authorities to adhere to the framework agreements entered by central purchasing bodies with a Member State as an alternative to their own need-meeting process at national level.

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Italy (University of Turin and the Piedmont Region Client Company, SCR), Belgium (MercurHosp – mutualisation hospitalière), Luxembourg (Fédération des Hôpitaux Luxembourgeois (FHL), Austria (the Federal Procurement Agency (FPA) – Associate partner ) and Spain (FIBICO – Associate partner). For a description of the project activities, see G. M. RACCA, *The Happi experience*, op.cit., forthcoming. See also S. PONZIO, 'Joint Procurement and Innovation in the new EU Directive and in some EU founded projects', in *Ius Publicum Network Review*, 2/2014.

(124) Art. 43 of Legislative Decree no. 50 of 18 April 2016 (Italian Public Procurement Code) which recalls art. 37(13) of the same Legislative Decree.

(125) Recital no. 73, Dir. 2014/24/EU.

(126) I. H. ANCHUSTEGUI, *Collaborative Centralized Cross-Border Public Procurement: Where are we and where are we going to?*, in *Centralização Das Compras Públicas*, 2018, forthcoming.

That approach foreshadows a ‘tender of tenders’ or second-tier award procedure.(127) In principle, it allows contracting authorities to bypass dysfunctional procurement systems or severe corruption in their own country. Such a model of cross-border procurement promises a greater impact on the economic, social and territorial cohesion of the European Union.(128)

## **6. Innovative Joint Cross-border Procurement Strategies through Framework Agreements**

Cross-border cooperation framework agreements seem to be the most flexible tools for sophisticated strategies among contracting authorities from different Member States. Cross-border procurement may mean gaining very high value, but it may also yield sophisticated strategies based on market analyses to pursue industrial policy goals. Such strategies may contribute to safeguarding competition and ensuring SMEs’ access to opportunity, for example through more (and appropriately sized) lots. By defining and translating similar and harmonized clauses, cross-border procurement may help overcome legal and linguistic barriers to procurement trade arising from conflicts among different national provisions.(129)

The choice of the contractual model to adopt in order to carry out a joint cross-border procurement is closely related to the definition of the underlying cooperation agreement. Under the Procurement Directives, framework agreements have become a stimulus for innovation and for the access of SMEs to public procurement markets through aggregation of public demand and the division (and fair allocation) of that demand into lots by territory or sector.

(127) See R. CAVALLO PERIN and G. M. RACCA, *Plurality and Diversity of Integration Models: The Italian Unification of 1865 and the European Union Ongoing Integration Process*, cit.. See also R. CAVALLO PERIN, *Appalti pubblici: innovazione e razionalizzazione. Le strategie di aggregazione e cooperazione europea nelle nuove direttive*, cit., 36.

(128) G. M. RACCA and S. PONZIO, *Nuovi modelli organizzativi per il ‘joint procurement’ e l’innovazione dei contratti pubblici in Europa in Compra conjunta y demanda agregada en la contratación del sector público. Un análisis jurídico y económico* (P. VALCÁRCEL FERNÁNDEZ eds), Thomson-Aranzadi, 2016. As for territorial cohesion, however, it is noteworthy that a recent document by the European Court of Auditors (*ECA Special Report 15/2017, Ex ante conditionalities and performance reserve in Cohesion: innovative but not yet effective instruments*) complained that only 2 of the 57 action plans suggested for public procurement in the ECA General Report 4 were effectively implemented. In fact, in another special report (*ECA Special Report 10/2015, Efforts to address problems with public procurement in EU cohesion expenditure should be intensified*), the ECA also noted that ‘failure to comply with public procurement rules has been a perennial and significant source of error. Serious errors resulted in a lack, or complete absence, of fair competition and/or in the award of contracts to those who were not the best bidders’. In a following report (*ECA Special Report 17/2016*), the ECA also noted that ‘EU institutions can do more to facilitate access of economic operators (especially of small and medium-sized enterprises) for example by simplifying the rules to the fullest possible extent and by removing unnecessary hurdles which make life difficult for potential tenderers who want to identify procurement opportunities offered by the EU institutions’.

(129) Recital no. 73, Dir. 2014/24/EU.

In general, efficiency has improved because of a wide range of framework agreements that may be awarded; the number of awardees (single or multi-supplier framework agreements) may vary as well as the degree of accuracy of the contractual conditions ('closed' or 'open'). The Directives provide, for 'open' frameworks, for a reopening of competition so that local authorities may tailor their requests to their needs in the purchasing phase, which is particularly useful for cross-border joint procurement.(130)

The Procurement Directives provide for an additional innovative model of framework agreement (the so-called 'mixed' or 'hybrid model'). Such a model, where explicitly provided for in the tender documents, allows agencies to buy directly through the framework agreement (as in 'closed' model) or to re-open the tender between the economic operators under previously specified terms and conditions. This model seems to fit the joint cross-border award of a master contract that might allow users either to call off under their terms and conditions or to launch a mini-competition.

The possibility of using both options (re-opening the tender or not) must be specified in the tender documents as to avoid ambiguous interpretations of the rules governing procurement.(131)

An interesting and innovation-friendly national solution may also consist in having framework agreements, whose subject-matter is the supply of innovative goods and services. An annual expenditure analysis permits to define the categories of products and services and the related thresholds for which regional bodies, their consortia and associations, as well as National Health Service bodies, are obliged to join the framework agreements.(132)

In this way the choice of innovative solutions is encouraged with a quick entering in the market. Such a model might be experimented also cross-border to encourage participation of innovative suppliers.

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(130) Art. 33(4), Dir. 2014/24/EU. G. M. RACCA – G. L. ALBANO, *Collaborative Public Procurement and Supply Chain: the European Union Experience* in *The SAGE Handbook of Strategic Supply Management* (C. HARLAND, G. NASSIMBENI and E. SCHNELLER eds.), SAGE Publishing, London. G. L. ALBANO, C. NICHOLAS, *The Law and Economics of Framework Agreements*, Cambridge University Press, 2016. OECD, *Framework Agreements*, Public Procurement Brief 19, August 2011. CCS, *Guidance on Framework Agreements*, October 2016. The reopening of competition 'shall be based on the same terms as applied for the award of the Framework Agreement and, where necessary, more precisely formulated terms, and, where appropriate, other terms referred to in the procurement documents for the framework agreement'. OGC, *Framework Agreements*, September 2008. M. ANDRECKA, *Framework Agreement Transparency in the Call-Off Process*, in *EPPPL*, 2015, 231. G.M. RACCA and R. CAVALLO PERIN, *Framework Agreements and Joint Procurement: the Future Challenge*, presentation held at the University of Nottingham (24-25 June 2013).

(131) C. R. HAMER, 'Regular purchases and aggregated procurement: changes in the new Public Procurement Directive regarding agreements frameworks, dynamic purchasing systems and central purchasing bodies', in *Public Procurement Law Review* 2014, 4, 201-210.

(132) G. L. ALBANO, A. CIPOLLONE, M. SPARRO, *Divisione in lotti, partecipazione e competizione nelle gare d'appalto*, Quaderni Consip, 2, 2016, 13. See <http://www.consip.it> on innovative framework agreement.

In the public procurement market, demand aggregation allows governments to obtain economies of scale, lowering prices and transaction costs, and also to develop professionalism and to achieve strategies in defining specific objectives to be pursued through public tenders (social, environmental, innovation).

The forms of cooperation among contracting authorities from different Member States and, among these, the role played by framework agreements, may encourage further risk-benefit sharing in developing innovative cross-border procurement.(133)

### **7. The Execution Phase of Joint Cross-border Contracts**

The Procurement Directives notably provide for cooperation agreements which may define the procurement phase, as well as contract management and execution.(134)

As the execution of the contract is beyond the scope of the Procurement Directives, the relevant legislation is supplemented by national provisions and the European rules on international private law. These allow for the choice of the set of national rules to be applied to the execution phase that can differ from that of the award but can thus promote ‘competition’ among different legal systems.(135)

Each Member State can provide different terms and conditions for the execution phase. Nonetheless, the contracting authorities involved in joint procurement experiences might frame contract clauses, whenever possible, in accordance with regulations of the other partners in order to minimise the legal differences and facilitate the effective performance of the contract.

In this context, the tender documents could present a common set of rules which could serve as a platform for discussing new legal tools and models at the European level. In other words, administrative cooperation might serve as the basis for future European regulation in those fields – e.g. the execution of the contract – which are currently outside the scope of the Procurement Directives.

An example arises in providing a common term of payment or the pre-determination of the commitment by each partner in relation to each product or

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(133) Recital no. 73, Dir. 2014/24/EU. See: G. L. ALBANO, ‘Demand aggregation and collusion prevention in public procurement’, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (G. M. RACCA and C. R. YUKINS eds), *op. cit.*, 155; G. L. ALBANO and C. NICHOLAS, *The Law and Economics of Framework Agreements*, *op. cit.*

(134) Art. 39(4), Dir. 2014/24/EU.

(135) G. M. RACCA, ‘The role of third parties in the execution of public contracts’, in *Contrôles et contentieux des contrats publics | Oversight and Challenges of public contracts* (L. FOLLIOT-LALLIOT and S. TORRICELLI eds), Bruylant, Bruxelles, 2018, 415.

service to be performed.(136) This process should be kept consistent with the subject matter of the contract, in accordance with rules which comply with the existing regulations and always in keeping with mandatory rules.(137) A similar issue might arise in relation to bond provisions applied to suppliers awarded contracts in certain legal systems or applied in anticipation of award in others. In a cross-border framework agreement it would seem problematic to apply such different domestic rules and a compromise solution might be to require the successful tenderer the minimum amount admitted as a bond.

The evidence of such different provisions might prompt some to propose a more effective and harmonized rule.

Conversely, the contracts' execution might be performed according to the national law of the country of destination, as provided in the agreement. Such choice appears particularly suitable in case of awarding framework agreements on a cross-border basis, where normally the law of execution of the subsequent contracts depends on the place of the registered office of the beneficiaries of the framework.

It might be of interest to recall that, in order to enter into contracts under a framework agreement, the potential beneficiaries do not have to be directly parties to the relevant framework agreement, as recently confirmed by the ECJ.(138) The only requirements are that the tender documents clearly specify both the contracting authorities that may be potential beneficiaries of the framework agreement and the maximum amount of purchases to be covered by the subsequent contracts. In this model, it is possible that only one among the contracting authorities involved in the project signs the framework while

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(136) In the HAPPI case, in order to smooth the potential negative impact of such differences on the award phase, the project leader and the participants created a special document, explaining the call-off procedure for each country, and sent it both to the supplier and to all contracting authorities which were interested in calling off. See: EU Commission, *Making Public Procurement work in and for Europe*, cit.; G. M. RACCA, *Joint Cross-Border Procurement of Innovative Solutions in the Healthcare Sector. The HAPPI project experience*, cit.; EU Commission, *Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States*, report written by BBG and SKI, Brussels, March 2017.

(137) This question was addressed in the HAPPI case where the Italian rules on mandatory deposit pursuant to art. 103 of the Italian Public Contract code (Legislative Decree no. 50 fo 18 April 2016) should have been harmonized with the French legislation, under which it is not compulsory, except in the case of a request for anticipated payment by the successful tenderer (art. R2191-3, Code de la Commande Publique – Décret n° 2018-1075 du 3 décembre 2018). A compromise solution has therefore been proposed where the successful tenderer had to guarantee in Italy a minimum value deposit.

(138) ECJ, 19 December 2018, Case C-216/17, *Antitrust and Coopservice Soc. coop. arl v. ASST Sebino et al.*, § 56. See also Advocate General's Opinion, § 65, according to which 'There is no reason why the status of party to a framework agreement should mean that a party that has that status must have signed the agreement or even have played a direct part in its conclusion. As the Consiglio di Stato (Council of State) points out, the provisions of civil law governing representation and *negotiorum gestio* permit a person (in this case, an ASST) to conclude a binding agreement on behalf of others where those others have entrusted that person with this task or ratify it *a posteriori*'.

the other partners, if interested, remain free to submit orders (*call-offs*) and enter into the subsequent contracts.

Nevertheless, it should not go unmentioned that if contracting authorities agree on having their domestic law apply to contract execution, tenderers might find it problematic to accept asymmetrical choice of law conditions as part of the tender documentation. As a consequence, tender costs might be raised due to additional transparency requirements concerned with the law applicable to the contract during execution. Disconnecting public procurement and contract laws might create difficulties especially in countries that keep differentiated public contract law regimes. A decision like that might even trigger additional legal risks insofar as there is interaction of pre-award and post-award documentation and requirements, such as call-offs without mini-competition within framework agreements. Nonetheless all these issues can be addressed in the cooperation agreement and clearly explained in the contract documents. The tenderers might know that they bid for a cross-border lot of a framework that would imply the possibility (not mandatory) to deliver according to the master contract and the terms and conditions of different Member States. Thus an opportunity to easy entrance in a new market could be provided.

Given all of these constraints, in all the joint cross-border projects experienced before the entry into force of the last Procurement Directive, the idea to purchase goods and services from a CPB was truly greatly innovative and challenging. In the mentioned HAPPI project the CPBs signed the framework agreement on behalf of the partners that subsequently provided access free of charge to end users interested in purchasing the goods or the services covered by the agreement. Each subsequent contract had, then, to be concluded by individual beneficiary institutions (i.e. procuring entities) with the economic operator (holder of the contract) on the basis of what was provided for in the framework agreement and of what was evidenced by non-binding documents (e.g., a letter of consultation issued by the contracting establishment) which, however, could not make any substantial change to the terms defined in the framework agreement.

From a demand-side standpoint, the joint cross-border procurement may enhance the administrative, legal and coordinating capacities and resources of contracting authorities among Member States of the Union. A further aspect requiring specific consideration is that economic players, especially SMEs, do not always have the means or an adequate degree of flexibility in coping with the legal risks involved in cross-border activity or with the administrative complexities in different Member States. Therefore, the purpose of this process of 'self-regulation' is the integration, consolidation and homogenization of different provisions so that the enterprises, especially SMEs, are not

discouraged from exploiting the opportunities afforded by the internal market. The next challenge is to prove that evolution through electronic means and open and transparent platforms.

## *8. Lessons Learned from Transatlantic Experiences*

Cross-border procurement poses challenges which virtually cross the Atlantic, and which require shared capacities and strategies. Cross-border procurement in the U.S. and in the EU face common issues of policy, competencies, conflicts of law, jurisdictions and remedies.

The experience to date in cross-border procurement proves that it may significantly improve transparency, integrity and efficiency, and encourage the emergence of more effective contract rules as well. The voluntary choice of cooperation among contracting entities and mainly professional agencies provides the opportunity for administrative cooperation, as sister agencies define their way forward. A further understanding of how jurisdiction rules can be reconciled will help resolve pressing issues beyond joint procurement – how to assess mandatory grounds of exclusion, for example, and how to use tender evaluation to encourage innovation.

From the European standpoint, this will help European integration and the growth of the internal market; this suggests that Member States should not discourage such administrative cooperation, so that European citizens and firms can take advantage of this open and transparent cooperation that would, with time, improve quality in procurement.

Joint procurement is also of utmost importance for fostering innovative procurement of cross-border interest, for improving outcomes, and for leveraging all the advantages of the internal market, although sometimes in different and asymmetric ways and sectors.

The focus on integration helps explain why Europe goes much further in fostering cross-border procurement than the U.S federal government, and why the European regulatory regime seems more similar to voluntary cooperation among countries.

Uniquely, the EU has embraced joint procurement with the objective of promoting goals other than simply ensuring cost-savings, such as encouraging cross-border participation of SMEs, counteracting cartels, assuring integrity and efficiency, furthering environmental sustainability and developing circular economy tools. Interestingly, despite convergence, the EU's ideal of 'Unity in Diversity' allows EU Member States to promote those 'other goals,' which can be shared cross-border on a case-by-case basis. More pragmatically, joint (or

cooperative) in the United States procurement is used as leverage for gaining more efficiency and savings, including across borders, but without Europe's market integration goals. Nonetheless, in the long run such experiences show how cross-border procurement might improve procurement systems from without while also permitting them to pursue specific policy goals, not only nationally defined but also at regional and local levels. This might reconcile the imperative of local choice with the integrity and efficiency of transnational procurement systems.

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# CHAPTER 4

## The Relevance of Promoting Collaborative and Joint Cross Border Procurement for Buying Innovative Solutions(1)

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### 1. Introduction

The ultimate aim of this chapter is to highlight the leading role of public procurement in encouraging innovation, and how to boost this role through the promotion of joint cross-border procurement, or at least through collaboration between and among the different European Member States. The specificity of the object of the purchase makes innovation, as we will attempt to explain, especially useful in maximising the joint efforts of contracting authorities from different Member States.

With this in mind, it seems appropriate to analyse how innovation has found an important niche in public procurement law. Given the stated perspective, a basic overview on the possibilities of cross-border cooperation is likewise provided, more particularly, on those forms of cooperations which are encouraged by the current EU public procurement law. Moreover, this chapter will cover a number of concepts that are particularly relevant in enhancing the results of cross-border innovation procurement.(2) Lastly, a number of successful joint or collaborative cross-border innovation procurement experiences are discussed with a view to ascertaining drawbacks, if any, and identifying some of the lessons therefrom.

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(1) This paper has been written under the Research Project: “El tiempo de las reformas administrativas: hacia la excelencia en la contratación pública (*Smart Procurement*) a través de compras eficaces, estratégicas y transnacionales”, funded by the Ministry of Economy, Industry and Competitiveness, Spanish Government. (Ref: DER2015-67102-C2-2-P); a prior version of this piece was published through the *Ius Publicum Network Review* ([www.ius-publicum.com](http://www.ius-publicum.com)), issue 1, 2017.

(2) R. CAVALLO PERIN and G.M. RACCA, “Administrative Cooperation in the Public Contracts and Service Sectors for the Progress of European Integration”, in *European Democratic Institutions and Administrations Cohesion and Innovation in Times of Economic Crisis* (F. MERLONI and A. PIOGGIA eds), Berlin, Springer, 2018.

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## **2. The Public Procurement of Innovative Solutions as Public Strategy: The Importance of ‘Demanding’ Innovation by the Public Sector**

The positive image that accompanies the idea of ‘innovation’, which is usually linked to positive achievements in many aspects such as efficiency, productivity or competitiveness, is well known. In fact, it is considered an indispensable ingredient for sustainable growth. Innovation is likewise acknowledged as a key driver of economic growth, thus, governments use diverse mechanisms in trying to promote innovation in both public and private sectors.

The European Union has placed innovation at the heart of the Europe 2020 Strategy by means of the emblematic Innovation Union initiative. The aim is to structure an exhaustive strategy for knowledge-based innovation and to make Research & Innovation a priority for all EU countries in developing innovation policies.

However, as has been suggested, there are many instruments to promote innovation policies, and, until a few years ago, the trend of public policy that was developed in this area was based on the promotion of innovation through the use of instruments that reacted to developments in the private sector (e.g., subsidies) and not so much from demand previously defined by the public sector.

Nevertheless, various studies have shown that ‘public demand’ can be a major potential source of innovation, which is even better than many other existing instruments that are used in spurring innovation in public policies.(3)

Edler and Georghiou discussed a number of empirical studies that were conducted in the 1970s and the beginning of the 1980s. These included studies that compared R&D subsidies and State procurement contracts without direct R&D procurement. Interestingly, the authors concluded that over a longer period of time, public procurement had triggered greater innovation in more areas than R&D subsidies. They also analysed the quantitative and qualitative meaning of State demand for innovation and concluded that procurement policy “is a far more efficient instrument to use in stimulating innovation than any of a wide range of frequently used R&D subsidies”. Similar conclusions were reached in more recent analyses.(4)

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(3) G.M. RACCA, “Collaborative and strategic procurement for supporting industrial innovation”, in *La commande publique, un levier pour l’action publique?*, (E. Muller ed.), Paris, Dalloz, 2018, pp. 121 and ff.

(4) J. EDLER and L. GEORGHIOU, “Public procurement and innovation – Resurrecting the demand side”, *Res. Pol.*, 36, 2007, pp. 949-950. These authors explained that in a survey of more than 1,000 firms and 125 federations, over 50% of respondents indicated that new requirements and demand were the main source of innovations, while new technological developments within companies were the major driver for

The results of the above-mentioned studies were sharply in contrast to the low weight that had been given to public procurement as a tool for innovation in public policies. For many years, the potential and challenges posed in using public procurement for buying innovation have been largely overlooked as means of promoting innovation by the public sector.<sup>(5)</sup> With a few exceptions, public procurement has been ignored for this purpose, both conceptually and in practice; arguably, this may be attributed to the introduction of more stringent competition regulations across the European Union which has proven a major factor in the declining use of procurement for innovation.<sup>(6)</sup>

The relevance of promoting innovation from the demand side has taken a new and important perspective. As claimant, the public sector decides and imposes on the private sector what it wants to acquire, what it seeks to achieve, and what it will buy.<sup>(7)</sup>

Of the available instruments that stimulate innovation by the public sectors, public procurement has been revitalized as a truly rich tool. It has become a useful piece of the innovation policy at the European and national levels. The significant impact of public procurement in the EU economy has led to the acknowledgement of its large potential to achieve a fixed target. In fact, public procurement has been estimated to be worth around 14% of EU's GDP,<sup>(8)</sup> thereby making the capacity of European public administration to act on innovation by steering demand not at all irrelevant.

In other words, public demand, when oriented towards innovative solutions and products, has shown a great potential to improve the delivery of public policy and services, often generating improved innovation and benefits from the associated spillovers. From that perspective (demand side), public procurement should be the key element to promote innovation policies. In support thereof, the European Commission has recently issued "practical guidance on innovation procurement".<sup>(9)</sup>

The leading role of innovation is in line with the "strategic conception of public procurement". 'Strategic procurement' occurs when the demand for

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innovations in only 12% of firms. An analysis of the Sfinno data base collecting all innovations commercialized in Finland during between 1984 and 1998 showed that 48% of the projects leading to successful innovation were triggered by public procurement or regulation. *See also*, D. DRAGOS and B. RACOL, "Comparing Legal Instruments for R&D&I: State Aid and Public Procurement", *EPPPL*, 2017, p. 408.

(5) J. EDLER and L. GEORGHIOU, "Public procurement and innovation – Resurrecting the demand side", *op. cit.*, p. 949.

(6) *Ibid.*, p. 950.

(7) C. SOTOMAYOR LUIS, G. MORENO and J. MANUEL, "Compra Pública Innovadora. Fundamentos e instrumentación", *INAP*, 2013; G.M. RACCA, "Collaborative and strategic procurement for supporting industrial innovation", in *La commande publique, un levier pour l'action publique?*, *op. cit.*

(8) R. WILLIAMS, "Commission guidance on innovation procurement", *PPLR*, 2018, 5, NA141-NA142, 2018.

(9) Guidance on Innovation Procurement, Brussels, 15 May 2018, C(2018) 3051 final.

certain technologies, products or services is encouraged in order to stimulate the market.<sup>(10)</sup> For some time now, the view of public procurement as a mere instrument in the hands of the public sector for the acquisition of goods and services has been outdated. Little by little, and thanks to its importance in the economy, evidence is coming to light of this sector's potential for promoting different types of public policies, such as environmental, social and gender policies, and now also those linked with innovation.<sup>(11)</sup>

The EU has shown a firm commitment to promoting this strategic vision of public procurement, an approach that has gradually been reflected in different European documents. At the policy level, it began to take shape clearly in the Directives of 2004 and has been consolidated and intensified in the Directives of 2014. It is now assumed that public procurement can serve multiple objectives, and promoting innovation is potentially one of them.

With regard to innovation, public procurement can play a relevant role, not so much through ordinary purchases to achieve standard products, but through the purchase of new technologies and innovative products, services or processes. From this point of view, public procurement of innovation is a demand-side instrument and can be defined as the purchase "of a not-yet existing product or system whose design and production will require further, if not completely novel, technological development work".<sup>(12)</sup> In this context, the requirements that must be met are predefined by the public sector (by the contracting authority) through a list of functional requirements for the demanded product. The realization and design of the innovative product are in the hands of the awardee of the contract for innovation. The two principal reasons for the use of this policy tool are to satisfy and improve the supply of public services, and to meet political goals by stimulating demand in different areas such as transport, energy, environment, health, education, information and communications, where public authorities have strong social responsibilities. The public demand for innovation in those areas has a great potential to stimulate development in those markets.<sup>(13)</sup>

The demand approach is fundamental in public procurement because it is the public sector that 'decides', and 'imposes' on the products or services that

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(10) J. EDLER and L. GEORGHIOU, "Public procurement and innovation – Resurrecting the demand side", *op. cit.*, p. 953.

(11) J. GARCIA (ed.), *Contratación Pública estratégica*, Cizur Menor, Thomson Reuters/Aranzadi, 2013; T. ARNAIZ, "Comprando para asegurar nuestro futuro: la utilización de la contratación pública para la consecución de los objetivos políticos de la Unión Europea", *Observatorio de los contratos públicos 2010*, Madrid, Civitas, 2011, pp. 90 and ff. See also, EC, "Strategic Public Procurement: Facilitating Green, Inclusive and Innovative Growth", *EPPPL*, 2017, p. 219.

(12) B. ASCHHOFF and W. SOFKA, "Innovation on demand – Can public procurement drive market success of innovations?", *Research Policy*, 2009, p. 1236.

(13) *Ibid.*

will be bought. So the potential of ‘public demand’ in certain economic sectors where the public sector has relevant responsibilities (e.g., healthcare, transport services, new technologies, information & communication technology (ICT), education, sustainable construction, water and waste challenges) and constitutes one of the biggest buyers is indisputable.<sup>(14)</sup>

The procurement of innovation has great potential to stimulate sustainable growth and wellness. In fact, buying innovation helps create jobs and boost competitiveness of the European industry and SMEs.

As already highlighted in some EU documents,<sup>(15)</sup> it is imperative to find innovative and sustainable solutions to stimulate the market amidst the serious economic challenges that Europe is currently facing, though demand for innovative solutions through public procurement may still be taken with a grain of salt.

### ***3. Origin and Development of the Idea of Using Public Procurement as an Instrument for Fostering Innovation in the EU***

#### **3.1. Innovation in EU soft law.**

##### **Key milestones and the promotion thereof with the approval of the Europe 2020 strategy**

EU legislation has consolidated the notion that public procurement can foster important objectives linked to public policies. In particular, the Directives of 2014 on public procurement open the possibility of stimulating environmental and social objectives through contracts concluded by the public sector.

Prior thereto, references to innovation in EU legislation remained scant, and the need to foster research and development was only alluded to tentatively. For instance, recital 23 and Article 16.f) of Directive 2004/18 only included two generic references to innovation, *i.e.*, it only determined that pre-commercial public procurement was excluded from its scope of application. It was only after the Lisbon European Council of 2000 when the European institutions started to devote special attention to innovation by underscoring its crucial role in maintaining the social economic development and well-being amidst the challenges in an increasingly competitive environment.

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(14) G.M. RACCA, “Collaborative and strategic procurement for supporting industrial innovation”, in *La commande publique, un levier pour l’action publique?*, *op. cit.*; J. EDLER and L. GEOGRHIU, *Public procurement and innovation*, *op. cit.*, pp. 949-963.

(15) [www.innovation-procurement.org/about/](http://www.innovation-procurement.org/about/).

Among other objectives, the Lisbon Strategy (development plan for improving EU competitiveness for the period 2000-2010) paved the way for the increase in opportunities to encourage innovation through public procurement. Its guidelines were specified or defined by the Barcelona Research Council in 2002, where the challenge was set to increase public expenditure in this setting to up to 3% of the GDP by 2010, a goal which was never reached.

Since then, the Commission has gradually succeeded in promoting innovation with a view to converting it into one of the fundamental social values that Member States need to foster. It is worth noting that the Commission has approved different documents appearing in what is known as 'EU soft law', which provide substantial support for the new setting, to wit:

- 1) The 2003 Communication from the Commission: "Investing in research: an action plan for Europe", a document that highlighted the level of research investments in the EU *vis-à-vis* share in GDP, *i.e.*, in 2001, the level of research investment in EDU was only 1.9% of GDP compared to 2.7% in the US and 3% in Japan. This gap was considered to have worrying consequences for the long-term potential to stimulate innovation, growth and employment creation in Europe. As a result, the Action Plan was formulated which sets, among others, an action to *redirect public resources towards research using* the possibilities offered by Community frameworks such as public procurement rules.
- 2) The Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions: More Research and Innovation – Investing for Growth and Employment: A Common Approach, Brussels, COM(2005) 488 final.
- 3) The Aho Group Report: Creating an Innovative Europe (2006). This Report was further elaborated on by an Independent Expert Group on R&D and Innovation appointed following the Hampton Court Summit. At the Hampton Court Summit on 27 October 2005, Heads of State and Government decided to give higher priority to the key issues on which Europe needs to act to address the challenges of globalisation. First among these issues were research and innovation. The Commission asked a small group of four high-level experts to assess the situation and make proposals to boost Europe's research and innovation performance. In the report public procurement is mentioned as one of the ways to foster innovation.
- 4) Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Pre-commercial Procurement: Driving

- innovation to ensure sustainable high quality public services in Europe, Brussels, COM(2007) 799 final (14.12.2007)
- 5) The Lead Market Initiative (2008-2011), launched by the EU to seek the leadership of its companies in six markets classified as crucial for the development of the European economy. This initiative was committed to using public procurement as one of the tools available for achieving said leadership. More specifically, it encouraged the public procurement of innovative technologies in either of its two modalities: Pre-Commercial Procurement (PCP) or Public Procurement of Innovation (PPI).
  - 6) Europe 2020 (the successor to the Lisbon strategy) and its well-known initiative, Innovation Union: turning ideas into jobs, ecological growth and social progress (COM (2010) 546 final), addresses the implementation of swifter, more effective standardisation in the use of public procurement as an interesting approach for encouraging innovation.
  - 7) The “Horizon 2020, Research and Innovation framework programmes” (COM (2011) 808 final), adopted on 30 November 2011.

In relation to the “Europe 2020 Strategy”, innovation is clearly high on its agenda. The document highlights how the economic and financial crisis demonstrated the European economy’s structural weakness and gave rise to a sharp deterioration in the social and economic setting. Hence the Strategy’s objective is to ensure that economic recovery is supported by a set of reforms aimed at constructing solid foundations for growth and the creation of jobs within the European Union up to 2020, taking into account the long-term challenges posed by globalisation, the strain on limited resources and an ageing population.

If we analyse the perspective from which, in this Strategy, future growth is considered within the framework of the EU, it is easy to see that the pursuit thereof goes hand in hand with innovation. This is conceived as the plan for intelligent, sustainable growth drawn up by the European Commission for the coming decade, and established therein are the basic lines of action for the next ten years, aimed at achieving comprehensive development which will enable the Union to recover its status as a world leader.

As regards public procurement, the Europe 2020 Strategy calls for it to be employed to:

- a) Improve framework conditions for business in those markets where the public sector is a prominent purchaser to innovate, making full use of demand policies;
- b) Encourage the change towards being a more resource-efficient economy (e.g. with low carbon emissions) fostering the widespread use of ecological public procurement;
- c) Help to support the business setting, in particular for innovative SMEs.

In short, research and innovation play a key role in the Europe 2020 Strategy. One of its mantras would be reflected by the phrase “From the idea ... to the market,” stressing the need for closer relationships with operators and firm support for achievable projects, to prevent hundreds of millions of euros invested through research subsidies from failing to produce marketable results, as has been the case to date. That is why it is said that the aim with this approach is to oust the subsidy model in favour of a model based on demand through public procurement. It is not a case of vilifying the subsidy model until its demise, rather of resizing it, combining its use, in those cases where it may be more appropriate, with the fostering of innovation from the demand side.

### 3.2. The strengthening of the CPI through Directive 2014/24/EU

The 2014 EU Directives on public procurement consolidate the entire process in public procurement. Unlike the classical directive, in Directive 2014/24/EU of the European Parliament and of the Council (approved on 26 February 2014 and repealing Directive 2004/18/EC) on public procurement, the European Institutions highlight the relevant role of public procurement in stimulating innovation, so much so, that it is “of utmost importance to fully exploit the potential of public procurement to achieve the objectives of the Europe 2020 Strategy. In this context, it should be recalled that public procurement is crucial to driving innovation, which is of great importance for future growth in Europe”.

In fact, recital 47 of Directive 2014/24/EU expressly provides that: “Research and innovation, including eco-innovation and social innovation, are among the main drivers of future growth and have been put at the centre of the Europe 2020 strategy for smart, sustainable and inclusive growth. Public authorities should make the best strategic use of public procurement to spur innovation. Buying innovative products, works and services plays a key role in improving the efficiency and quality of public services while addressing major societal challenges. It contributes to achieving best value for public money as well as wider economic, environmental and societal benefits in terms of generating new ideas, translating them into innovative products and services and thus promoting sustainable economic growth”.

The ultimate aim consists, among others, of the attempt to attain the 2010 targets such as the increase in spending on Research and Development (R&D) up to 3% of the EU’s GDP by 2020. Compliance with this objective could also be helped through the use of public procurement. It is widely believed that, in addition to being a good thing *per se*, owing to the improvement it can entail

for the provision of public services, it will also improve citizens' quality of life and, at the same time, make it possible to create 3.7 million jobs, as well as to increase the annual GDP by around 800 billion euros by 2025.

The foregoing would also help the EU to recover its status as a world leader on both economic and social levels.

This is how we can assert that the promotion of entrepreneurial innovation through public procurement has become a key objective, particularly as of the approval of the 2014 Directives.

References to innovation now abound in Europe's principal text on public procurement; if we simply count the times that the word innovation is cited in the Directive, we will see that it is mentioned around 70 times.

This work is not a treatise aimed at studying public innovation procurement in all its facets. Hence, in addition to the foregoing, from the Directive we shall now draw attention to only two further aspects.

The first, the efforts that the Directive itself makes to provide a concept of innovation, which is amply endorsed in Article 2.1. (22) of the same.

The Directive states that: 'innovation' means the implementation of a new or significantly improved product, service or process, including but not limited to production, building or construction processes, a new marketing method, or a new organisational method in business practices, workplace organisation or external relations inter alia with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth".

If we analyse the concept of innovation proposed by the Directive, we can see that not only does it refer to something that previously did not exist and which is created from scratch (either a product, service or process), but also to something which already existed and which is significantly improved upon. Furthermore, that which has already been designed but which has yet to reach the market, or has done so in a limited manner, could also be considered innovative.

Besides the concept appearing in the Directive, if we conduct a general study of 'innovation' in the academic-scientific setting, we discover that it alludes to a broad, complex phenomenon subject to analysis from multiple different stances, levels and perspectives. Perhaps this is why myriad definitions have been put forward as to what should be understood by 'innovation', without it being easy to pinpoint one that is sufficiently broad and comprehensive for the scientific community to agree to accept it as being sufficiently all-embracing of all the elements it needs to cover.

In this work, and owing to the material setting affected by public procurement (namely, the acquisition of goods and services in the framework of the

public sector), the concept of innovation that interests us will be that traditionally linked to industrial development, the economy, markets and technology. Notwithstanding this, owing its particular impact in the sphere of the public sector, we cannot fail to mention the expansion undergone by the concept of innovation, opening up to issues of a social nature. Indeed, the social element is an aspect or perspective that has been incorporated more recently into innovation, giving rise to the notion of ‘social innovation’.(16) Although linked to the public sector, from the perspective of the procurement conducted by the public sector, it is logical that the definition of this notion taking shape in the Directive be based, as we have pointed out, on the classic conception of the term, linked to industrial development, the economy, the markets and technology.(17)

In any case, the definition of innovation appearing in the Directive of 2014 fits in well with the classic idea of innovation that, as we have seen, is employed in the academic-scientific setting.

The second of the aspects appearing most clearly in Directive 2014/24, the firm intent to promote innovation procurement, lies in the provision of a new procurement procedure especially conceived for this end. In its basic aspects, it is regulated under the guise of ‘innovation partnership’, in Article 31, and the application thereof will be particularly appropriate when the aim is to promote the so-called Public Procurement of Innovative Solutions (PPI).

#### **4. What are we talking about when we talk about ‘Joint Public Procurement’?**

On the other side of the coin, joint, aggregated and collaborative public procurement strategies in a broad sense have been increasingly used in recent years. In fact, improving their practice and solving the different and non-trivial problems that their implementation reveals, are some of the main challenges for the public procurement regulation in the immediate future.

As graphically summarised in recital 59 of 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 (hereinafter, Directive 2014/24),

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(16) C. PAZ, E. LEBREDO and J. CARLOS, “La innovación social desde el ámbito público: Conceptos, experiencias y obstáculos”, *Gestión y Análisis de Políticas Públicas, Nueva Época*, No. 15, January-June 2016.

(17) H.D. KOHLER and S. BEGEGA, “Elementos para un concepto sociológico de innovación”, *EMPIRIA, Revista de Metodología de Ciencias Sociales*, No. 29, Spetember-December 2014, pp. 67-88; M. ALBORNOZ, “Indicadores de innovación: las dificultades de un concepto en evolución”, *Revista CTS*, No. 13, vol. 5, November 2009, pp. 9-25; E. CARRASCO, F. FUENTE and B. ROBLEDO, “Compendio de definiciones del concepto ‘innovación’ realizadas por autores relevantes: diseño híbrido actualizado del concepto”, *Dirección y Organización*, No. 36, October 2008, pp. 61-68.

there is a strong trend emerging across Union public procurement markets towards the aggregation of demand by public purchasers. The aim, to a large extent, is to obtain economies of scale, including lower prices and transaction costs. However, it does not stop there, but furthermore contributes to other important objectives. It may favour transparency and contribute to the much-demanded and necessary integrity of public procurement. It also could serve to stimulate greater professionalism in management of public procurement, identification of the best purchasing possibilities or the most suitable design of what is being purchased. It could also contribute to a higher participation and turnout in the procedures convened; and likewise encourage sustainability by promoting more and better environmental standards, as well as intensify the development and generation of innovative solutions that are essential nowadays.

Likewise, fostering joint procurements is part of the Europe 2020 Strategy key initiatives. It is believed that, in many ways, its objectives can be better attained if the public procurers join or coordinate their efforts. In this regard, current Directives emphasize the importance of joint public procurement as an instrument to contribute, as well, to the achievement of the European strategic goals and, therefore, have tried to improve the legal framework.

But the first to be clarified is “the toolkit available to contracting authorities willing to engage”<sup>(18)</sup> in centralised, joint, collaborative or coordinated procurement procedures. And at this point a conceptual clarification must be made, because current Directives do not completely polish up the definitions, and the literature on those ‘joint or cooperation strategies’ in the field of public procurement is still too scarce. There is no general and commonly accepted and closed list of the possibilities that should be included in the concept. Nor does a general and commonly accepted concept exist for identifying the different categories that could be included in the list.

Nonetheless, many institutional documents and academic articles often use the terms such as ‘collaborative procurement’, ‘cooperative purchasing’, ‘joint public procurement’, ‘coordinated procurement’, ‘aggregated purchase’, ‘pooled purchasing’, ‘alliance purchasing’, ‘bundled purchasing’, ‘collective purchasing’, ‘combined purchasing’, ‘mutual purchasing’, ‘shared purchasing’, etc. There is a large variety of terminology in use, and although it is possible to recognize some patterns in the usage and meaning of it, in general, the expressions are used without properly clarifying the scope of each of them.

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(18) A. SANCHEZ-GRAELLS, “Collaborative Cross-border Procurement in the EU: Future or Utopia?”, paper presented at the workshop on “Collaborative Efficiency in Government: The Trend, The Implications”, ECPR Joint Sessions, Scuola Superior Sant’Anna and University of Pisa, 24-28 April 2016.

Within the EU boundaries, we must cite the LEAP GPP Toolkit, elaborated by Local Authority Environmental Management and Procurement Project. This instrument contains a definition of ‘joint procurement’, and the description of different models and types. According to this, the three cumulative elements that have to be present in a joint procurement are:

- a) The combining procurement actions of two or more contracting authorities;
- b) The voluntary behaviour of the contracting authorities implied to contribute to the procurement process;
- c) Only one tender published on behalf of all participating authorities.

In particular, the ‘Toolkit D’ explains that ‘Joint procurement’ (JP) “means combining the procurement actions of two or more public authorities. The key defining characteristic is that there should be only one tender published on behalf of all participating authorities”.

However, as explained by Tunde Tatrai, this definition could lead to serious misunderstandings and the European Commission should not take it as a point of reference in the interpretation of joint procurement in Europe.<sup>(19)</sup> I agree with this author who defends the idea that there are different types of ‘joint public purchasing’ whose differences are mainly determined by trust, commitment, intensity of communication or willingness or facility to work together.

Thus, in the broad concept of ‘joint procurement’ we can find many varieties, among them, permanent joint procurement organisations, e.g., Centralised Purchasing Bodies who act on behalf of a number of different public authorities; singular contracts concluded by a contracting authority on behalf of a number of different public authorities; or many contracts launched by different contracting authorities but after having defined common elements, etc.<sup>(20)</sup>

This broad way of understanding the idea involved in the term ‘joint procurement’ is present in Directive 2014/24/EU, and clearly follows from its Recital 71, second paragraph, when it explains that: “Joint procurement can take many different forms, ranging from coordinated procurement through the preparation of common technical specifications for works, supplies or

(19) T. TATRAI, “Joint public procurement”, ERA Forum 2015, 10 March 2015, *ERA Forum*, 2015, 16:7–24, DOI 10.1007/s12027-015-0374-3, 10.

(20) G.M. RACCA and S. PONZIO, “Nuovi modelli organizzativi per il joint procurement e l’innovazione dei contratti pubblici in Europa”, in *Compra Pubblica Agregada* (R.F. ACEVEDO and P. VALCARCEL FERNANDEZ eds), [complete ref.] 2016, pp. 373-406; G.M. RACCA, “Joint Procurement Challenges in the Future Implementation of the New Directives”, in *Modernising Public Procurement: the New Directive* (F. LICHÈRE, R. CARANTA and S. TREUMER eds), Copenhagen, Djøf Publ., 2104, pp. 225-254.

services that will be procured by a number of contracting authorities, each conducting a separate procurement procedure, to situations where the contracting authorities concerned jointly conduct one procurement procedure either by acting together or by entrusting one contracting authority with the management of the procurement procedure on behalf of all contracting authorities”.

It is especially common when talking about joint or collaborative public purchases to highlight the advantages that they may entail.<sup>(21)</sup> The most typical advantages or benefits associated with purchases in which are involved multiple public bodies are: payment of lower prices; reducing transaction costs; administrative cost savings; reduced workload; achieving greater quality in final products and services; sharing new knowledge and risks; being part of critical mass; standardising public demands; promoting the creation of networks to share experiences and pooling expertise, etc. In sum, there are interesting achievements that can contribute to maximizing the efficiency of the buying power in the public sector.

Besides, the development of ‘joint public procurement strategies’ – we refer to the broad meaning – is thought to be one of the ways in which the pursuit of the economic and horizontal or secondary goals can be more easily attained. Furthermore, when the ‘joint public procurement strategy’ involved contracting authorities from different EU Member States, the EU moves forward to the real Internal Market integration – because participating public buyers have to think more openly than when they act with a ‘local’ perspective.<sup>(22)</sup>

But, at the other end of the scale, there exist important limitations, difficulties or disadvantages that must be taken into consideration when thinking about ‘joint public procurement strategies’, in particular, in cases of ‘joint cross-border public procurement strategies’. Characteristic disadvantages linked to ‘joint public procurement strategies’ are set-up costs; co-ordination costs; losing flexibility and control, for instance, less flexibility in the requirement to conform to the specifications and material terms of the base contract; supplier resistance, for instance from local, small or disadvantaged suppliers; or, even, antitrust issues.<sup>(23)</sup> Regarding in particular the experiences of Joint

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(21) G.M. RACCA and G.L. ALBANO, “Collaborative Public Procurement and Supply Chain in the EU experience”, in *Strategic Supply Management* (C. HARLAND, G. NASSIMBENI and E. SCHNELLER eds), London, Sage, 2013, pp. 179-213.

(22) A. SANCHEZ-GRAELLS, “Collaborative Cross-border Procurement in the EU: Future or Utopia”, *op. cit.*

(23) H. WALKER, M. ESSIG, F. SCHOTANUS and T. KIVISTO, “Co-operative Purchasing in the Public Sector”, in *Public Procurement. International Cases and Commentary* (C. HARLAND, J. TELGEN, K.V. THAI, G. CALLENDER and K. MCKEN eds), London, Routledge 2007, pp. 325-342.

Cross Border Public Procurement strategies, we cannot ignore the relevant legal and linguistic problems that could emerge.

Recital (73): “Joint awarding of public contracts by contracting authorities from different Member States currently encounters specific legal difficulties concerning conflicts of national laws. Despite the fact that Directive 2004/18/EC implicitly allowed for cross-border joint public procurement, contracting authorities are still facing considerable legal and practical difficulties in purchasing from central purchasing bodies in other Member States or jointly awarding public contracts. In order to allow contracting authorities to derive maximum benefit from the potential of the internal market in terms of economies of scale and risk-benefit sharing, not least for innovative projects involving a greater amount of risk than reasonably bearable by a single contracting authority, those difficulties should be remedied. Therefore, new rules on cross-border joint procurement should be established in order to facilitate cooperation between contracting authorities and enhancing the benefits of the internal market by creating cross-border business opportunities for suppliers and service providers [...]”.

It will depend on many factors, such as the joint or collaborative structure, which can amplify or minimize some advantages or disadvantages.

In any case, the choice of the concrete formula and the organizational structure will depend on different variables. It is not the purpose of this contribution to analyse the whole spectrum of possibilities and their regimes. On the contrary, the purpose of this study is much more modest. It simply consists in emphasizing the importance or the opportunity of intensifying the use of ‘Joint Cross-Border Public Procurement strategies’, in the different existing formulas, from the more to the less intense ones, in the field of the public purchase of innovation.

### ***5. Directive 2014/24/EU and the Increasing Opportunities for Joint Cross-Border Public Procurement?***

The importance of the public sector’s purchasing power capacity could be expanded through the establishment of cross-border purchasing networks for the implementation of coordinated strategies.(24) It can be achieved by

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(24) G.M. RACCA, “Atti del convegno Appalti pubblici: innovazione e razionalizzazione. Le strategie di aggregazione e cooperazione europea nelle nuove Direttive”, Rome, Consiglio di Stato, 14 May 2014. Among the most advanced and innovative joint procurement experiences, the Healthy Ageing Public Procurement of Innovations (HAPPI) project stands out for having combined product innovation (‘what to buy’) with an innovation of the procurement procedure. The partners in the HAPPI project decided to act together from the beginning in order to share the risks connected to the purchase of innovative solutions in the field of active ageing. This project has been one of the first concrete examples of cross-border joint

creating a broad cooperation at the EU level, among contracting authorities from different Member States, to buy together, to launch coordinated contracts, or to create networks to define benchmark and best practices, as means for establishing a significant intermediary and reference for private operators from the side of public demand. As we will attempt to explain this can be very relevant with regard to the purchase of innovative solutions.

In this regard, Directive 2014/24 has opened up new opportunities, not only for occasional collaborations to aggregate some types of procurements among national contracting authorities, but also for cooperation between contracting entities from several Member States that wish to carry out joint procurement.

Nevertheless, these techniques entail certain risks that need to be analysed in order to limit their use and to carefully consider when to resort to aggregation or coordination, or to design techniques to prevent such risks and minimise them. For example, an excessive concentration, either of demand or supply, may lead to collusive practices, restriction of competition, or may adversely affect access of SMEs to the market.

On the other hand, leaving aside the specific case of the creation of the so-called central purchasing bodies, it is clear that a basic element of joint procurement or aggregation of purchasers is the coordination of the different parties, to accept diverse formulae. Thus, coordination can be articulated either through consensus of the several contracting authorities, on common elements, such as procurement technical specifications that need to be included in every procurement procedure used by each contracting authority; or by jointly designing a single procurement procedure, managed by just the one contracting authority on behalf of the others.

The use of demand aggregation or the aggregation of purchasers internationally is interesting from several points of view. This study intends to highlight the important role it can play in boosting Public Procurement of Innovation; however, we need to first look at how the Directive 2014/24 provides for internationalisation of joint purchases.

From the point of view of our analysis, there are two precepts in the Directive that have a direct relationship with joint purchases that we need to look at. On the one hand, there is Article 38 (“Occasional joint procurement”) and on the other hand, Article 39 (“Procurement involving contracting authorities from different Member States”).

With regard to occasional joint purchasing, Article 38 emphasises the need for regulating the joint responsibility that arises from the implementation of

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public procurement to buy innovative solutions in the field of ageing well: *see* R. CAVALLO PERIN and G.M. RACCA, *European Joint Cross-border Procurement and Innovation*, Chapter 3.

certain specific procurements.<sup>(25)</sup> In particular, the precept expressly accepts two possibilities, namely that the procurement procedure is jointly carried out in its entirety or that only certain parts of the same are carried out jointly. As indicated, the Directive focuses on clarifying the scope of such joint responsibility of the participating contracting authorities for fulfilling their obligations pursuant to the Directive. The solution is clear, the said joint responsibility is directly related to participation in the procedure and therefore, if the procurement procedure is jointly carried out in its entirety, then all contracting authorities concerned shall be jointly responsible regardless of how the procedure is administered or managed. However, if the procurement procedure is jointly carried out in part, then the joint responsibility will affect only the parts that have been jointly implemented. It thus follows from the above that each contracting authority will be responsible for fulfilling its obligations for the procedures or parts it conducts in its own name and on its own behalf.

To illustrate the above, if several contracting authorities jointly prepare and award just the one procurement procedure, then they will be jointly responsible for any irregularity or contravention of the Directive committed during such procedure. On the other hand, if a procedure is jointly developed but each party later conducts its own part and some parties default on the provisions of the Directive while others do not, e.g.: some do not fulfil the required advertising principles for the procedure while the remaining parties do so, then only the parties violating the Directive, and not others, will be responsible for such default, regardless of whether they had collaborated in the definition of the basic terms of the procurement model followed. To conclude, whenever several contracting authorities act jointly, they respond jointly and whenever each party acts separately, they respond individually.

With regard to procurement involving contracting authorities from different Member States, Article 39(1) expressly states that the contracting authorities from different Member States may act jointly in the award of public contracts by using one of the methods provided for in the Article. As can be seen, the perspective that prevails is that of the contracting authorities or contracting entities, whose right to acquire products, works and/or services through contracting authorities from other European States is upheld.

The said entitlement is significantly buttressed through the ban imposed on Member States, and referred to in section 2 of the same article, according

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(25) S. PONZIO, "Joint Procurement and Innovation in the new EU Directive and in some EU-funded projects", *Ius Publicum Network Rev.*; G.M. RACCA and S. PONZIO, "Nuovi modelli organizzativi per il joint procurement e l'innovazione dei contratti pubblici in Europa", *op. cit.*; G.M. RACCA, "Joint Procurement Challenges in the Future Implementation of the New Directives", *op. cit.*

to which a Member State shall not prohibit its contracting authorities from using centralised purchasing activities offered by central purchasing bodies located in another Member State. But the fact that prohibition is not permitted does not imply that clarifications cannot be made. Therefore, national law can opt to specify that its contracting authorities can only resort to centralised purchasing activities carried out on a permanent basis for the procurement of supplies and/or services destined for contracting authorities, or for awarding public contracts or signing framework agreements for works, supplies or services intended for contracting authorities.

As stated in recital 73 of the Directive, this general authorisation is justified as a response to the specific legal difficulties that arise due to the lack of a minimum harmonisation among national laws. Once again the aim is to maximise the internal market potential in terms of economies of scale and risk-benefit sharing, especially for innovative projects that have a higher risk than that reasonably borne by a single contracting authority.

The authorisation is not unconditional. In fact, the Directive prohibits use of any methods (provided for cross-border joint procurement) to circumvent mandatory public law rules, which in conformity with Union law, are applicable to them in the Member State where they are located. As an example, we may cite the provisions on transparency and access to documents or specific requirements for traceability of sensitive supplies such as substances that are hazardous or harmful to health or the environment.

In regard to the methods used, the Directive mentions the following: (a) the joint award of a public contract; (b) the conclusion of framework agreements; (c) the administration of dynamic purchasing systems and (d) the award of contracts based on a framework agreement or on the dynamic purchasing system in accordance with the provisions of Article 33(2)(3) and (4) of the Directive.

Another outstanding novelty is the provision concerning the hypothesis that several contracting authorities from different Member States incorporate or establish a common legal entity (of the type, for example of, European Grouping for territorial cooperation) whose actions may include cross-border procurement.

In all these cases, the European legislator is essentially concerned about which Law governs each of these new forms of cross-border cooperation and the protection mechanisms that shelter the economic operators.<sup>(26)</sup>

The Directive provides different guidelines in this regard. Hence, in the case of implementation of centralised purchases by a central purchasing body the

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(26) G.M. RACCA and S. PONZIO, “Nuovi modelli organizzativi per il joint procurement e l’innovazione dei contratti pubblici in Europa”, *op. cit.*; G.M. RACCA, “Joint Procurement Challenges in the Future Implementation of the New Directives”, *op. cit.*

national provisions of the Member State where the central purchasing body has its registered office shall apply. The same solution is applied, among other cases, to the award of a contract through a dynamic purchasing system.

In any of the four methods for articulating cross-border joint purchasing listed above (joint award of a public contract; framework agreement; administration of dynamic purchasing systems; and the award of contracts based on a framework agreement or on a dynamic purchasing system), the Directive requires the participating contracting authorities to have an agreement in place that determines both the responsibilities of the parties and the relevant national applicable provisions, as well as internal organisation of the procurement procedure, in particular, concerning its management, the distribution of works, supplies or services to be purchased and the conclusion of contracts.

Kindly note the different solution envisaged for the provision of centralised purchasing by a central purchasing body – in which case the applicable legislation is always that of the Member State where such body is located. In the case where several contracting authorities from the different Member States purchase jointly, these States must conclude an agreement that defines, among other issues, the applicable national rules, which may be from any of the respective Member States. In the former case, the Directive imposes the solution while in the latter case it lets the parties decide.

Finally, when setting up a joint legal entity, the participating contracting authorities must choose between applying the national rules of the Member State in which the joint legal entity has its registered office or the national provisions of the Member State where the joint legal entity is carrying out its activities.

However, although the current legal picture is much better than the previous one, it is not enough. As emphasized in detail in a recent paper,<sup>(27)</sup> having a close look at the provisions included in the Directive, it is clear the legal framework is not sufficient and does not cover all the potential legal dimensions that can derive from the relationships emerging from Joint Cross Border Public Procurement.

Besides, it is usual when talking about joint cross border public procurement to emphasize only its advantages, but it should not be forgotten that the available data prove that the experiences about it are quite heterogeneous, and there exist unhappy experiences, as well.

I share this skeptical view. But difficulties must not become an insurmountable wall. And at least, with regard the buying of ‘innovation’ – so taking into account the specificity of the object of the purchase – it is especially relevant to the joining of efforts of contracting authorities from different Member States.

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(27) A. SANCHEZ-GRAELLS, “Collaborative Cross-border Procurement in the EU: Future or Utopia”, *op. cit.*

It should be one of the areas where joint cross border public procurement would have a greater application, and regarding legal difficulties there is a clear evidence that they are being overcome acceptably. So, in spite of barriers, public authorities have the power and the duty to promote innovation through cross-border joint public purchase as well. Not acting does not solve problems, but only favours uncompetitiveness in the long term.

For instance, in a scenario of cross-border procurement by using joint procurement without being involved central purchasing bodies, it is particularly interesting to assess the case of jointly *awarding* a public contract. Tendering a unique procedure could be considered the perfect situation in a joint cross border procurement scheme. But sometimes precisely because of some of the aforementioned difficulties – significantly the legal ones – contracting authorities from different Member States instead of giving up promoting one singular tender prefer to renounce it to prepare a unique tender under another formula with fewer demands for cooperation or coordination. As will be explained, there are examples of procurement innovation projects, where contracting authorities involved choose to promote “at the same time” separate procurement procedures with common elements and common organization. PAPIRUS Project is an example of what we can call ‘coordinated procurement’.

## ***6. Collaborative or Joint Cross-Border Public Procurement for Boosting Innovative Solutions***

### **6.1. Introduction: new strategic approach to innovation**

In any case, in spite of difficulties, one can appreciate the interest of the European Commission in encouraging the potential of ‘joint’ ‘cooperative’ ‘collaborative’ cross-border public procurement. There are different reasons why the European Commission paid attention to this perspective. On one hand, the Commission seeks to attain the economic goals of the Europe 2020 strategy, but also still hopes to further the single market integration. It is a fact that cross-border purchases help buyers to approach public procurement from a European perspective.

Alongside this, some of the benefits from joint cross border public procurement applied to innovation are: a) pooling resources and experiences; b) sharing risks that are typically associated with any innovation activity so that they are manageable for each party; and c) better identification of opportunities.

In brief, the European Commission underlines the desire of the EU to adopt a new strategic approach to innovation, and in this approach, collaboration of public purchasers lies at the heart of the strategy.

The aggregation of public purchasers with similar market profiles but located in geographically dispersed (local, regional, national or international) areas, may be particularly decisive when launching public procurement of innovation projects (PPI projects). One of the objectives sought to enhance procurement via joint purchase instruments is precisely that of stimulating innovation and internationalisation, in order to obtain technologically advanced and innovative products and services at better prices. Hence, joint international collaboration will significantly increase management efficiency of the public actors that have been recognised competencies in areas of great relevance to the citizens. The public sector must take advantage of synergies if it wants to extract maximum performance from the innovative potential of the private sector.

As stated by the European Commission in its Communication of 2010 on the Innovation Union, given the scale and urgency of the societal changes and the scarcity of resources, Europe can no longer afford the current fragmentation of effort and slow pace of change demanded by society. Therefore, efforts and expertise in the field of research and innovation must be pooled together because this contributes to the generation of a greater critical mass. Conditions that allow breakthroughs to rapidly find their way to the market must be created right from the beginning, so that such innovations can quickly provide benefits to citizens and increase competitiveness. The Commission has also identified the fields that particularly need large innovative developments and these are the ones where the greatest societal challenges lie: population ageing, climate change effects and the reduced availability of resources.

Moreover, if we focus just on stimulating innovation, one cannot overlook the fact that one of the great incentives for companies to increase their innovative efforts lies in the size of the market in which they will be able to sell their new products or services. The bigger the market, the more business opportunities will be considered, and the greater the interest for achieving satisfactory innovation. This is especially so for new products and/or services whose real demand is still unknown. Market uncertainty and the suspicion that it might be too small for marketing purposes are elements that adversely affect development of innovative products or services. Therefore, the creation of larger markets may be a relevant incentive for arousing the interest of economic operators to participate in projects to buy innovation. Simultaneously, from the point of view of the public sector, generating the said economies of scale, to lower prices payable by the contracting entities.

In this regard, the European Commission, after taking note of the positive experiences of several Member States that supported innovation in pre-commercial procurement through the Small Business Innovation Research

(SBIR) programme, has reached the conclusion that this type of approach could be applied more widely and furthermore be combined with joint procurement between different contracting entities, thereby creating several much larger markets, which would greatly boost innovation and new innovative enterprises, especially SMEs, which are the predominant business type in Europe.(28)

However, the potential benefits from the aggregation of purchasers applied to innovative purchases go even further. Other advantages provided by pooling resources and experiences derived from joint public procurement, especially at the international level (of most interest to the object of this study), lie a) in sharing risks that are typically associated with any innovation activity so that they are manageable for each party; and b) in better identification of opportunities. In this case, networking by entities interested in boosting PPI may help uncover potential opportunities for the aggregation of demand in the innovation sector.

It is highly desirable that contracting authorities interested in innovation policies assess the possibility of associating and coordinating with other entities in order to implement this type of project through aggregation of their demands.

The European Commission, in its aforementioned Communication of 2010, underlines the desire of the EU to adopt a new strategic approach to innovation. In this approach, the aggregation of public purchasers occupies a central location. In fact, the initiative presented by the Commission, which is framed within the scope of the Europe 2020 strategy, seeks to improve innovation conditions in all stages of development and is furthermore an initiative that is also expected to have a positive impact on employment, growth and social progress in the Union.

In order to help channel this type of joint procurement, the Commission undertook to provide guidance in accordance with the public procurement Directives and to examine the opportunity to introduce additional rules to facilitate achievement of a true cross-border scope. To that end, the new Directive 2014/24 (as mentioned in the earlier section), contains new rules for cross-border joint procurement that allow contracting authorities to take full advantage of the internal market potential.

So, if we agree on this approach, the next step consists of identifying some procedures, mechanisms, measures, patterns or guidelines to facilitate the launching of joint cross-border public procurement for buying innovation.

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(28) See C. SANTERRE-FUNDERBURG and C.R. YUKINS, The U.S. Small Business Innovation Research (SBIR) Program: *A Comparative Assessment*, Chapter 11 in this book.

## 6.2. Spurring institutional channels in order to achieve information, exchange experiences and provide support (economic, legal, etc.)

The European Commission has provided significant and increasing support for innovative procurement since 2009, which includes, joint cross-border innovation procurement.

The type of support can be divided into two broad categories:

- a) The direct economic support via Funds. EU Programmes and in particular the European Structural and Investment Funds and Horizon 2020 offer interesting funding opportunities to promote joint innovation public procurement – including both PPI and PCP –;
- b) Indirect support via measures such as:
  - The Procurement of Innovation Platform, an online platform composed of a website, a procurement Forum and a Resource Centre, that helps public authorities, procurers, policy makers, researchers and other stakeholders harness the power of Public Procurement of Innovation (PPI) and Pre-Commercial Procurement (PCP);
  - The Public Procurement of Innovation Award aims to recognise successful public procurement practices used to purchase innovative, more effective and efficient products or services.

The European Assistance For Innovation Procurement (EAFIP), supports public authorities in awarding more and better innovation procurements across the EU. This initiative focuses on promotion of the benefits of innovation procurement, as well as training and assistance to public procurers with a concrete interest in implementing innovation procurements. The initiative is focused on certain public sectors, such as construction, housing and community amenities; health and social protection; education, recreation, culture and religion; environment; public order, safety and defence; exploration, extraction, production, transport and distribution of energy such as electricity, gas, heat, oil, coal, other solid fuels; transport services such as railway, urban railway, tramway, trolleybus, bus services, airport and port related activities; water; etc.

In addition, there are very interesting channels to help public buyers get involved in these types of purchases. These channels help to generate useful ‘networks’ that contribute to the identification of common interests and possible partners, and to share the experiences of buyers, which can help to promote good practices and avoid the bad ones or common inconveniences.

### 6.3. Elements for success of the PPI, particularly within the framework of joint international procurement

The successful launch of innovative public procurement depends largely on following a set of stages or steps prior to starting the procurement procedure or items related to the same. Some of these steps are also relevant from the point of view of joint purchasing, which is why attention is later focused on them in this study. As examples of steps required prior to the start of the procurement procedure, we will be discussing preliminary market consultations, identification and planning of purchasing needs and provision of prior information to the market through the so-called early demand maps. And finally, in view of its special relevance, the support of multidisciplinary technical groups to the contracting entity will also be considered as an element of the procurement procedure.

#### 6.3.1. Technological and market surveillance, as instruments for identifying and effectively planning purchase needs

Whatever the objective of the joint purchase and especially in the case of innovative purchase, each of the participating public entities should program or schedule their own needs as an individual contracting body, *i.e.* it must clearly define beforehand, the products and services that will be procured jointly.

A good planning tool worth having is technological and market surveillance. Technological surveillance involves follow-up of progress made within a technological context and the new solutions generated. However, market surveillance involves monitoring and analysis of the various operators in a given market, such as competitors, suppliers and customers.

Without prejudice to each entity having to perform the aforementioned individual planning, the identification of opportunities can be considerably improved with greater connection and data pooling between the different public sector entities. This collaboration will lead to better planning of procurement. Hence, the promotion of such contacts between public authorities from different countries can be especially fruitful when each of them stays abreast with developments in their nearby markets and shares the news and benefits from these markets with other bodies that would not receive this information immediately. The implementation of joint international procurement can serve to encourage the creation of more or less stable networks to this end.

### 6.3.2. The preparation of ‘early demand maps’

After gathering all the information mentioned in the two previous stages (preliminary consultations and technological and market surveillance), the public sector will be in a better position to design and prepare the specific tendering procedures. In this regard, it should not be overlooked that the PPI framework also contains another key instrument called the ‘early demand map’ for this preparatory phase. These maps are intended to provide anticipated information on the needs of the public purchaser to the market, which will allow private economic operators to focus their R&D activity on such needs. Thus, the early demand maps present two essential characteristics. On the one hand, they require contracting entities to plan their purchases sufficiently in advance and, on the other hand, they allow companies to plan their investments by knowing the real business opportunities offered by the public sector. In short, the early demand map is an incentive to business investment and can stimulate economic growth and creation of employment. And in this case too, the aggregation of efforts can improve effectiveness and results.

### 6.3.3. Preliminary market consultations

As previously explained, public demand has an important role to play in stimulating innovation. In fact, its interaction with the supply-side can have crucial implications for innovation dynamics. Several studies have shown that some of the major tools to foster systemic innovation policy include the organisation of discourse between and among users, consumers, and others that are affected by innovations in order to articulate and communicate needs, preferences and real demand to the market.(29) Furthermore, the scale and characteristics of demand in a given location have been recognised as major determinants of the competitiveness of locations and their innovation dynamics.(30)

PPI requires technical expertise and an insight into the market that the public purchasers often do not have. Hence, one of the first needs of the public sector when it wants to undertake a PPI contract is that of contacting those who can provide such information, *i.e.*, operators in the respective market, specialised independent authorities or experts etc.

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(29) J. EDLER and L. GEORGHIOU, “Public procurement and innovation – Resurrecting the demand side”, *op. cit.*, 1, p. 950. See also J.M. GIMENO FELIU, Public Procurement as a Strategy for the Development of Innovation Policy, Chapter 9 in this book and A. MIÑO LÓPEZ, Preliminary Market Consultations in Innovative Procurement: A Principled Approach and Incentives for Anticompetitive Behaviors, Chapter 15 in this book.

(30) J. EDLER and L. GEORGHIOU, “Public procurement and innovation – Resurrecting the demand side”, *op. cit.*, 1, p. 950.

In the case of joint innovative procurement, this need increases significantly, since such aggregation of purchasers presumably involves markets in several countries that even today can have very different characteristics, even though we are talking about the same subject (for example, think of the telecommunications market, which is very different in Britain than in Greece).

These consultations, which have to be carried out prior to the formal start of procurement procedures, are normally articulated through a ‘technical dialogue’ referred to in Directive 2004/18/EC in its recital 8 according to which “before launching a procedure for the award of a contract, contracting authorities may, using a technical dialogue, seek or accept advice which may be used in the preparation of the specifications provided, however, that such advice does not have the effect of precluding competition”. Directive 2014/24 devotes its Article 40 to elaborate on this issue.

Public authorities aim to obtain a wide range of information through the contacts provided about the market capacities in which they carry out the contract; the state of the art, science or technology; or the type of solutions available in the specific sector. These discussions can also help to define the technical specifications in terms of performance or functional requirements of the contractual services, which then become the object of the contract; to determine the criteria that would be more suitable for awarding the contract to be announced; or to ensure that the economic operators get to know the fields that are of interest to the public sector for future procurements and their requirements.

Information obtained from the preliminary market consultations will be used to plan, design and develop the procurement procedure.

The wider the scope of the public sector call and the greater the participation, especially from the private innovative sector, the greater will be the interest and usefulness of the consultations.

The organisation of these consultations should not be very complex in joint international innovative procurement. The best operational approach would be to hold a prior consultation in each of the participant countries and that each consultation be managed by the public authority or contracting public authorities of the respective country. However, depending on the case and the market characteristics, it might perhaps be more appropriate to hold a single international consultation or several consultations in the one country.

Even though these consultations were previously possible, there was no regulation governing how they should be carried out. Given that reference to the market consultations are made in the articles of Directive 2014/24 and not just in one recital and that the aim is to boost and promote innovative

procurement, the transposed laws should at least provide certain applicable guidelines in this respect.<sup>(31)</sup>

In accordance with Article 41 of Directive 2014/24, all contacts made between the public and private sectors as a result of these consultations must be consistent with the principles of transparency and equal treatment and non-discrimination of the participants, so as not to distort competition in future tenders whenever economic operators that were also present in the technical dialogue participate.

It is demonstrated that when these queries are made the desired innovation is achieved more quickly.

In international projects, as will be discussed later, these consultations are usually carried out in the different countries involved, particularly with economic operators in the sector.

#### 6.3.4. The support of multidisciplinary technical groups

In order to ensure smooth running of innovative procurement, it is important to have a team of independent experts with multidisciplinary training and sufficient technical expertise in several areas, such as legal, technical, economic or project management. In this regard, it is recommended that the contracting authority have the support of a multidisciplinary technical group throughout the contracting procedure and even for drafting the procedure. The group's mission will be to advise the contracting entity or entities on the different technical-innovative issues connected with the subject matter of the contract.

These multidisciplinary technical groups are even more important in many cases of joint international public procurement because of the coordinated nature of the contracts. It is advisable that the group or committee be unique and common given the coordinated nature of the purchase. It should be composed of a balanced number of members appointed in accordance with the proposals made by each public entity involved in the call for tender or tenders. Hence, there will be one or more tenders depending on whether the various entities convene a single procurement procedure or each one carries out its own procedure, albeit coordinated with the rest, for technical-innovative aspects. Obviously, if it is a case of a central purchasing body located in a Member State other than that of the contracting authority, then the applicable provisions will be the national provisions of that Member State (Article 39[3] of Directive 2014/24). If, as in Spain, there are no regulations envisaged in this regard, then in such a case, parties should reach a consensus on the establishment of

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(31) See also O.P. VODA and C. JOBSE, "Rules and Boundaries Surrounding Market Consultations in Innovation Procurement: Understanding and Addressing the Legal Risks", *EPPPL*, 2016, p. 179.

a multidisciplinary technical support group for the various purchases to be carried out.

If the mentioned multidisciplinary technical group is established, then the entities involved in the procurement shall decide on the specific functions to be assigned to this group, as well as the governing guidelines or rules of operation, for example, the working language, the exact number of members, the procedure for carrying out the meetings, the meeting venue or venues etc.

### ***7. Innovative SMEs: The Need to Accommodate Them in Joint Cross-Border Public Procurement Procedures***

This paper has so far highlighted the benefits of joint purchases or aggregation of purchasers for boosting innovative public procurement. However, these techniques can also pose some relevant risks that need to be taken into account in order to take the necessary measures to minimise them. It would be appropriate to focus now on one such risk, namely: the possible exclusion of innovative SMEs from these contractual procedures.

Directive 2014/24 contemplates these problems and first admits the strong aggregation trend of demand shown by public purchasers from various States in view of the advantages discussed above. It then advocates the need for careful monitoring of their implementation “in order to avoid excessive concentration of purchasing power and collusion, and to preserve transparency and competition, as well as market access opportunities for SMEs”. This concern is clearly in line with one of the main reiterated aims of the Directive, namely; to facilitate and promote participation of SMEs in public procurement, in line with the Commission’s Communication “Small Businesses Act for Europe”, and the Directive even proposes adaptation of public procurement to the needs of SMEs.

Paradoxically, despite their smaller size in relation to other companies or thanks precisely to the same, SMEs manifest a spirit and entrepreneurial dynamism that highlight their capacity to adapt to the economic environment. Their great potential for technology and knowledge innovation in turn is a decisive contribution to economic growth and social sustainability. In Spain, as well as in other countries, the innovative technological offer linked to ICTs in many fields is led by innovative SMEs that confer a high added value to our business fabric. Their high degree of flexibility and speed when adapting to changes demanded by the market from time to time, play a major role in innovation and adaptation of new technologies.

In Europe, SMEs and the self-employed stand out within the business community for their quantitative and qualitative importance. Studies show that it is precisely these companies and entrepreneurs that are main drivers of the economy given their capacity to generate employment and potential for creating value.

In order to respond to and alleviate as far as possible the risks referred to in the specific case of instruments for aggregation of purchasers, one of the measures that should be encouraged is the aforementioned interrelationship between the different business sector operators, especially the relationship between innovative SMEs and larger firms. On the other hand, the creation of networks between innovative SMEs may encourage cross-border cooperation through which a greater effectiveness and scope can be achieved in the development and improvement of instruments to support innovation.

## 8. Analysis of Cases

Below are two cases that we found particularly interesting in response to the various aspects covered hereinabove. We are also aware of other interesting scenarios like the project HAPPI “Healthy Ageing – Public Procurement of Innovations”, or the project epSOS – “European Patients Smart Open Services”, but in order to avoid unnecessary repetitions, we felt it was appropriate to focus attention on just two of them, and therefore we have chosen one example from each of the two modalities, *i.e.*, one example of pre-commercial public procurement and another on public procurement of innovative technology.

### 8.1. The DECIPHER Project

The DECIPHER project (Distributed European Community Individual Patient Healthcare Electronic Record, *i.e.*, shared clinical records of patients in the European Union), was an innovative public procurement project, in the pre-commercial modality, that was promoted and co-funded by the EU and included within the European Commission’s seventh framework programme (FP7). It had a budget of €900,000. The project started in February 2013 and ended in March 2017.

The project aimed to develop a mobile application that allows citizens to securely access their health data when they move to other countries. The application should be flexible and compatible with the different infrastructures, standards and interfaces that each health system uses, as well as fully comply with the laws and regulations that guarantee security and privacy of data access. The project started in February 2013 and had a term of three years.

Several countries, namely: Spain, Italy, United Kingdom and Finland, were participating in the project. Spain participated through the Department of Health of the Catalonian Government, via the TicSalut Foundation, which acted as the tendering organisation, and the Catalonian Quality and Health Assessment Agency (AQuAS), which coordinated the pre-commercial public procurement process and performed project evaluation.

This pre-commercial public procurement (PCP) was structured into different phases as shown in the following description:

The first phase, called Phase 0 (or exploratory phase), was based on an open tender process in which any company could participate. After concluding the Phase 0 tender process, the proposals received were evaluated and the best nine proposals were shortlisted to participate in Phase 1. Companies or consortia which progressed to this new phase (Phase 1) would receive a maximum of €25,000 each to develop a design proposal for the solution in three months. After completing Phase 1, all proposals from participants were re-evaluated and the six best designs were selected to participate in the next phase (Phase 2). The solution proposals that survived this phase received a maximum funding of €52,500 each to develop a prototype in a maximum period of 6 months.

Prototypes were evaluated again at the end of Phase 2 to select the three that best answered the needs identified by the health system to participate in the following phase (Phase 3), where each participant received €120,000 to test the prototypes developed during a period of 9 months. Projects would then enter in the last phase (Phase 4) which corresponded to marketing of the product or service.

In total sixteen bids were submitted by 22 organizations from seven countries. Nine bidders were awarded and entered Phase 1 of DECIPHER PCP. Six bidders prepared their prototypes in Phase 2. Three bidders entered Phase 3.

An international consortium of entities from all participating countries (Spain, Finland, Italy and the United Kingdom) was created to implement this project. In particular, the consortium was comprised of four public sector healthcare authorities (Catalonian Quality and Health Assessment Agency/Spain, ESTAV Center/Italy, TicSalut/Spain and CMFT-TRUSTECH/United Kingdom; the latter three were the authorities that were buyers of PCP DECIPHER) and of three other additional organisations (ANCI Innovazione/Italy, Barcelona Digital Center Tecnològic/Spain and VTT Technical Research Center of Finland). These additional organisations contributed to the DECIPHER project by providing support to technically define the subject of this PCP, as well as by evaluating tender bids and the development of solutions.

However, as has been indicated earlier, project coordination and evaluation of the technologies developed, as well as the overall innovation process, was

managed by the Catalonian Agency AQUAS, on behalf of all the contracting entities that participate in the project. It was the sole ‘Contracting Entity’ that represented the consortium and it acted with the support of a ‘Procurement Committee’, chaired by the Director of AQUAS. This Committee in turn was supported by an ‘Expert Committee’ comprised of:

- a) External experts appointed by the ‘Contracting Entity’ drawn from among patients, health professionals, experts in e-health and/or mobile solutions and investment experts related to these matters;
- b) Experts appointed by the procurement entities of PCP DECIPHER;
- c) Technical experts appointed by the “Contracting Entity” at the behest of the PCP DECIPHER consortium. These in turn are members of one of the PCP DECIPHER consortium partners. Procuring entities are excluded from the expert committee.

This project was considered to be a big step forward for the configuration and organisation of international joint public procurement models and processes. This was the first time ever that several European public health administrations have formed a consortium in conjunction with technology suppliers, to define the technological solutions required to address the needs of health systems.

In order to stimulate participation of SMEs, the tendering specifications included some measures that can be viewed as favourable for such promotion. In particular, the participation of entities similar to the temporary joint ventures (termed Grouping of Tenderers) was envisaged. This is so because “any natural or legal person (including duly registered non-profit entities such as, for example, universities), can participate, either individually or as a group or association that encompasses several tenderers that is temporarily created precisely to participate in PCP DECIPHER and to assume responsibility for the implementation of the contracts awarded within the framework”.

Moreover, a high amount of subcontracting was permitted in each phase of the procedure, *i.e.*, up to a total of 49% of the services to be executed.

Prior to implementation, a ‘Market Consultation Day, DECIPHER Pre-Commercial Procurement process’ was organised. This contributed to raising awareness about the contractual process and was attended by some sixty company representatives from different countries. Attendance at the event was free and companies specialised in healthcare technologies and R&D centres were invited to participate. The objective was to inform companies present about the scope of the project, the pre-commercial public procurement process that was being developed, and the needs and requirements of the IT application that had to be developed.

Another issue of great interest that the DECIPHER project highlights is the one related to the applicable law and competent jurisdiction for resolving any conflicts that could arise.

With regard to the applicable law, the bidding specifications expressly stated that the entire procedure of PCP DECIPHER would be governed by Spanish law. Moreover, since this was a pre-commercial public procurement that meets the requirements of EU Law (namely, that the award is directed towards R&D services paid in full by the contracting authority and that risks and benefits are shared between the public purchaser and the winning companies, and furthermore, that the innovative solutions are far better than those available in the market), the contract was outside the scope of the European Directives, as well as of the Spanish TRLCSP (Consolidated text of the Public Sector Contracts Act); that is to say, it was an excluded contract. However, as the specifications indicated, in accordance with the provisions of Article 4(1)(r) of the TRLCSP, the principles of publicity, competition, transparency, confidentiality, equality and non-discrimination, and that of the most advantageous economic proposal, were guaranteed throughout the procedure. They also clarify that the competitive procedure (particularly, although not exclusively, the decisions on exclusion of tenderers and the award of the framework agreements and contracts) would be subject to Spanish Administrative Law, and of special relevance in this case is the Common Administrative Procedure Act. However, any decisions, issues and/or discrepancies concerning the performance of the contracts, once awarded, would be subject to the general Spanish Civil Law, with special relevance in this regard to the Spanish Civil Code.

As can be seen, the DECIPHER specifications applied the doctrine of severable acts under which contract preparation and award were governed by Administrative Law, while contract effects, compliance and extinction were subject to Private Law.

In regard to the competent jurisdiction for resolving any conflicts that could arise, the DECIPHER specifications began by asserting the exclusive jurisdiction of the Spanish courts, which was construed as accepted upon mere submission of the proposals by the candidates.

Consistent with the applicable law, the specifications further clarified that the selection of contractors was the competence of the Administrative jurisdiction, in particular, the Administrative Chamber of the High Court of Catalonia, with prior appeal for review before the Regional Minister of Health of the Government of Catalonia.

In contrast, any dispute or claim related to the implementation of the Framework Agreement or with the contracts concluded between the Contracting

Entity' and the contractor would fall under civil jurisdiction, in particular, with the civil courts (courts of first instance of Barcelona).

One of the problems presented by the exclusion of the PCP contracts from the TRLCSP, along the terms expressed in its Article 4(1)(r), concerned the jurisdiction that must be considered competent to deal with any arising conflicts. In this regard, a solution other than that stated in the DECIPHER specifications and which we feel is more in line with the public nature of the activity being carried out, was based on the understanding that the PCP contracts concluded by public entities, when fulfilling some of their public specific competence functions, are special administrative contracts, and hence are within the competence of the administrative jurisdiction, even during the implementation phase.

## 8.2. The PAPIRUS Project

The other project to which we want to pay attention is the so-called PAPIRUS Project (Public Administration Procurement Innovation to Reach Ultimate Sustainability/Innovation in Hiring Public Administration to Achieve Maximum Sustainability). It was a project co-financed by the European Commission whose duration was from October 2013 to October 2016.

The development of this project sought to introduce innovative solutions in the construction sector. Specifically, its objective was to promote the use of new materials and possibilities capable of generating Zero Energy consumption, both in new buildings and in rehabilitated buildings. That is, the goal was to achieve environmentally sustainable construction.

The EU's concern for this area is understood if we realize that urban buildings are responsible for 40% of energy consumption in Europe. This consumption accounts for about a third of the carbon dioxide emissions in the continent. In view of these figures, it has seemed appropriate to promote public action aimed at improving them so as to reduce significantly the emissions of greenhouse gases in the coming years, both in new buildings but also in the rehabilitation of buildings. The European objective is to achieve a reduction of emissions between 80% and 95% by 2050. In pursuing this goal, the involvement of public administrations will have a clear role.

In this project there were four countries involved, Spain, Italy, Norway and Germany. The contracting parties were: in Spain, Sestao Berri 2010 S.A. (Urban regeneration agency of Sestao); in Italy, ATC Torino (Territorial Agency for housing in the province of Turin); in Norway, Oslo Kommune (City of Oslo); and in Germany, the Landratsamt Enzkreis (Municipality of Enzkreis). Each of the participating parties chose one or several buildings to be built or rehabilitated using the new innovative technologies provided by contractors for the

different fields of construction required. The type of buildings to which the innovations were applied were very different. Spain promoted the *construction* of two buildings included in the social housing system. In Italy these technologies were applied to the *rehabilitation* of a social housing building. Norway *built* a nursing home. Finally, Germany undertook the *rehabilitation* of an educational building.

Due to legal difficulties it was decided to launch four procurement procedures. PAPIRUS is an example of 'coordinated public procurement' in four pilot sites in four European countries (Spain, Germany, Norway and Italy). So it was not a model of joint procurement in the narrow sense of the expression.

Each of the contracting authorities promoted its own contract, with its documentation, publication, award, etc. Each tender procedure was performed in the respective national language and in English. The PAPIRUS partners launched at the same time four open procedures in the four countries involved. The tender documents of each procedure were adapted to the particularities of each procuring entity's national legislation as well as the technical requirements of each case study.

Notwithstanding these separate efforts, relevant aspects were established on a consensual basis and were, therefore, common to the four contracts. Thus, the identification of the issues in which innovations were looked for; the definition of functional specifications that should be satisfied through the awarded companies; the award criteria of the contracts; or the moment in which the contract procedures were launched (it was desired these launches be as close as possible), etc. For instance, the award criteria were prepared by a 'Joint Cross-Border Evaluation Team' (JCBET), composed of members from the four pilots and the project coordinator Tecnalía. The JCBET also had an important role in the evaluation of the bids. The composition of the JCBET was aligned with the national regulations of each contracting entity.

As far as the thematic fields were concerned, the five that were chosen were related to the following functionalities: the reduction of energy losses through the opaque envelope of buildings (for example, super-insulation); the reduction of energy losses in winter and solar gains through the window in summer (e.g.: smart window); the development of technologies that provide good quality natural lighting (e.g. technologies for the use of natural lighting); the proposal of thermal energy storage solutions that increase thermal comfort and change the maximum heating and cooling loads (e.g., materials and solutions for storage of thermal energy); and, finally, the development of lightweight prefabricated panels with low CO<sub>2</sub> emissions (for example, the industrialized internal partition with minimal thickness, high thermal and acoustic insulation and low carbon footprint).

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As regards the buildings to which these innovations will be applied, they were very different in each country. Spain promoted the construction of two buildings of official protection; in Italy these technologies were applied to the rehabilitation of a social housing building; Norway built a nursing home; and Germany rehabilitated an educational building.

In spite of the fact that, as mentioned above, each of the entities convened its own contract, in this case an international consortium was also created. It was integrated by seven members from five different countries: TecNALIA Research Innovation Foundation (Spain) as technical expert and, in addition, as general coordinating entity of the project; Oslo Kommune (Norway), Landratsamt Enzkreis (Germany), ATC Torino (Italy), Getica Srl (Italy) and Sestao Berri 2010, S.A. (Spain), who acted as public buyers; and ASM Centrum badan i analiz rynku sp. ZOO. (Poland), which is an expert in outreach.

In addition to the various meetings and contacts between the parties involved in the project, a number of preliminary market consultations took place, one in Brussels and others in the four countries involved. More than 200 representatives of interested companies attended these meetings. In those events the companies gained an understanding of the characteristics of the project; the needs that were sought to be satisfied; expressed their concerns (for example, the difficulties of SMEs to participate in these contracts); or even promoted ideas on evaluation criteria to be considered in subsequent tenders, etc.

As regards the law applicable to contracts, unlike the previous case, in this case four different contracts were launched – although with some important common characteristics as mentioned above – for instance the applicable law was in each case the one of the country where the contract was launched. Therefore, four different sets of laws were applied: Spanish, Italian, Norwegian and German.

As regards the promotion of SME participation, the four contracts launched permitted different companies, associated or temporarily consorted, to submit a joint offer. Likewise, vendors also were allowed a considerable margin to subcontract parts of the works and services, although in this case, the specific percentage was established by each contracting entity, so it was not the same in all contracts.

As mentioned before, there were five thematic areas addressed by this project. This resulted in the identification of five different lots. Each of the contracting authorities decided the lot or lots that would be included in the particular contract that would launch. This decision was made depending on the available funds and on the specific characteristics of the constructions to which the innovations would be applied. For example, in the case of Spain, the contract included only two lots: a) Solutions to reduce energy losses through

buildings opaque envelopes; b) Solutions to reduce energy losses in winter and solar gains through window in summer.

The type of the contract was diverse from one country to another. Thus, each contracting authority configured its contract depending on the scope of the activity to be assumed by the awarded bidder. In Spain, it was conceived as a service contract that had as its object the purchase of products and the operations of installations of such products. In Germany, it was seen as a public works contract that also had as its object the acquisition of products and their installation. In Italy, it was treated as a public supply contract excluding the installation and placement of materials. Finally, in Norway it was conceived as a public supply contract which aimed at the purchase of products and operations for its installation.

A very low number of offers were submitted in all four countries, but not for all lots. This contrasts with the huge interest and participation in the five market events beforehand. Once bidder groups formed, no actual international participation was detected. There were presented: Torino: 3 offers; Oslo: 4; Germany: 10; Spain: 6. But twelve offers had to be excluded. As a result of the sparse offers Torino and Oslo launched new tenders for some lots.

All but one contract awarded after the PAPIRUS coordinated tender have been executed smoothly and reliably. One of the companies awarded by Sestao Berri (Spain) had a financial problem, so they proposed the cession of the contract to another company that could fabricate, supply and install the same product.

The project coordinator of the PAPIRUS Project, Tecnalía, prepared a very useful document explaining the main characteristics of the project. It also included a section about “lessons learned” where it is explained that PAPIRUS partners faced and overcame quite a lot of obstacles and barriers during the innovative procurement process.

In the pre-tender stage the main difficulties lay in finding a common ground for the coordinated tender in four different countries. Besides, the preparation of common tender documents was very challenging because of the differences in national law and in practice regarding public procurement among the four participating countries. Even if there is EU legislation (Directives), national legislation was found to be a barrier to joint procurement.

The preparation of the coordinated tender was the most time-consuming and challenging phase of this project. The PAPIRUS consortium not only established convincing tender documents and manageable means of awarding the offers, but also created a climate that aimed to facilitate cross-border procurements and the participation of SME and bidder’s consortia. Still, despite all the

efforts the participation in the tender was disappointing, and many bids had to be excluded.

The consortium drew some conclusions from the low number of bids:

- a) The tender documents were too demanding, the requirements were not sufficiently clear and included too many criteria, particularly award criteria; the bidders were discouraged and not ready for this kind of justification package they had to provide;
- b) Ensure that all important actors are involved from an early stage, such as end-users, technical and legal experts, policy makers, officials;
- c) Too many award criteria and requirements disrupt the focus of genuinely important objectives and the functionality required;
- d) PPI requires subjective award criteria; mathematical formula limit the freedom to propose different innovative solutions.

Future implementation of PPI by the different partners: Encouraged and motivated by the results and lessons learned of the PAPIRUS project, the four partners who are public procurers will definitely use PPI for further suitable procurements in the future – not only in the construction sector.

## 9. Conclusions

The main idea that must be highlighted from this chapter is that joint or collaborative public purchases – in the broad meaning we have explained – may entail relevant advantages that can contribute to maximize the efficiency of the public buying power to gain better and more powerful innovation.

The limitations, difficulties or disadvantages, obviously, must be taken into consideration when launching joint cross-border public procurement projects. However, taking into account the specificity of the object of the purchase – innovation, to stimulate maximum expected results – the joining of efforts of contracting authorities from different Member States can be especially useful.

There already are quite interesting experiences in launching different types of joint cross-border procurement for buying innovation, from which many useful lessons can be drawn. Particularly interesting are the experiences analyzed in the study promoted by the European Commission: “Support of the internal market policy for growth: Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States” (2017).<sup>(32)</sup> This study includes recommendations for the implementation of joint cross-border procurement procedures based on the results of case studies. It offers a practical approach on

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(32) doi:10.2873/10021

how to carry out joint cross border procurement procedures, how to foster legal certainty and how to allow for effective contract management and monitoring. The recommendations take into consideration the different models of joint cross-border procurement described in Directive 2014/24/EU, and are structured based on the chronological order applied to a tender procedure starting from the planning of a tender to contract management.

In brief, improving the preparation of these projects, learning from the experience and, in particular, solving the legal problems for their implementation, are some of the main challenges vis-à-vis the regulation for launching joint cross-border procurement in the immediate future.

There is no perfect model of collaborative purchasing, and buyers should identify and choose the coordination or collaboration strategies that best suits to each case, but according to the experiences carried out up to the moment, there is evidence that joint cross-border procurement can be a very effective tool to boost better innovative solutions.

The benefits associated with innovation make it a worthwhile gamble to intensify the startup of joint cross-border procurement projects in this particular field.



## **PART II**

# **Smart Cities and Procurement**

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## CHAPTER 5

### Smartness and the Cities

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#### *1. Smartness and the city*

From a strictly ideological viewpoint, the concept of ‘smart’ city has evolved from the notion of intelligent city, which much scholarship, mainly Anglo-American, has noticed approximately since 2008.<sup>(1)</sup> However, the notion of smart city is qualitative, so its borders are hard to define. The qualification of smartness is not sufficiently clear to allow a measurement of the starting points and pace of the transition. The starting point data were represented by the application of information and communication technologies to the urban structure. The first approach, using the rate of adoption of technologies, gave birth to graded tables of a prevailing sociological nature.

In the second phase, which is still ongoing, new evaluation factors have been included. These factors are much more complex and often impalpable. Some criteria refer to the capacity of artificial intelligence to penetrate and root in contexts such as social structure, environment, culture; to attract business and draw energies; to affect the governance and to facilitate the existing democratic processes or opening new ones; and to permeate the urban and social environment, making it evolve towards a ‘cyber-civics’ model. Such parameters tend to yield results in terms of competitiveness, efficiency, environmental sustainability, lifestyle quality, and prosperity. Many of these outputs are hard to measure. Furthermore, the causal relationship with the possible conditioning factor is almost impossible to demonstrate; however, many international classifications apparently refer to the rate of transformation of local democracy and the quality of living.<sup>(2)</sup>

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(1) See e.g. R. HOLLANDS, “Will the real smart city stand up?”, *City*, 2008, pp. 302-320; M. DEAKIN, “From intelligent to smart cities”, in *Smart Cities, Governance, Modelling and Analysing the Transition* (M. DEAKIN ed.), London/New York, Routledge, 2014, pp. 1 and ff.

(2) Such as the Human Development Index (Hdi) created by the United Nations, which takes into account, besides the gross product, life expectations, school attendance, adult alphabetization; the Better Life Index (Bli) by the Organisation for Economic Co-operation and Development, active since

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Among other things, the scarce public law scholarship that has followed the development of this phenomenon has noticed that the legal rules have remained substantially the same in all contexts all over the world. In the United States, for instance, the traditional Dillon's rule, which governs the principle of American localism,(3) has not been modified. States have also refrained from intervening with new legislation.(4) The most important changes in regulation have been introduced at the local level, from measures to reduce car traffic and air pollution through access regulation and fiscal measures as well as town and country planning.

The European legal system, in the absence of any reference to the city dimension in the Treaties, began to approach the local entities in terms of soft law. The very first mention of urban problems is usually traced back to a communication of 1997.(5) Since then a series of intergovernmental agreements were adopted in ministerial meetings, from Lille(6) to Rotterdam,(7) from Bristol(8) to Leipzig,(9) from Marseille(10) to Toledo.(11) The real turning point has been the Communication of 2009, at least with regard to the technologies aiming at energy saving.(12)

In 2010, Strategy Europe 2020(13) carved out seven development objectives and seven pilot initiatives. One of the last ones, The European Digital Agenda, emphasizes the idea of the smart city as a short-hand summary of

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2011, is founded on twelve parameters; other elaborations of private sources are the Cities in Motion Index, started by the University of Navarra in 2014, and the City Index Master Indicators Survey, operated since 2011 by the Council Advisor Boyd Cohen, kind of consortium of big private operators.

(3) See e.g. R. BRIFFAULT, "Our Localism: Part II – Localism and Legal Theory", *Col. L. Rev.*, 1990, p. 346.

(4) G.E. FRUG, *City Bound. How States Stifle Urban Innovation*, Ithaca/London, Cornell UP, 2008, ch. 1.

(5) EC Comm., "Towards an urban agenda in the European Union", Com (97)197. See e.g. E. CARLONI and M. VAQUERO PINEIRO, "Le città intelligenti e l'Europa. Tendenze di fondo e nuove strategie di sviluppo urbano", *Ist. Fed.*, No. 4/2015, pp. 879 and ff.

(6) 3 November 2000, "Lille Action Programme".

(7) 29 November 2004, "Ministerial Meeting on Territorial Cohesion".

(8) 6-7 December 2005, "Bristol Ministerial Informal Meeting on Sustainable Communities in Europe".

(9) 24-25 May 2007, "Leipzig Charter on Sustainable European Cities".

(10) 25 November 2008, "Final statement by the ministers in charge of urban development".

(11) 22 June 2010, dedicated in particular to urban regeneration and urban, smart and sustainable development.

(12) EC Comm. to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, "Investing in the Development of Low Carbon Technologies (SET-Plan)", COM(2009) 519/4. See also, earlier, EC Comm. to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, "Towards a thematic strategy on the urban environment", COM (2004)60, February 2004; and "Thematic Strategy on the Urban Environment and the Decision", No. 1411/2001/EC of the European Parliament and of the Council of 27 June 2001 on a Community Framework for cooperation to promote sustainable urban development, COM/2005/0718.

(13) EU Comm., "Europe 2020: A strategy for smart, sustainable and inclusive growth", COM (2010) 2020 final, March 2010.

technological progress, rational use of resources, networks and participated governance. On this side too, although with some delay, the concept completes its evolution from the Intelligent Transport Systems (ITSs) as a starting point. Such a move presupposes to achieve results in terms of the quality of urban life compatible with sustainable development and intergenerational preservation of natural resources.

In recent years, the EU soft legal sources mention the UN data on living in metropolitan areas more and more frequently. More than half of the world's population lives in urban centers, consumes more than 75% of the energy total and is responsible for about 80% of world emissions, although it occupies less than 2% of the territory.<sup>(14)</sup> In 2040, 75% of the world population will live in urban centers and will devour more than 90% of the energy total, notwithstanding the efforts towards the reduction of energy consumption.

The 2011 policy paper "Cities of tomorrow"<sup>(15)</sup> focuses on the convergence of various communitarian policies on urban topics. It concludes that a city aiming at energy self-sufficiency through local or regional plans should both reduce congestion and provide more leisure time, to be invested in participation. To achieve this, cities need a prevalence of renewables, supported by smart grids; zero-distance consumers guaranteed by online purchases; and low-consuming urban transports.

In 2012<sup>(16)</sup> the Commission began to release some resources to support roughly twenty integrated projects, where ICTs, energy and transports are coordinated to make the cities an engine for development and an agent of diffusion of models in the European market. For the first time, the Commission seems to openly prefer a cooperation between productive sectors, society and political representation. It also requests simplification of the regulatory instruments and elaborates some energy and environment indicators.

In 2014,<sup>(17)</sup> the "Urban Dimension of EU Policies" was initiated. These policies request private individuals, public authorities and their associations to provide ideas and stimuluses for the creation of an Urban Agenda. The results were presented on the occasion of the second European Cities Forum, held in Brussels on June 2, 2015.<sup>(18)</sup> All urban initiatives were consolidated in the

(14) Which will increase to 5% in 2025. The number of residents in urban areas, that has already reached 3.5 billion will grow up to 6.5 in 2050: forecast by United Nations, Department of Economic and Social Affairs, Population Division, "World Urbanization Prospects: The 2011 Revision", New York, 2012.

(15) EU Comm., "Cities of tomorrow – Challenges, vision, ways forward", 2011.

(16) EU Comm., "Smart cities and communities – European innovation partnership", C (2012) 4701, July 2012.

(17) EU Comm., "The urban dimension of EU policies – Key features of an EU urban agenda", COM (2014) 490 final, July 2014.

(18) Commission Staff Working Document, "Results of the Public Consultation on the Key Features of an EU Urban Agenda", July 2014.

cohesion policies, and new operational instruments have appeared, the most important of which seem to be the partnerships for the innovation of towns and local communities, the urban innovation actions, and the European Climate Adaptation Platform (Climate-ADAPT).

The 2014-2020 phase of the Horizon 2020 Program(19) recently added a third pillar dedicated to the application of technologies to social environment. Seven sub-programs combine the promotion of alimentary safety and sustainable agriculture, safe, clean and efficient energy, intelligent and low-consume transports, welfare and health, protection of climate and natural resources, freedom and safety, and inclusive capacity. In terms of the request for proposals and intellectual engagements, the passage from technological progress through innovation in the interest of the market is completed. The program has helped to ripen political objectives, for example, conducive to the quality of life in local communities. This effort reproduces the evolution of the European institutions from the economic to the political dimension, through the looking-glass of the city in the smart dimension.

The European Union offers resources through the Structural Funds, whose aims and intervention techniques are predefined.(20) In all the programs and sub-programs included in the Funds, the urban environment is considered the main beneficiary of the expected improvement in the use of resources, the reduction of emissions, research and development, infrastructures, and socio-cultural and general public interest services. Urban sustainable development, therefore, has progressively become a kind of cross-sectional mission, and the notion of a smart city is its emblem.

## 2. *Smartness: Some implications*

Smartness has many implications, involving different aspects of human activities concerning community life. The first and perhaps most important dimension is the one of town and country planning and building techniques. The methods applied in such an area must adhere to the social instances that have come to fruition together with the awareness of the limits to growth. The perception of the narrowness of resources and the impossibility of a continuous untroubled growth dates back half a century,(21) but this notion has acquired broader currency and consistency after the recent financial crisis. The new

(19) See e.g. S. ARGENTATI and N. CUSUMANO, "Horizon 2020: The EU Framework Programme for Research and Innovation", in *Finanziamenti comunitari 2014-2020. Strategia, gestione e rendicontazione* (V. VECCHI *et al.* eds), Milan, EGEA, 2015, pp. 43-59.

(20) On this theme, see e.g., M. CAPPELLO, "Guida ai fondi strutturali europei 2014-2020", Santarcangelo di Romagna, Maggioli 2015.

(21) See e.g. D. MEADOWS *et al.*, *Limits to Growth: the 30 year-update*, London, Routledge, 2005.

sensibility resembles similar approaches in former epochs, because each model of a town, its structure and relationship with the countryside, have always been at the heart of a culture and its time.

The era of the unlimited expansion of building, of the occupation of available ground, and of the consumption of a geologically fragile and over-anthropized territory is finally over. Town and country planning at zero-soil consuming is more and more frequent, at least in Europe. Limitation of soil use, urban regeneration, recovery of abandoned industrial areas, redevelopment, regeneration, requalification and reutilization of the building heritage, landscape protection and preservation of agricultural areas are the new imperatives of contemporary urban planning. Such ideas presuppose a different use of instruments such as the environmental impact evaluation and its extension to wider areas, the closer involvement of private capitals in planning and building operations, a more efficient economic use of historic sites and cultural goods, a stricter inclusion of public services in the planning activities, and many more operational devices.(22)

Sophisticated technologies must be intensively applied.(23) Necessarily, the Internet, social networks, and collection and use of data must be put at the service of infrastructure, utilities, and economic development, according to the theory that technology shall be functionalized for sustainable development.(24) Smart mobility is the first and simplest application of urban intelligence. Applications for access to or parking in town, person- or means-localization such as GPS, cameras, automatic billboards have been tested as techniques of traffic regulation according to energy, environmental or planning needs. Car-pooling

(22) In the enormous amount of literature on this subject, see e.g. N. BRENNER and N. THEODORE (eds), *Spaces of Neoliberalism: urban restructuring in North America and Western Europe*, Oxford, Wiley-Blackwell, 2002; A. AMIN and N. THRIFT, *Cities. Reimagining the Urban*, Cambridge, Polity Press, 2002; L.J.C. MA and F. WU (eds), *Restructuring the Chinese City, Changing Society, Economy and Space*, Abingdon, Routledge, 2005; S.R. CURWELL, M. DEAKIN and M. SYMES (eds), *Sustainable Urban Development*, London, Routledge, 2007; M. DEAKIN, G. MITCHELL, P. NIJKAMP and R. VREEKER (eds), *Sustainable Urban Development*, London, Routledge, 2007; L. VAN DEN BERG, E. BRAUN and J. VAN DER MEER, *National Policy Responses to Urban Challenges in Europe*, Farnham, Ashgate, 2007; S. ALBEVERIO, D. ANDREY, P. GIORDANO and V. VANCHERI (eds), *The Dynamics of Complex Urban Systems*, Leipzig, Physica, 2007; M.E. ALMIRALL, T. BAKICI, H. HIELKEMA et. al., "Smart Cities as Innovation Ecosystems Sustained by the Future Internet", EU Fireball White Paper; M. ALBERTI, G. BRADLEY and C. RYAN (eds), *Urban Ecology*, New York, Springer, 2008; P. JONES and J. EVANS, *Urban Regeneration in the U.K., Theory and Practice*, London, SAGE, 2008; S. TSENKOVA and Z. NEDOVIC-BUDIC (eds), *The Urban Mosaic of Post-socialist Europe*, Leipzig, Physica, 2008; M. PACIONE, *Urban Geography: A Global Perspective*, New York, Routledge, 2009.

(23) One of the more recent investigations on how technologies shape the smart cities can be found in K.S. WILLIS and A. AURIGI (eds), *Digital and Smart Cities*, New York, Routledge, 2018.

(24) See e.g. P.J. VERGRAGT, "How Technology Could Contribute to a Sustainable World", in *GTI paper series, Frontiers of a great transition*, Boston, Tellus Institute, 2006; H. SHAFFERS, N. KOMNINOS, M. PALLOT, M. AGUAS, R. VOS and D. ALARCÓN, *Technology and Innovation for Sustainable Development*, New York, Bloomsbury Academic, 2016; O. VERMESAN and P. FRIESS (eds), *Building the Hyperconnected Society: IT's Research and Innovation Value Chains, Ecosystems and Markets*, Aalborg, River Publ., 2015.

has been in use for decades. Car-sharing of electric vehicles handled through smartphones and social networks is already widely diffused. The deployment of low-environmental impact means of public transportation is under way. The next step is the accomplishment of a full mobility on demand, which allows individual persons to plan their movements and to buy their routes through one app only, irrespective of the means chosen. That would save billions of work hours, as well as enormous amounts of energy. It cannot be forgotten that some prominent voices favour a moderate use of technology for the sake of green values.(25)

Another implication of city smartness is the new regulation in the collection, treatment and disposal of waste, which has hygienic, economic, social, environmental, cultural effects and is capable of activating virtuous circles. The most common technology in this area is the so-called radio frequency identification (RFID), which allows garbage tracing and should eliminate or abate the NIMBY syndrome.

A pivotal idea in the concept of smart city is that of network, as a system of infrastructures interconnected through centralized ICT platforms, able to monitor mobility and transportation, logistics, energy use, urban safety. The main way to reach such aims is the use or re-use of the electric illumination network, thus making it an instrument of interconnected services. The European SET-PLAN(26) since 2012 has put in motion the Smart City European Initiative and a joint program managed by The European Energy Research Alliance (EERA).(27) A line of financing has been provided by the European Energy Efficiency Fund (EEEF).

A collection of scientific and technological devices, known under the name of domotics, tends to make a home more comfortable. Many of them are not quite recent but have been applied together in a sort of integrated management of the house. Home automation and gateways of connection with external networks introduce a smart coordination of illumination, heating and air conditioning, together with safety systems preventing intrusions and domestic accidents. Building automation at the condominium or complex level allows further savings, though with some possible risks in terms of privacy. The same blend of devices is useful for the verification of the state of real property, both from the viewpoint of seismic risks and building quality: the availability of such data in the cloud helps in formulating diagnoses about the future of the asset and

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(25) See e.g. J. VIITANEN and R. KINGSTON, "Smart Cities and Green Growth: outsourcing democratic and environmental resilience to the global technology sector", *Env. and Planning*, 2014, pp. 803-819.

(26) Commission Staff Working Document SEC (2009) 1295.

(27) On this point, see the Web portal EERA, including the complete description of the activities of the Joint Programme on Smart Cities: [www.eera-sc.eu/](http://www.eera-sc.eu/).

even insurance policies. Building materials belong to the same perspective: the capacity of resisting and reacting against humidity, mechanical stress, wind, acidity of air and water combine energy self-sufficiency, and adaptation to the environment. Bio-architecture and bio-building technology consist in smart materials. Bio-mimetics aim at achieving full eco-compatibility, reducing anthropic impact and using renewable resources.(28)

The use of information is another typical area where smartness requires capacity in collecting data, in sharing them in a proper manner and handling them for the betterment of the quality of living in the city. From the management of traffic to the control of criminality, smart cities help to widen the choice of services thus, increasing efficiency, reducing costs.(29)

### **3. Smartness and public administration: A fresh start**

The implementation of the concept of smart city implies a radical change of attitudes and methods on the side of the public administrations involved. It is easy to formulate at least some of the most important switches or even leaps that are requested from the public subjects implicated in the pertinent administrative actions. After the Second World War, several modernization cycles have been observed in the history of public administration.(30) The administrative procedure has been codified in several European countries, following the example of the U.S. Administrative Procedure Act: administrative justice has been rationalized and made faster and more efficient, as well as richer in terms of actions available; liberalizations and privatizations have changed the structural profile of public administration, even enlarging its notion; several types of administrative acts have given way to private law contracts, though retaining their capacity for pursuing public interests; and many others have been reformulated in order to allow some form of participation in their making.

(28) See e.g. P. GRUBER, *Biomimetics in Architecture: Architecture of Life and Buildings*, Vienna, Springer, 2011; P. CHEN, J. MCKITTRICK and M.A. MEYERS, "Biological Materials: Functional Adaptations and Bioinspired Designs", *Progress in Materials Sciences*, 2012, p. 1653.

(29) Lately, see for example A.M. TOWNSEND, *Smart Cities. Big Data, Civic Hackers, and the Quest for a New Utopia*, New York, Norton & Co., 2013; R. KITCHIN, "The Real-Time City? Big Data and Smart Urbanism", 79 *GeoJ.*, pp. 1-14; K. KOURTIT, P. NIKKAMP and J. STEENBRUGGEN, "The Significance of Digital Data Systems for Smart City Policy", 58 *Socio-Ec. Planning Sc.*, 2017, pp. 13-21.

(30) See e.g., J.C.N. RAADSCHELDERS, "Administrative History", in *The SAGE Handbook of Public Administration* (B. GUY PETERS and J. PIERRE eds), 2<sup>nd</sup> ed., London, SAGE, 2012, p. 207; and H.G. RAINEY, "Public Management: old and new", in *The SAGE Handbook of Public Administration*, op. cit., pp. 13 and ff.; H.-U. DERLEIN, *From administrative reform to administrative modernization*, Bamberg, BUP, 1998; C. POLLITT and G. BOUCKAERT, *Continuity and Change in Public Policy and Management*, Cheltenham/Northampton, Edward Elgar, 2011.

An even greater innovative capacity is required now. In a relatively short time span, a real reconversion is needed.

First, a more modern interpretation of urban planning techniques has been imposing itself on architects, lawyers, planners of all kinds. They have been progressively compelled to shift from the traditional approach, consisting of an authoritative and unilateral regulation of the use of land, imposed on private subjects, to a reasoned negotiation between the responsible local authorities and their consultants on one side and the economic operators on the other. The aim is no longer to find the optimal theoretical order in terms of town planning from the exclusive viewpoint of public interests, but to strike a balance between them and the capacity of private investors to support public initiatives concerning for instance the recovery of buildings, blocks or urban districts, mainly in case of deindustrialization, total renewal or decontamination. Compromises can be found on grounds such as the recognition of building rights in other parts of the town, in advantages acknowledged in the form of free access to public networks or other technological devices, of public transportation facilities, of energy plant sharing, and many others. The opening of town planning to the participation of the public is nothing new. Since the 1940s it has become compulsory both in Europe and the United States, thanks sometimes to the general codification of the administrative procedure or due otherwise to the introduction of special planning provisions. However, this recent trend is becoming a real ideological turning point in the history of planning, away from imperative models towards negotiation patterns.(31)

Obviously, this kind of cooperation in urban planning procedures takes different shapes according to the local contexts: in countries where there still is a large availability of land, building programs can afford to be slack or at least to operate in conditions of lesser normative density. On the other hand,

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(31) See e.g. L.G. ANTHOPOULOS and A. VAKALI, "Urban Planning and Smart Cities: interrelations and reciprocities", in *The Future Internet Assembly* (F. ÁLVAREZ ed.), Cham, Springer, 2012, pp. 178-189; S. LELAND and D. READ, "Stimulating Real Estate Development through Public-Private Partnerships: Assessing the Perceived Opportunities and Challenges", *Pub. Ad. Q.*, 2012, pp. 311-340; B.T. GOLDSTEIN and C. MELE, "Governance within public-private partnerships and the politics of urban development", *Space and Polity*, 2016, pp. 194-211; R. FARHAT, "Accountability in urban regeneration partnerships: A role for design centers", *8 Cities*, 2018, pp. 8-16. Empirical case studies, e.g., in E. HEYRKENS and F. HOEBA, "Private Sector-led Projects. Comparative Insights from Planning Practices in the Netherlands and the UK", *Planning Practice & Res.*, 2014, pp. 350-369; M. MILENKOVIĆ, M. RAŠIĆ and G. VOJKOVIĆ, "Using Public Private Partnership Models in Smart Cities – proposal for Croatia, Information and Communication Technology", *Electronics and Microelectronics (MIPRO)*, 2017, pp. 1656-1661; R. HENRIQUE DE OLIVEIRA and M. PINHANEZ, "Public Private Partnership and the promotion of smart cities initiatives – Insights from Rio de Janeiro", *Brazilian J. of Marketing Research, Opinion and Media (PMKT)*, 2017, pp. 375-388; C. TESTONI and A. BOERI, "Smart Cities: Public Policies and Business Models for a Sustainable Development. Stakeholder Networking and Innovative Public Procurement in Italy", *Architectonica*, No. 4/2015, pp. 29-45; as far as the United States are concerned, see D. CUSTOS and J. REITZ, "Public-Private Partnership", *Am. J. of Comp. L.*, 2010, pp. 555-584.

in countries where land consumption has already been high, especially in Europe, and zero-expansion plans are necessary due to the need to prevent new localizations in non-urbanized areas, land use is more likely to be bound by stricter and more rigid rules, notwithstanding the cooperative approach.

Furthermore, contemporary plans must include a number of services that used to be peripheral, but now need to be encompassed and incorporated lest they might be set aside, projected and executed separately, jeopardizing the smartness of the city itself. Some authors<sup>(32)</sup> give the examples of e-business services, e-health and tele-care services, e-learning services, e-security services, environmental, transportation and communication services. The contents of town plans become, therefore, much wider and richer. Their very nature changes from a mere regulation of an urban territory to coordination of building activities with all kinds of networks, whose coexistence and interaction are the essence of smartness.

From the viewpoint of the administrative instruments to be applied to the relationship between public authorities and private operators, the trend is necessarily towards a lesser use of the classical administrative acts, such as licenses, permits, concessions, and assenting to the use of land, and a growing recourse to public/private partnerships allowed by European directives and regulations. Such instruments are preferable due to greater flexibility in the choice of private partners and adaptability during the carrying out of the operational activities.<sup>(33)</sup> This approach is even more evident in administrative law countries, where the traditional culture would easily recommend the adoption of the typical and much less creative unilateral acts: even in such contexts it is often alleged that open auction mechanisms or classic tender procedures are less efficient than public-private partnerships.<sup>(34)</sup> It is widely believed that these more modern instruments of administrative action have fewer drawbacks and many more advantages than the traditional ones. These modern instruments are probably quicker or at least shield public

(32) L.G. ANTHOPOULOS and A. VALAKI, "Urban Planning and Smart Cities: interrelations and reciprocities", *op. cit.*, p. 184.

(33) In the recent literature see e.g. J.F.M. KOPPENJAN and B. ENSERINK, "Public-Private Partnerships in Urban Infrastructures: Reconciling Private Sector Participation and Sustainability", *Pub. Ad. Rev.*, 2009, pp. 284-296; D. CUSTOS and J. REITZ, "Public-Private Partnerships", *op. cit.*; G.A. HODGE, C. GREUVE and A.E. BOARDMAN, *International Handbook on Public-Private Partnerships*, Cheltenham, Edward Elgar, 2010; S. LELAND and D. READ, "Stimulating Real Estate Development through Public-Private Partnerships", *op. cit.*; E.I. HOPPE and P.W. SCHMITZ, "Public-Private Partnerships versus Traditional Procurement: innovation incentives and information gathering", *Rand J. Econ.*, 2013, pp. 56-74; R. CHAKRABARTI KUMAR and V. PRATAP, *Public-Private Partnerships in Infrastructure: managing the challenges*, Cham, Springer, 2018.

(34) See e.g. L. CHEVER and A. LE LANNIER, "Regulatory Instruments for Public-Private Partnerships", in *The Economics of Public-Private Partnerships. Theoretical and Empirical Developments* (S. SAUSSIER and J. DE BRUX eds), Cham, Springer, 2018, pp. 39-77.

authorities from delays both in the construction and operation phases,(35) thus eliminating hidden costs. They allow public subjects to rely on fixed-price contracts, loading all extra costs on private investors, thus converting additional financial costs in a sort of insurance premium, though the situation of the loan market may create excessive risks and/or render financial engineering less functional, suggesting the return to the old comfortable public procurements.(36) They partially relieve public subjects from the demand for public works in times of fiscal stress. They help administrative authorities to draw back from an active role in terms of control of the use of resources as input into the administrative action and to switch to a regulatory role aimed at checking the quality of the outputs.(37) It is obvious that they fit better in times of financial stability, while they are put at risk in times of restrictions to access to financing.(38) Nevertheless, the changes in the debt market can be coped with through adjustments in the balance between public subjects and private investors through appropriate clauses. Some literature has commented on this evolution, describing the new trend as a re-internalization process(39) or even doubting that the model has preserved its original shape, formed around the idea of a prevalent or exclusive financing.(40)

#### ***4. Smartness and public procurements***

Another important innovation related to the implementation of the idea of the smart city, though not exclusively depending on it, is the introduction into the regulation of public procurements of a new sensibility towards environmental interests. That has not meant the simple creation of a special type of procurements; it has implied the adoption of new criteria, applicable to all public procurements, aiming at orienting public authorities towards purchasing goods and services that are less dangerous for the environment with preference and in comparison with other less environmentally friendly categories. Given the enormous purchasing power of the public contracting authorities, representing significant shares of the GDP,(41) green choices by

(35) S. DOMBERGER and P. JENSEN, "Contracting out of the Public Sector. Theory, evidences, prospects", *Ox. Rev. Econ. Policy*, 1997, p. 67.

(36) F. BLANC-BRUDE, H. GOLDSMITH and T. VÁLILÁ, "A comparison of construction prices from traditionally procured roads and PPPs", *Rev. Ind. Org.*, 2009, pp. 19-40.

(37) F. MARTY, S. TROSA and A. VOISIN, *Les partenariats public-privé*, Paris, La Découverte, 2006.

(38) Standard & Poor's, *Anatomy of construction risk: Lessons from a millennium of PPP experience*, London, 2007.

(39) See e.g. F. MARTY, "The Evolution of Financing Conditions for PPP Contracts: Still a Private Financing Model", in *The Economics of Public-Private Partnerships*, *op. cit.*, pp. 79 and ff.

(40) Some literature also confronts the problem of partnership from the side of private operators: see e.g. F.D. SANDULLI, A. FERRARIS and S. BRESCIANI, "How To Select the Right Public Partner in Smart City Projects", *R & D Management*, 2017, pp. 607 and ff.

(41) In the EU it is alleged to amount to about 17%.

public subjects have a strong capacity for reorienting consumers towards green products, to stimulate their production and to trickle down influence to other significant segments of the market. The main hurdle in the achievement of such results could consist in the informative deficit of public authorities, which are normally poorly aware of technological progress and might resent structural asymmetry in their relationship with the private sector. The obvious remedy, therefore, is the recourse to flexible techniques in the adjudication of public procurements, such as competitive dialogue and other negotiation practices, that favor a growing acknowledgement of the acquisition of the result of scientific research on the side of the administrations. From a more ideological viewpoint, green procurements belong to a wider philosophy of sustainable development, meeting the needs of the present generation without sacrifice for the expectations of future generations, and supporting economic growth only within the limits of the betterment of the quality of environment, health, life and of the rational use of resources. In economic terms, the idea of the market as a value in itself boosts the use of tenders founded on simple, transparent, non-discriminatory competition criteria leaving no or little room for non-strictly-economic parameters. However, energy and environmental factors have been gaining the attention first of scholars and later of the global public opinion, substantially modifying the traditional approach.

In the EU context, the starting point has been a Communication of 2001.<sup>(42)</sup> Already in the Maastricht Treaty of 1992 the balanced development of economic activities and the principle of sustainable growth had found their way into the primary rules of the Communities. In the Amsterdam Treaty of 1997 the integration principle was included in Article 6, now 11, of the Treaty on the working of the UE, and gave birth to the White Paper on Public Procurements of 1998,<sup>(43)</sup> recognizing the protection of the environment as a fundamental component of a modern economy. In 2001 the Sixth Program for the Environment<sup>(44)</sup> mentioned the need for separating environmental deterioration from economic growth. Then, Directive 2004/17 and 18 for the first time recognized the possibility of taking into account non-economic factors, including the environmental ones, in the adjudication of tenders.<sup>(45)</sup> Since that time, all of the EU legal systems have dedicated some attention to several aspects of the eco-qualities of the goods or services at stake in public procurements. For instance, the contracting authorities are authorized to emphasize the environ-

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(42) EU Comm., "Interpretative communication on the Community law applicable to public procurement and the possibilities for integrating environmental considerations into public procurement", COM (2001) 274.

(43) White Paper, "Public Procurement in the European Union", COM (1998)143.

(44) EC Comm., "Environment 2010: Our future, our choice", 24 January 2001, COM (2001) 31.

(45) Considering 1, 2, 5.

mental<sup>(46)</sup> qualities of the object of the tender, prescribing functional requirements or quality performances related to environmental conditions starting with the framing of the technical specifications. Some of them may be defined through mechanical reference to European or multinational eco-labels. Eco-labels carry a presumption of conformity to the required prescriptions. Eco-conditions are usually unreviewable by the judges in charge of the control of administrative action, although they cannot be used to create unjustified obstacles to competition. Serious environmental crimes can be qualified as causes of exclusion from public procurements. Specific environmental experience, when having some relation with the object of the tender or its execution, can contribute to the technical capacity of the bidder, which can also be demonstrated through adherence to systems of environmental management, the most consolidated of which is the Eco-Management and Audit Scheme (EMAS).<sup>(47)</sup> According to Article 53 of Directive 18, when the adjudication system is the economically advantageous offer, the contracting authority has discretion to introduce green criteria into the method of selection of the bids, provided that the system works out in reasonable terms. Special conditions, also with reference to green clauses, can be imposed on the execution of the contract, in the application of Article 26 of Directive 18, on condition that they are made known from the beginning of the procedure.<sup>(48)</sup>

A great number of EU soft law acts, adopted after 2010,<sup>(49)</sup> have consistently followed the same line. The quality/price objective has advanced together with the promotion of social needs, including protection of the environment, energy efficiency, struggle against climate change. The achievement of the Europe 2020 strategy for sustainable growth has been more and more clearly connected with the public procurement policy. Research and innovation have also been related to the best use of public procurements in order to promote sustainable growth, for instance applying the concept of life-cycle costing as a measure to save energy and at the same time economic and environmental costs. Many other suggestions have been elaborated according to this philosophy: for example, it was proposed that violations of European environmental obligations were relevant both as a cause of

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(46) See ECJ, 25 March 1995, C-324/93; ECJ, 17 September 2002, C-513/99; ECJ, 10 April 2003, C-20/01 and 28-01.

(47) Several EMAS Regulations have been issued over time, such as 1993/1836/CEE (EMAS I), 2001/761/CE (EMAS II), 2009/1221/CE (EMAS III).

(48) The state of the story at 2008 in G. BELLOMO, "Il Green Public Procurement nell'ordinamento multilivello dell'ambiente", *DPCE*, 2008, pp. 940-959.

(49) See e.g. EU Comm., 2020, 3 March 2010, COM (2010); EU Comm., "The Green Paper on the modernisation of EU public procurement policy: Towards a more efficient European Procurement Market", 27 January 2011, COM (2011) 15; EU Comm., "Making Public Procurement work in and for Europe", COM(2017), p. 572.

exclusion of an operator and as matter of verification in case of anomalously low bids.

With some elements of prudence, many of these suggestions have been accepted in the drafting of the new Directives 2014/23, 24 and 25. Several provisions of such Directives implement different aspects of the idea of green procurements.<sup>(50)</sup> The notion of life-cycle, for instance, is precisely defined and firmly practiced.<sup>(51)</sup> The State legal systems are supposed to adapt it to different aspects of the adjudication and execution of the procurement.<sup>(52)</sup> The main element of novelty is probably the transformation of the adjudication at the lowest price into lowest cost, which includes all the environmental externalities.<sup>(53)</sup>

After the Directives, the EU Commission has collected and disseminated data, identified best practices and suggested the widespread adoption of new public procurement models in order to boost the trend toward city smartness. Since April 2016<sup>(54)</sup> it has described procurements as “an enormous and overlooked opportunity to spur innovation”, even if there is wide consciousness of the difficulty related to legacy process, lock-in and the diffused preference for large integrated contracts. Indications from real cases show that Public-Private Partnership (PPPs) are by far the preferred formula. The most widely applied procurement models are innovation platforms, also called participation platforms. These platforms have been used widely in places such as Copenhagen. Widespread use implies a call for support to experts, entrepreneurs and other stakeholders, the creation of innovation teams, fixed budget, production of prototypes, recourse to compulsory consortiums. Another successful formula is the pre-commercial procurement (PCP), founded on the collaboration with the authorities and the bundling of demand. It has been used in towns such as Eindhoven, Malmö and Bassano del Grappa in the field of public lighting. Such models are progressively moving to the field of infrastructures.<sup>(55)</sup>

(50) Starting from considering 2, 41, 47, 91, 96 and 123 of Dir. 24/2014; consid. 4 of Dir. 2014/25 and consid. 3 of Dir. 2014/23.

(51) Art. 67 and 68.

(52) The Italian reception in G. FIDONE and F. MATALUNI, “Gli appalti verdi nel codice dei contratti pubblici”, *Riv. Quadr. Dir. Amb.*, 2016, pp. 4-62.

(53) See S. VALAGUZZA, *Sustainable Development in Public Contracts. An Example of Strategic Regulation*, Naples, Editoriale Scientifica, 2016; and R. CARANTA, “Helping Public Procurement Go Green: The Role of International Organizations”, *EPPPL*, 2013, p. 49.

(54) EU Com. report, *Analysing the potential for wide scale roll out of integrated Smart Cities and Communities solutions. Public procurement models for SCC solutions*, April 2016; EU Com. report, *Smart Cities. Stakeholder Platform. Public Procurement for Smart Cities*, November 2013.

(55) See e.g. J.M. KOH, *Green Infrastructure Financing. Institutional Investors, PPPs and Bankable Projects*, Cham, Springer, 2018.



## CHAPTER 6

### Public Contracts and Smart Cities

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#### *1. Introduction*

We, all the contributors to this book, could certainly give examples of how, in our own jurisdictions, technological changes suddenly brought about significant evolutions in the law of public contracting. French students learning administrative law of contracts soon hear a reference to a famous case of 1902 in which the Council of State ruled that a municipality which had entrusted a private company with the public lightning using gas could impose on this company to move to electric lightning, since this technology had become available and appeared to be more convenient: in case the company would refuse, the municipality could terminate the contract and choose another contractor.<sup>(1)</sup>

Due to technological innovation, the functioning of our cities (*i.e.*, becoming ‘smart’), is certainly in a phase of profound transformation. The purpose of this chapter will be to make some suggestions about the changes this transformation may induce in the legal arrangement of public contracting.

We will first try to identify the main lines of transformation which are caused by the ‘smart city’ revolution in the functioning of cities (*see* Section I, below), then point to some related consequences already perceptible in contractual procedures and regimes (*see* Section II, below), and finally propose some assumptions about what could be some long-run consequences on categories of contracts made by local authorities in the context of urban management (*see* Section, III, below).

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(1) Conseil d’État, 10 January 1902, Compagnie Nouvelle du Gaz de Deville-lez-Rouen.

## **2. Transformations Induced in Urban Functioning by the Evolution Towards ‘Smart Cities’**

There is not one and only way of defining the ‘smart cities’ movement; nevertheless, it seems possible to assert that it is the product of a triple set of transformations in the practical functioning of cities: (2) a transformation of infrastructures, the growing importance of digitalization and data, and changes in governance.

### 2.1. Transformation of the urban infrastructure

Generally speaking, what is in motion in ‘smart cities’ is an overall advance in urban functions and services caused by new technologies, which provide new solutions to the old problems which have been poisoning the urban life for so long: traffic congestion, air pollution, lack of security, and the like.

‘Smart cities’ technologies manage to improve the urban functioning by modernizing the existing urban services and by creating new ones, (e.g. shared mobility, new types of communications).

At the same time, the ‘smart cities’ evolution transforms the urban infrastructure by enriching it with new developments (e.g., new communication tools). It also has the tendency to impose a growing interconnection between its various component parts (*i.e.*, the water distribution infrastructure conveys data which are valuable for the prevention of floods, the urban furniture is essential for dispatching information, and so on).

Relatedly, the urban infrastructure is nowadays capped by a digital ‘meta-infrastructure’, which is essential to its interconnection and its coordination.

### 2.2. Digitalization and data

Data are the real fuel of ‘smart cities’. In the latter, firstly, an enormous quantity of data is constantly created or collected. Some of those data are elaborated in a sophisticated way by the various parts of the urban infrastructure, others are simply traces left in captors (e.g., the traces our mobile phones leave on the operators’ computers each time we pass close to one of their relays). One of the important facts in digitization is that the collection of data in “smart cities” is made by both the private actors and the public ones.

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(2) A. TOWNSEND, *Smart Cities*, New York, Norton & Co., 2013; *Ville intelligente, ville démocratique?*, symposium organised by Berger-Levrault and the Chair “Mutations de l’Action Publique et du Droit Public” of Sciences Po, Berger-Levrault, 2014.

Once data are collected, they are in general assembled and linked in order to contribute to some services; using traces left on their relays, for example, telecommunications providers can provide municipalities with information concerning the mobility of people in the city.

With the development of ‘open data’ in many cities, urban data can also be ‘reused’ by citizens or private businesses in order to create new services, and in particular applications for smartphones concerning transportation, real estate opportunities, neighborhood security and so on.

### 2.3. Changes in governance

‘Smart cities’ evolutions also induce transformations in the relationship between the public authorities and the private sectors of the community. In fact, the changes in their relationship are already emerging, specifically in the distribution of their functions. For instance, private infrastructures, especially in communications, have become an essential component to the city’s overall functioning. This may lead to the development of new public-private partnership; an arrangement which is not always easy to build, even if it only involves the sharing of data that potential partners consider as a source of wealth.

One of the possible problems of this new type of relationship centers on the issue of governance (*i.e.*, “who governs the smart cities?”). That is, what will be the exact role of municipalities in the face of autonomous mobility, autonomous production of energy, and the like? Apparently, the national legislations are still silent on this issue.

Further, the ‘smart cities’ transformations are also capable of transforming the relationship between local government and the citizens. Through open data, the citizens in ‘smart cities’ have become more completely informed of the various aspects of city life; they are in a better position to develop their own urban services. A new political balance is being prepared.

### ***3. (Already partially observed) consequences upon contractual procedures and regimes***

Consequently, the ‘smart cities’ evolutions affect the contractual procedures and regimes. These consequences are in fact pushed forward by three factors: digitalization of procedures and overwhelming presence of data, well-rooted concern for sustainable development, and the centrality of innovation.

### 3.1. Digitalization of procedures and overwhelming presence of data

Smart cities are sometimes called ‘digital cities’. Although the term is a bit restrictive, it certainly refers to the essential features of “smart cities” functioning, which is widely driven by digital technologies and data. In the field of public contracting, it has obvious advantages but it also raises a range of issues.

Digitalization promotes transparency in contractual procedures,<sup>(3)</sup> thereby making it an essential pillar of ‘smart procurement’, as promoted by the European Commission.<sup>(4)</sup>

At the same time, the digitalization process of cities can cause difficulties related to public contracting situations and arrangements.

In order to develop the digital infrastructure of their territories, local governments have to find contractual solutions since, in general, they do not possess the corresponding technical expertise at a sufficient level. The local governments sometimes resort to concession-type arrangements: the problem being, when this orientation is chosen, that it means building a contractual arrangement in which the private contractor assumes a significant economic risk, otherwise the contracts cannot have the nature of concessions under EU law.<sup>(5)</sup>

Another question derives from the fact that contractors of municipal authorities collect, in the implementation of the contract, a certain quantity of data, which the authorities will in general be willing to recover since those data will frequently be quite useful to the accomplishment of municipal functions. The problem is that, for the contractors, these data are commercial assets they will often want to keep for themselves.

If we look at French law on the issue, up to recently, there was no general principle, and this meant that the solution was left to the contracts, which often did not contain any stipulation on the subject. The recent law on digital assets in public action<sup>(6)</sup> has tried to address the issue, and introduced into the law on concession contracts<sup>(7)</sup> a concept of ‘general interest data’, which is developed in the following terms:

“Where a public service is contracted out, the contractor will make available to the public authority all data and databases collected and produced in

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(3) J.R. GRANADOS *et al.*, “Ciudades inteligentes, compras inteligentes, Analisis de la incidencia de las TIC en la transparencia contractual de la administracion local”, in *Regulating Smart Cities* (J.B. PADULLÈS *et al.* eds), Barcelona, Universitat Obertat de Catalounya, 2015, p. 346.

(4) EC, “Public Procurement for Smart Cities”, November 2013.

(5) F. OLIVIER and N. SULTAN, “Les schémas d’aménagement numérique en pratique: portage et contrats public”, *Contrats et Marchés Publics*, April 2012, p. 7.

(6) Loi sur la République Numérique, 7 October 2016.

(7) Law of 29 January 2016 on concession contracts, Art. 53(1).

the operation of the public service and which are indispensable to its implementation, in an open standard freely reusable and usable by an automated processing system”.(8)

The other side of the same coin stems from the development of cities’ open data. Normally, among the information which is made public through open data are the contracts made by local authorities, either pursuant to legal obligation or by voluntary choice.(9)

Then, an important limit to the open diffusion of data related to contracts will result from the fact that a part of these data is personal (example: consumption of water or gas by users of a contracted-out water or gas distribution public service), and thus cannot be made public without anonymization, while others can be commercial data which the contractor may lawfully require to be kept secret.

### 3.2. Concern for sustainable development

One can say that the smart city is a daughter of the sustainable city. It is the same historical movement that carries the two mutations: in a sense, the smart city is the sustainable one, with the addition of the ‘fuel’ brought by digital technologies.

Thus, in the smart city, all the efforts made in order to address sustainability concerns and the requirements concerning transparency and fair competition in public contracts are prolonged, whether they are related to environmental criteria in the allocation of public contracts or to environmental conditions in the implementation of contracts.

There is no need to elaborate on it, since it is a question that did not wait for the smart cities to be well-framed.

### 3.3. Innovation as a central issue

A major feature of the services provided by smart cities is that they are often new or, if they already exist, they are transformed in their practical application by new technologies. For that reason, the development of the smart city’s new functionalities constantly imposes a high degree of innovation. This has huge consequences in contractual practices of urban governments: they must absolutely get the most innovative solutions when awarding new contracts, as well as when renewing existing contracts.

(8) “*Lorsque la gestion d’un service public est déléguée, le concessionnaire fournit à l’autorité concédante, sous format électronique, dans un standard ouvert librement réutilisable et exploitable par un système de traitement automatisé, les données et les bases de données collectées ou produites à l’occasion de l’exploitation du service public faisant l’objet du contrat et qui sont indispensables à son exécution*”.

(9) In the French system, the administrative procedure Act (“*Code des relations entre l’administration et les administrés*”) imposes the obligation of having an open data system on all local governments whose population exceeds 3.500 inhabitants (Art. L.312-1-1).

The problem is that the traditional regulation of public contracting is not excessively compatible with innovation. Strong formalism, emphasis on the price criterion for the award of the contract, transparency requirements that put candidates at risk of free delivery of their innovative secrets without obtaining the contract – all this hampers the development of what the OECD calls ‘procurement for innovation’.(10)

However, legislators and in particular the European ones have become aware of these obstacles, and they have recently tried to pave the way for innovation in contractual procedures, in particular by the creation of the Innovation Partnership, by the 26 February 2014 Directive on procurement.(11)

The main characteristics of this mechanism are well defined in the article 31.2 of the Directive:

“2. The innovation partnership shall aim at the development of an innovative product, service or works and the subsequent purchase of the resulting supplies, services or works, provided that they correspond to the performance levels and maximum costs agreed between the contracting authorities and the participants.

The innovation partnership shall be structured in successive phases following the sequence of steps in the research and innovation process, which may include the manufacturing of the products, the provision of the services or the completion of the works. The innovation partnership shall set intermediate targets to be attained by the partners and provide for payment of the remuneration in appropriate instalments.

Based on those targets, the contracting authority may decide after each phase to terminate the innovation partnership or, in the case of an innovation partnership with several partners, to reduce the number of partners by terminating individual contracts, provided that the contracting authority has indicated in the procurement documents those possibilities and the conditions for their use”.

The essential keys of the instrument are, thence, that innovation can be developed within the award process and candidates are not obliged to disseminate their innovations before being sure to get the contract.

With this, naturally, all possible problems are not solved. Thus, for example, the question of who will have the intellectual property rights in the innovations has to be dealt with in contracts. In general, it will probably be admitted that the contractor has them, but also that the public entity does not have to pay for the use of them in the ambit of the contract. In some cases,

(10) OECD, “Public Procurement for Innovation, Good Practices and Strategies”, 2016.

(11) Called ‘partenariats d’innovation’, in France innovation partnerships were introduced into French law by a decree of 26 September 2014. For guidelines emanating from the Ministry of Economy’s legal section: [www.economie.gouv.fr/daj/partenariat-innovation-2016](http://www.economie.gouv.fr/daj/partenariat-innovation-2016).

though, the public entity will have made a significant intellectual input into the innovation and then the intellectual property rights will have to be shared – including for the future through a consortium agreement.(12)

To conclude this point, it should be mentioned that the deployment of innovations in smart cities will only be effective if an effort is made to standardize certain products and processes that are intended to be replicated extensively. Standardization is a catalyst for innovation, as the OECD says.(13) And standardization has big consequences on public contracting, in which it enhances the homogenization tendencies.

#### ***4. (Probable) long-run consequences on categories of contracts***

If one turns to the long term, one can be convinced that the smart cities developments are likely to change deeply the geography of contractual practices in local governments.

A general impression which one can have is well formulated by an author, who suggests that “Smart Cities public procurement is much more likely to take the shape of services – and performance-based contracts rather than supply-and technical specification-oriented contracts”.(14)

A similar idea can be expressed by saying that urban public contracting in smart cities is likely to evolve towards wider shaping: more parties assembled, more (functionally) global contracts, longer terms.

##### **4.1. More parties assembled**

If, as we suggested, one of the characteristics of smart cities is that functions and pieces of infrastructure will be more and more interconnected, this will probably mean that local authorities will have to gather around them, in order to rationalize the whole urban functioning, a wider number of actors than they usually do.

One can then anticipate contractual arrangements in which a wider range of contractors will be present. This can lead to legal difficulties concerning for example liability imputation: when something goes wrong in a wide set of interconnected actors, it becomes more difficult to determine who is at the origin of the dysfunction.

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(12) Advancity, “Innovation et villes durables : repères pour l’action”, Note d’approfondissement juridique, 2015

(13) OECD, “Public Procurement for Innovation, Good Practices and Strategies”, *op. cit.*, p. 10.

(14) S. VERMA, “Smarter Public Procurement for Smart Cities in India: Outlining Procurement Challenges and Reforms for Increasingly Complex and Innovative Government Contracts”, in *BW Smart Cities World*, Iss. 3 July-August 2015, pp. 70-75.

This first line of evolution is very much linked with the second one.

#### 4.2. More (functionally) global contracts

Indeed, if the prospect of a growing interconnectedness of functions and pieces of infrastructure is correct, then it likewise implies that local governments will have to settle more complex contractual arrangements with their partners.

One can imagine, for example, that these complex contracts could be made ‘urban management contracts’, by which a municipality would entrust multi-expertise entities with the task of, for example: renovating – in a sustainable way – an urban area, and then, during a certain time, making sure that utilities are provided in it, ensuring that energy autonomous mechanisms would remain operative, and also collecting, transferring data and making possible their reuse, et cetera.

It is clear that such contractual organizations will confront various rules which, in contemporary procurement law, rather favor the ‘splintering’ of contracts in order to make competition more intense and effective. It is true that rules concerning pure public procurement as well as concessions sometimes leave open the way to global contracts, in which contractors are entrusted with several different functions assembled, but they remain enclosed within strict conditionality.<sup>(15)</sup>

Legislation will probably have to be made more flexible, or alternatively opened to new types of contracts of the ‘urban management’ type.

#### 4.3. Longer terms

In line with what has just been explained, if the public contract regime has to be adapted to the ‘globalizing’ needs of interconnected smart cities, it will also have to shift in the sense of more readily accepting long-term contracts, and making the contractors responsible for the overall management of the infrastructure of an area of the city during a period of time which obviously cannot be too short.

In the current state of public procurement law, this meets the same kind of limits that confront functionally global contracts.

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(15) In the context of French Law, see F. TENAILLEAU, “Les contrats globaux après l’ordonnance du 23 juillet 2015 relative aux marchés publics”, *Rev. dr. immob.*, January 2016, p. 15.

# CHAPTER 7

## Procurement and Smart Cities: Exploring Examples on Both Sides of the Atlantic

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### *1. Introduction*

Smart cities are the new Eldorado for companies in developed countries.<sup>(1)</sup> They create new opportunities in the already saturated market of old infrastructure: booming innovations trigger new services and new demands, connected devices call for replacement of a lot of existing goods, virtual services produce tons of data, fueling a new market. Stakes and expectations are high in an area where there seems to be no limits for innovation. Across the Internet, consulting firms and startups advertise about their knowledge and expertise in the making of smart cities. Established or incumbent service providers prospect local officials, proposing smart “turnkey” projects.

But current smart cities initiatives around the world remain heterogeneous, scattered, and still in their infancy, exploring several business models. Smart cities projects are developed at different speeds, based on different legal arrangements, and contractual options. While countries in Europe, Asia and elsewhere took the first steps in promoting the concept of smart cities, the effort to develop smart cities has gained momentum in the United States in recent years. This chapter discusses smart city efforts in France and in the U.S., in particular, the early success in the city of Philadelphia in developing smart city initiatives, and its move toward a more comprehensive smart city program.

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(1) See L.G. ANTHOPOULOS, *Understanding Smart Cities: A Tool for Smart Government or an Industrial Trick?*, New York, Springer, 2017; a prior version of this piece was published through the *Ius Publicum Network Review* ([www.ius-publicum.com](http://www.ius-publicum.com)), issue 2, 2018.

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The smart city concept, as applied in the U.S., is consistent with its application in other parts of the globe. For example, in a 2016 report, the National League of Cities (NLC), which was founded in 1924 as a national organization to strengthen local governments, notes that:

“Smart city initiatives involve three components: information and communication technologies (ICTs) that generate and aggregate data; analytical tools which convert that data into usable information; and organizational structures that encourage collaboration, innovation, and the application of that information to solve public problems”.

For many countries, green and sustainable development is also an essential objective embedded in smart cities projects. However, as things are evolving rapidly in this field, smart cities projects may vary. Traditional legal frameworks must be adapted for smart cities as they require several *ad hoc* regulations such as intellectual property regulation, transparency and data regulation, energy regulation, environmental regulation, or dedicated sources of financing. In this context, the question of the choice of the legal framework and of the optimal contractual mode takes on many dimensions, seemingly only practical but in fact highly theoretical as well. In today’s transparent environment with public decisions prepared under the scrutiny of citizens, classical questions about privatization, or public ownership, free negotiations or competition, performance monitoring and public service obligations, are becoming more sensitive at the local level. Where experiments are mushrooming, public contracts are considered as tools that can be mobilized for building and operating smart cities. Flexible in scope to a certain extent but sometimes rigid during their formation process, public contracts may offer an interesting legal answer in the era of ‘smart cities’. One can indeed identify trends: (1) a variety of services surpassing the single goal which characterized traditional procurement contracts; (2) questions regarding the traditional public procurement procedures; (3) a call for collaborative innovation between the public and the private sectors; (4) the need for smart public and private financing; and (5) an integrated, decentralized, and evolving delivery of material and immaterial services calling for specific contractual clauses. Each of these elements raises legal issues, with exponential difficulties, only mentioned by this modest chapter exploring, through several examples, how public contracts could be vectors for innovation in smart cities.

## ***2. Public Policy as Main Driver for Smart Cities' Innovation***

Smart cities projects are usually promoted by public champions. In September 2015, the Obama administration announced a smart cities initiative that sought to:

“[I]nvest over \$160 million in federal research and leverage more than 25 new technology collaborations to help local communities tackle key challenges such as reducing traffic congestion, fighting crime, fostering economic growth, managing the effects of a changing climate, and improving the delivery of city services”.<sup>(2)</sup>

In a related effort, initiated in December 2015, the U.S. Department of Transportation (DOT) issued a Smart City Challenge that asked mid-sized cities across America to develop ideas for an integrated, first-of-its-kind smart transportation system that would use data, applications, and technology to help people and goods move more quickly, cheaply, and efficiently.<sup>(3)</sup> DOT received 78 responses and chose 7 finalists to work with DOT to further develop their ideas.<sup>(4)</sup> In addition to efforts at the federal level, organizations such as the Smart Cities Council are actively involved in promoting smart city development by bringing together public sector leaders, experts and other stakeholders to raise awareness about smart technologies.<sup>(5)</sup> Thus, as these examples indicate, the U.S. smart city effort has involved a range of local, national and federal initiatives. In addition to Philadelphia, the U.S. cities involved in the early smart city efforts included: New York, San Francisco, Boston, Seattle and San Jose. As of 2017, many more U.S. cities are pursuing smart city initiatives.

Philadelphia's smart city effort was initiated during Michael Nutter's tenure as mayor of the City, from 2008 through 2016. Prior to his election as mayor, Nutter was a member of the Philadelphia city council for 15 years. This breadth of experience gave Nutter insights into the dynamics of municipal government. As mayor, Nutter recognized the importance of analyzing data as it relates to a city's activities, and also understood that in terms of data collection, Philadelphia needed a more complete sense of measurement.<sup>(6)</sup>

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(2) See Fact sheet, “Administration Announces New ‘Smart Cities’ Initiative to Help Communities Tackle Local Challenges and Improve City Services”, The White House, Office of the Press Secretary, 14 September 2015.

(3) See U.S. Department of Transportation, “Smart City Challenge”, December 2015.

(4) *Ibid.*, p. 3.

(5) See Smart Cities Council, Web site.

(6) S. GOLDSMITH, “Infusing Government with a Data-Driven Culture, Philadelphia's former mayor explains the steps his city took to make effective use of data”, Harvard Kennedy School Ash Center, May 2016.

Nutter found that, as in many municipalities, there was a lack of coordination between departments.(7) In addition, Nutter found that the recession highlighted the need for greater collaboration.(8) Nutter also observed how data was being used in other cities, such as New York, and recognized that although the City possessed large amounts of data, they were not being used to maximum advantage.(9)

The current European policy goals are reflected in the EU 2020 Strategy(10) without mentioning smart cities, which were not a main concern when the agenda was prepared in 2014. However, the later Investment Plan for Europe, also called the Juncker Plan, has proved useful in triggering €164bn in its first 18 months for smart cities development, “but it is not addressing regional inequality” said Markku Markkula, the President of the European Committee of the Regions.(11) The EU is trying to better coordinate EU regulations and national regulations, and to improve knowledge sharing regarding smart cities through the urban agenda for the EU.(12) In the course of Horizon 2020, the EU Framework Programme for Research and Innovation, the European ‘Sharing cities’ initiative is monitoring the deployment of new services in three cities (London, Milan, and Lisbon) and three more are joining (Bordeaux, Warsaw, and Burgas); those innovations include, for example, integrated smart lighting with other smart service infrastructures (eV charge, smart parking, traffic sensing, flow data, Wi-Fi etc.), interconnected initiatives supporting the shift to low carbon shared mobility solutions (specifically eV Car-Sharing, e-Bikes, eV Charging, Smart Parking, e-Logistics), Integrated Energy Management System, and Urban Sharing Platform (USP) – which manages data from a wide range of sources including sensors as well as traditional statistics. These initiatives build on common principles and open technologies and standards. In turn, these new virtual services may eventually disseminate idiosyncratic digital services, a dramatic move forward which raises its own concerns regarding legal safeguards.

As an EU Member State, France has prepared several instruments which frame its policy regarding smart cities with successive national plans for digital development, and a dedicated Ministry on digitization since 2014. It has

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(7) *Ibid.*, p. 6.

(8) *Ibid.*

(9) S. GOLDSMITH, *op. cit.*, p. 6.

(10) European Council, June 2014, EUCO 79/14.

(11) Pan European Network, “Smart cities, Go Green, Go Smart”, May 2017, p. 3.

(12) EU Comm., “Urban Agenda for the EU”, the urban themes (such as air quality, circular economy, climate adaptation, digital transition, innovative and responsible public procurement, urban mobility, and urban poverty) were set forth in the Pact of Amsterdam, ratified by urban-policy ministers from the EU member countries in May 2016. Recommendations for innovation in public procurement were elaborated.

launched, since 2016, a network of public and private actors for the sustainable city ('Vivapolis') who brainstorm about the modernization of traditional utilities and creation of new activities within the ambit of the sustainable policy goal. Several grants and labels have been designed not only at the national level but also at the European and international levels to boost local endeavors (French Tech, Eurocities Network, UNESCO network of Creative cities). However, smart cities projects are more 'bottom-up' in nature, usually driven by proactive municipalities with a smart city champion. According to TACTIS (2015 study), 60% of these municipalities have elaborated dedicated strategies, even updated ones based on lessons learned. From a legal perspective, French towns are keen to take on such proactive approaches as they are responsible for providing local public services for citizens, at least the traditional ones such as utilities and beyond: water, sanitation, roads, cemeteries, firefighting, public transportation, public schools, civil registry, local public archives, socio and health services, etc. Presently, there is no legal framework regarding new services, including virtual services, to be deployed by smart cities. According to the French Law (Code on Local Governments)(13) and administrative case law, beyond the mandatory local public services, it is up to the competent public authority, the State or a local authority, to assess whether a collective need justifies the institution or maintenance of a public service. In addition, a local government may entrust the management of a local public service to a private company. In this case, EU competition law defines the legal framework applicable to both the public authority and the private companies in charge of the management of local public services as regards the objectives they can pursue, such as the method of management and the conditions of their financing.

While some private consulting firms advocate for a reduced public involvement with a 'Government as versatile facilitator',(14) it is worth remembering that smart cities projects pertain to urban planning decisions, or at least affect that policy arena. While the city of Philadelphia was taking its initial steps in creating a smart city, it was also updating the comprehensive plan of the City, which identifies its present and planned physical development. Philadelphia's home rule charter requires the City Planning Commission to "prepare and adopt, from time to time modify, and have custody of a comprehensive plan of the City showing its present and planned physical development. The comprehensive plan shall [...] provide for the improvement of the City and its

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(13) *Code général des collectivités territoriales.*

(14) Quote from the PwC NL Website: "Within this approach, municipal authorities transform from individual entities to a whole network, and will no longer be the sole service provider – they will act as a versatile facilitator or supply chain manager for the various involved parties. Bonds can be reinforced using new technologies and 'open' and 'big' data, which will help to improve measurability and predictability. These parties can then work together to resolve social problems and generate value for the public".

future growth and development and afford adequate facilities for the housing, transportation, distribution, health and welfare of its population”.(15) The plan “envisions a city with an expanded transportation network that better connects home and workplace; ensures convenient access to sources of healthy food; supports the productive reuse of vacant land; provides modern municipal facilities that serve as the anchors of strong neighborhoods”.(16) In France as well, Urban Law is the primary concerned legal field when it comes to carrying out smart cities projects, including physical infrastructure.

### 2.1. First steps – Operational changes

The NLC report notes that while the technologies for a smart city are essential for smart development, technology alone is insufficient. A key challenge lies in establishing the organizational components and administrative structure to effectively utilize the technology.(17) Thus, appropriate policies and administrative departments capable of implementing them are needed to facilitate smart city development. In 2012, subsequent to the creation of the Office of Innovation Technology (OIT), Philadelphia established the Mayor’s Office of New Urban Mechanics (MONUM), which was modeled after a similar effort by the city of Boston. MONUM’s mission was to “develop and promote innovative and entrepreneurial approaches to and processes for solving complex civic problems.(18) In a press release, Mayor Nutter stated that MONUM “will have the flexibility to experiment, the ability to re-invent public-private partnerships and the strategic vision to create real change for Philadelphia. I am excited to establish the Office of New Urban Mechanics as a civic innovation tool for urban transformation”.(19) The creation of OIT and MONUM thus offers tools for greater collaboration within the City’s departments, as well as with the private sector in identifying innovative solutions to the City’s needs.

Most of the time, the initiative for creating or upgrading existing city/neighbor (‘smarter cities’) depends on public authorities (Nice or Montpellier in the South of France launched such projects fully seven years ago, while other municipalities have more recently joined the movement: Mulhouse, Chartres, Roubaix),

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(15) “Philadelphia Home Rule Charter”, Section 4-600.

(16) Cover letter from Mayor Michael A. Nutter accompanying the Citywide Vision document for Philadelphia 2035, dated 2 June 2011.

(17) *Ibid.*, 16, 11.

(18) Executive Order No. 5-12 at Section 2. The Order, at Section 2, further states the MONUM “shall work to encourage the region’s entrepreneurial, startup, and business incubator communities to solve civic problems and shall promote those solutions in partnership with the Office of Innovation & Technology, the Office of the Deputy Mayor for Planning and Economic Development, and other City departments and offices as well as outside partners”.

(19) “Philadelphia Mayor Formally Creates Office of New Urban Mechanics”, Govtech.com, 11 December 2012.

although some of them may try to harmonize and scale up spontaneous private or citizens' initiatives (Grenoble, Toulouse, Paris or Rennes in Brittany).(20)

Development of smart cities projects may vary according to the size of the city. Big cities such as Paris, or State capitals in the U.S., have sufficient leverage for conducting their smart initiatives on their own, while small towns tend to combine forces. In France, where the decentralization process has reached an incredible level with more than 36,000 cities and villages for a population of only 67 million, administrative superstructures are needed. Dedicated public bodies (EPCI(21)) pooling traditional services such as water distribution, public transportation, or waste management, are already in place. A 2017 Report on smart cities prepared by a Member of Parliament(22) recommends using this administrative layer as the bedrock of the smart cities, to equip each EPCI with new competences on data, and economics, enabling it to support territorial innovations, promote common sharing among communities, and finally, increase training so that all the decisions surrounding the digitization of local public services can be made in an informed way. It is fair to say that the smart cities effort may induce a re-centralization process for the smallest towns, but it can also accompany rebirth of rural territories.(23) In mid-size towns, a specific status of 'metropolis' allows them to centralize services for the whole agglomeration including suburban cities(24) as in Toulouse.(25)

## 2.2. Building on public needs

Smart cities create new demands from citizens, asking for new local services that should be driven by public policies. The NLC report also suggests that smart city initiatives should focus on the desired outcomes before seeking solutions from the marketplace. Cities should "find out what their residents and local businesses want to see happen, and turn those desires into clearly defined objectives before proceeding with smart initiatives".(26)

(20) Ministère de l'Environnement, de l'Énergie et de la Mer – Commissariat général au développement durable, "Villes intelligentes, smart, agiles : Enjeux et stratégies de collectivités françaises", 2016, p. 4.

(21) The acronym EPCI stands for "Établissement public de coopération intercommunale", which could translate as Public body for intercities cooperation.

(22) R.M.L. BÉLOT, *Sur les smart cities, De la smart city au territoire d'intelligence(s) – l'avenir de la smart city*, 19 April 2017.

(23) Groupe Caisse des Dépôts, *Guide Smart city vs. Stupid village?*, September 2016 (in French).

(24) Enacted on 7 August 2015, the law on the New Territorial Organization of the Republic (NOTRe) entrusts new powers to the regions and clearly redefines the competences attributed to each territorial collectivity. This is the third part of the reform of the territories, after the law of modernization of territorial public action and affirmation of metropolises and the law on the delimitation of regions.

(25) Project "Smart city 2015 – 2020. Toulouse open métropole!".

(26) *Ibid.*, p. 25.

Initial public initiative leads to questions pertaining to governance. Not only so these new activities shine a light on the public actors taking responsibility for the new public services to be deployed – the activities also raise the bar regarding civil society’s expectations. New tools based on Internet technology will also offer new monitoring powers to citizens who want to take direct part. In Paris, a first strategy on a smart and sustainable city was published in 2015, but since the deployment of new services and connected goods, the Committee of Partners (the city’s representatives of business, and socio-economic actors) initially divided in working groups covering topics such as energetic transition, mobility, urban logistic, waste, etc., had to reposition their role upfront in the design of the projects and their objectives.(27) The Committee of Partners experimented with a co-construction movement relying on a bottom-up approach. How this movement could be reflected in the definition of the needs prior to a bidding process raises new questions.

### 2.3. Smart cities require combined operation of traditional services and e-services

The public will that supports innovation in cities explains why this movement usually begins by focusing on new governance tools, bringing direct participation and legitimacy. These soft public services cost far less than physical infrastructure with an immediate and effective impact on citizens’ life. For each such set of virtual services, outsourcing may not be needed, so long as cities have access to the required IT technical skills. Like many U.S. cities, Philadelphia seeks to “manage urban growth during an era of tight budgets and often conflicting priorities”.(28) In addition to its high urban density, the City also has a significant poverty rate of more than 25%.(29) Issued in June 2011, Citywide Vision for Philadelphia2035 is the City’s current development plan for the next 25 years. Among the initial projects undertaken by MONUM’s was a pilot program known as Textizen. Textizen is a tool for gathering real time feedback using cell phone text messaging.(30) The City sought a method to address: (1) the difficulty for prospective participants to attend public meetings at the scheduled time and location, and (2) the desire of some citizens to provide feedback anonymously.(31) In addition, the City also sought to maximize engagement of low-income populations, which comprise approximately 37% of households in Philadelphia.(32) The creation of Textizen by

(27) *Rapport Villes intelligentes*, 2016, p. 33.

(28) *Rapport Villes intelligentes*, *op. cit.*, 27.

(29) *Trends in Smart City Development: Case Studies and Recommendations*, p.22.

(30) *Textizen Philadelphia*, on *Participedia – Strengthen democracy through shared knowledge*, 2016.

(31) *Ibid.*, p. 30.

(32) *Ibid.*

MONUM highlights the benefits of sharing ideas between smart cities, given that MONUM was modeled after an effort in Boston. Textizen also represented a successful test of a fundamental element of smart cities – the use of technology to connect directly with citizens in developing policy.

Virtual service may be an autonomous activity (ex.: restricted opening of public facilities' doors) requiring its specific rules and monitoring, but most of the time these new services are (or will be) interconnected through platforms offering a panel of services. Such tools greatly improve governance and transparency in local governments, offering tangible successful results for the citizens. One of Philadelphia's earliest and most successful smart city initiatives, Philly311, is essentially a non-emergency contact program, providing the public a direct way to request services, submit a complaint, and provide feedback to the City. Philly311 was modeled after a program in Baltimore where that city sought to reduce the number of non-emergency calls being made to 911 emergency call centers. Similarly, Philadelphia sought to reduce the call volume to 911 by offering citizens an alternative for non-urgent matters. Philly311 offers various ways to contact the City: telephone, mobile application, web application, email, and social media. By offering citizens distinct options for urgent (911) and non-urgent (311) requests, the City has been able to fulfill a key objective of allowing agencies and departments to focus on their core mission and manage their workload efficiently.<sup>(33)</sup> Philly311 has also provided additional data to City officials to assist in their decision making and it is used to monitor and track operational performance.<sup>(34)</sup> The data obtained from the 311 system identifies 'hot spots' around the city that need attention. For example, the 311 data have changed the way the City prioritizes street light replacement. Clusters of call from a particular area indicate that an issue, such as replacing a street light, needs to be addressed.<sup>(35)</sup>

Another important benefit of Philly311 is the promotion of transparency and integrity within the City government processes. City officials discussed with Nam and Pardo that, prior to Philly311, many citizens did not know where to request a service. Some sought out a member of the City council as a representative of their community. Because of a lack of understanding of the process, many citizens believed they needed to know someone within government to obtain a service. Philly311 has shed a light on how the process works and citizens have a better understanding of their government, thereby reducing the need to seek 'favors' from someone within government. Thus, Philly311 became an anticorruption strategy, as since its launch, citizens can see more

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(33) T.A. PARDO and T. NAM, "Transforming City Government: A Case Study of Philly 311", Albany, Center for Technology in Government, 2012.

(34) *Ibid.*, p. 33.

(35) *Ibid.*

clearly how their government works, reducing the need to seek to influence city officials to obtain services.(36)

Traditional or physical networks may also evolve. In energy distribution, the development of smart grids is a key element for smart cities. Digital technologies make it possible to better control the electricity consumption of office buildings, dwellings, or public lighting, which may represent up to 40% of the electrical costs for a town. In France, the IssyGrid project was initiated in 2011, created by the city of Issy-les-Moulineaux (located in the south-west suburbs of Paris). This laboratory initiative intended to build a whole new business neighborhood while achieving savings and reducing the carbon footprint by optimizing consumption and pooling resources between offices, homes and businesses.(37) It relies on the production of renewable energies (photovoltaic panels, cogeneration, micro-wind, etc.), the energy consumption of dwellings, offices and shops, and the storage of the electricity produced. In 2016, IssyGrid became operational with three photovoltaic production facilities, one of which is connected to IssyGrid via a network, an intelligent public distribution station that can be remotely controlled from the ERDF regional management agency and that optimizes exchanges between consumption, production and storage, two energy storage systems, a system for forecasting photovoltaic energy, fourteen interconnected information systems, and an energy monitoring dashboard able to provide the data in open data format.

Traditional services will also be linked to virtual services (e.g., a garbage collection service will be operated when an electronic sensor is indicating that the trash container is full). What is genuinely new in Smart cities is the transversality(38) of services: infrastructure providing for utilities, for example, can also deliver immaterial or virtual services. The NLC report, mentioned above, adds that: “a smart city is a city that has developed some technological infrastructure that enables it to collect, aggregate, and analyze real-time data and has made a concerted effort to use that data to improve the lives of its residents”,(39) by performing analytics, for example, and developing software applications. In France, the water distribution is so far one of the more connected network with 20% of small cities with remote systems for monitoring individual consumption and station control,(40) followed by waste management with, for example, connected goods such as weighting trash cans

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(36) *Ibid.*

(37) Press release, “Premier *smart grid* de quartier opérationnel en France”, 26 September 2013.

(38) F. RICHARD, “Des solutions au service de la ville intelligente”, Summary of work, 16 November 2017.

(39) *Textizen Philadelphia*, *op. cit.*

(40) *CDC Guide on Smart city vs. Stupid Village*, 2016, p. 16.

which allows for tariff incentive or geolocated garbage trucks to optimize the collections. Sound public lighting is also popular as a source of energy savings with, for example, connected furniture and energy recovery pavers on the roads. The Internet of Things (IoT) opens up a vast range of services that have only just begun to be explored.(41)

As noted by the 2017 CNIL Report on smart cities,(42) the arrival of major digital players in urban services (Sidewalk City Lab, Waze Connected Citizen of Alphabet / Google, Uber or Facebook) raises the question of the real rewards required from individuals and public actors for services presented as free. Furthermore, creativity on platforms, and artificial intelligence development also multiply services among citizens such as goods' rentals (apartments, gardens, cars, tools, manpower etc.). These trends illustrate one major characteristic of the smart city concept: collective services can also be customized to each individual's needs.

### ***3. Smart Cities Need Innovative Procurement Techniques***

Traditional procurement methods do not fit with the requirements of these kind of projects: off-the-shelf answers are out of purpose, since with all their incremental and experimental needs, smart cities call for smart design and engineering while large competition requires standardization of the technical elements. Indeed, the design of the procurement procedure itself may have a strong implication on innovation. As was noted in the OECD Report on Public Procurement for innovation:(43) “The use of public procurement for innovation is defined as any kind of public procurement practice (pre-commercial or commercial) that is intended to stimulate innovation through research and development and the market uptake of innovative products and services”. For its part, the EU 2020 plan has also promoted demand-side innovation policies to support public procurement beside other action tools (legislation increasing consumer confidence in innovative products, safety regulations, standards).(44) However, designing standards in the context of smart cities opens a new issue, recently addressed by the World Standards day.(45)

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(41) World Bank Group, “Internet of Things: The New Government-to-Business Platform”, 2017.

(42) Commission nationale de l'informatique et des libertés (CNIL), “La plateforme d'une ville. Les données personnelles au cœur de la fabrique de la *smart city*”.

(43) OECD, *Report on Public Procurement for innovation – Good practices and strategies*, 2017, p. 18.

(44) “Demand-side policies for innovation”, [https://ec.europa.eu/growth/industry/innovation/policy/demand-side-policies\\_en](https://ec.europa.eu/growth/industry/innovation/policy/demand-side-policies_en).

(45) 2017 World Standards Day, “Standards make cities smarter”. See also the EU General Directorate GROW Conference, “Cities set standards to become smarter and more sustainable”, 19 October 2017.

### 3.1. Needs assessments

Considering the variety of solutions and services, it is crucial to evaluate the needs of the future city or neighborhood. A pre-assessment of all the costs, externalities and expected gains, coupled with a financial analysis is a pre-requisite, recommended by the B elot Report(46) in France. Such analysis shall ensure that digital infrastructure will be both flexible and evolve through time. However at least two layers of public contracts may be necessary to conduct a smart cities project. If the first set covers the service contracts that will help the City task force to conceive its future smart city policy, relying on the expertise of consulting firms, the second set will be cover creating and operating new infrastructure and/or services. In July 2016, the Office of Innovation and Technology (OIT) in Philadelphia issued a Request for Ideas (RFI) on how the city could utilize assets for new technological purposes to improve operations while generating revenue at the same time.(47) The RFI indicated that the information obtained would be used by the City as a basis for further discussion and the development of an RFP. Among the topics listed in the RFI were: meter reading, street lighting controls, gunshot detection, transportation analytics, infrastructure monitoring, public safety surveillance, free, high-speed public Wi-Fi, and sensor technology.

### 3.2. Procurement design

Regarding the design of its procurement processes, smart cities require a sequential approach through progressive steps combined with a comprehensive framework. After reviewing over 100 RFI responses, Philadelphia determined that to best support the Internet of Things (IoT) solutions, it first needed a strategic plan to guide the City through a process of identifying how to make IoT possible in Philadelphia in a way that reflects the needs of its citizens and business communities. Subsequently, on 28 April 2017, OIT issued a Request for Proposals (RFP) seeking a vendor to develop a comprehensive and strategic smart city roadmap.(48) The RFP stated that:

“The City desires to enhance its ability to deliver quality services for the residents and businesses of Philadelphia through the development and use of secure interconnected information, communication, and sensor technology

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(46) L. B ELOT, *Rapport au premier ministre sur l’avenir des smart cities – De la smart city au territoire d’intelligence(s) – l’avenir de la smart city*, 19 April 2017.

(47) See “Request for Ideas: Using Technology to Create a Smart City”, City of Philadelphia Office of Innovation and Technology, 12 July 2016.

(48) See “Request For Proposals: Consulting Services to Develop a Smart City Roadmap For The City of Philadelphia”, City of Philadelphia Office of Innovation and Technology, 28 April 2017.

and Internet of Things (IoT) solutions. This roadmap will guide the City in realizing its vision to become a Smart City”.(49)

Therefore, after a number of pilot projects and focused smart city initiatives, Philadelphia is poised to pursue a more comprehensive approach to becoming a smart city. An RFP issued by the City in April 2017, seeking a vendor to develop a comprehensive and strategic Smart City roadmap, while not providing much detail, indicates a recognition of the issues of privacy and cybersecurity. The RFP states that the City seeks a vendor familiar with best practices and regulations around IoT security and privacy.(50) In addition, the RFP identifies (as a ‘Tangible Work Product’) a security framework to ensure safe development of IoT solutions, which will provide continued assessment of risk moving forward and create transparent policies around privacy and protection of sensitive information and protected data.(51)

In France, while numerous and innovative projects are mushrooming, difficulties remain with the current set of procurement procedures, which are not customized for the special needs of smart cities projects. In particular, local actors are complaining about the remaining complexity, lack of fluidity and issues faced by small businesses and start-ups to participate in public biddings. Negotiations or dialogue procedures, such as the competitive dialogue or the competitive negotiations, could be more accurate than the call for tenders, in this context. Prior to the bidding process, and through a pre-commercial analysis, the procurement team should explore the market and available solutions. This could also justify the call for variants and/or for contracts divided in tranches, allowing the public entity to sequence the project in a risk-averse approach.(52)

Through the implementation of the 2014 EU Directives, local governments have been tempted to experiment using Innovative Partnerships (Dir. 2014/24, Art. 31). However, the initial feedback is not positive,(53) specifically in the ambit of smart cities projects: the procedure tends to be too narrowly defined for a specific product or service while smart cities are often looking for comprehensive, collaborative, and exploratory services such as the ones designed after ‘hackathons’.(54) Indeed, the use of an innovative partnership,

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(49) *Ibid.*, p. 38, 1.

(50) *Ibid.*, p. 38, 2.

(51) See “Request For Proposals”, *op. cit.*, p. 38, 7.

(52) This last solution is advised by the *Député* (Representant) L. BÉLOT in his 2017 Report, *Rapport au premier ministre sur l’avenir des smart cities – De la smart city au territoire d’intelligence(s) – l’avenir de la smart city*, *op. cit.*, p. 74.

(53) No one single contract after two years: see P.A. MOGENIER, *Deux ans après son adoption, retour sur le Partenariat d’innovation*, 1 March 2016.

(54) *Report of the ministère de l’Environnement*, 2016, p. 47.

as an R&D tool, is only allowed(55) when there is no other solution available on the market; this constraint can reduce potential use of this new contract. While for smart cities, local buyers may look for existing services, but they are in need of an ad-hoc architecture. Moreover, this innovative partnership may be more suitable for manufacturing or developing a single product or service when the smart city initiative calls for a ‘bouquet’ of services. Fearful of using the wrong procedure that may lead to a criminal conviction of favoritism (unfair advantage), French procurement staff and local representatives either prefer to choose the traditional methods of procurement which are not tailored for such innovative solutions, or they opt for a genuine ‘experiment’ outside the procurement rules, such as the Issy Grid project.(56) In the context of the Internet of Things, few initiatives have been launched(57) addressing interoperability, and most are coming from the private sector. However, experimentations are not viable schemes for companies since they are looking for perennial activities that could be standardized and reproduced.(58) Precise technical specifications may not be the best adapted to an evolving environment: functional requirements with performance criteria would better reflect the potential services reconfiguration that may take place later on.

Thus, smart cities project can also trigger procurement reform. The FastFWD program in Philadelphia promoted additional procurement innovation for the City, which has worked with Citymart, an organization that focuses on problem-based procurement methods and practices. Citymart trains city officials to use problem-solving and problem-based procurement methods and has worked with the City’s Office of Innovation Management to reach out to city departments, train workers on how to rethink the way they approach problems.(59) This training includes guidance on preparing a clearly defined solicitation (tender) to maximize competition.(60)

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(55) Decree 25 mars 2016 on public procurement contracts, Art. 93: “The purpose of the innovation partnership is to research and develop innovative products, services or works within the meaning of 2° of II of Article 25 as well as the acquisition of products, services or works resulting therefrom need that can not be satisfied by the acquisition of products, services or works already available on the market. The buyer may decide to set up an innovation partnership with one or more economic operators who perform the services separately under individual contracts. This decision is indicated in the contract notice or in another document of the consultation”.

(56) L. BELOT Report, *Rapport au premier ministre sur l’avenir des smart cities – De la smart city au territoire d’intelligence(s) – L’avenir de la smart city*, op. cit., pp. 67-78.

(57) Listed by the World Bank Report on IoT, 2017, RAMI 4.0 (Led by the German Federal Ministries of Economic Affairs and Energy and of Education and Research, and with stakeholders); IIC (Industrial IOT Consortium); OFC (Open Connectivity Foundation) and Project Haystack.

(58) L. BELOT Report, *Rapport au premier ministre sur l’avenir des smart cities – De la smart city au territoire d’intelligence(s) – L’avenir de la smart city*, op. cit., pp. 56, 76.

(59) R.P. SHEPELAVY, *Solving... Not Buying*, 18 March 2016.

(60) *Ibid.*, p. 60.

In France, and in Europe, one may think about introducing procedures for unsolicited proposals, at least in the context of smart cities and digital services, as local governments are particularly solicited by start-ups and innovative companies looking for new markets and sources of data. Contracts can be a way of developing new activities and services. In this context, Germany considers reforms such as the relaxation of government procurement requirements.(61)

Finally, positioning the sustainability goal at the core of the smart cities initiative must have a direct impact on the procurement policy. Therefore, procurement criteria must look for energy production from renewable sources, energy efficiency and waste management. In this area, the recent procurement concept of life cycle costing analysis may be the most persuasive tool. IssyGrid, presented above, makes it possible to smooth peaks of consumption and to ensure the general balance of the network while reducing the carbon footprint of the neighborhood.

#### ***4. Going Beyond Public Procurement Contracts: Smart Public-Private Collaboration***

Building advanced broadband technologies networks requires heavy infrastructure investments for the moment often financed by public authorities. In France, the Government is conducting a national plan for the equipment of all remote areas, a plan that will provide benefits to smart cities local projects as well. In other contexts, cities may have to find their own solutions. The British city of Bristol, and Mississauga in Canada “are trying to overcome such challenges by constructing their own infrastructure and offering them to businesses for use”.(62) In the U.S., national or federal initiatives in R&D public procurement trigger change in IT and subsequent development at the local level. However, given the magnitude of the smart cities’ projects, their necessary exploratory dimension, the potential arising of technical or legal issues, the contractual arrangement should channel a true collaboration between public and private partners. Since public services cannot fulfill all needs, private and public services, managed by public and private bodies, must, more than ever, be complementary.

After the great fire of 1666, which destroyed 1/6 of its houses, the city of London was reorganized around ‘squares’, or ‘garden squares’, whose pieces of land were distributed for free by the King to constructors who invested in building new houses to be rented by tenants. This first modern town planning

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(61) Federal Government of Germany, *Digitale Agenda 2014-2017*, August 2014.

(62) World Bank Report on IoT, 2017, *op. cit.*, 41, 14.

was indeed based on what one would call today Public-Private Partnerships (PPP). However, the partnership can range from a simple collaboration to a strong legal relation built on a contract. Based on several topic examples around the world, a 2017 World Bank report on the Internet of Things recommends a tripartite collaboration including academia, through ‘public-private-academic partnerships and platforms’. However, the PPP referenced in the World Bank report should not be mistaken with its contractual version: in this report it is only a way to underline the collaboration that has to be put in place. A ‘coordinator’ office may reinforce the missions conducted through these ‘PPAP’ which “cover both infrastructure and non-technical aspects, including policy assessments and implications, public perception and awareness, data stewardship, financial models, business value propositions, competency and skill requirements”.

In the Netherlands, the Dutch experience is enlightening in that it leaves a large part to innovation, not only technological but also organizational and legal.<sup>(63)</sup> The predominant approach is that of consultation, on a given territory and involving different stakeholders. There is a range of legal support: an initiative directly piloted by municipalities, experimentation in the form of public-private partnerships between a public entity and a company, sometimes without competition, or using a concession contract in the transport sector. Indeed, Dutch authorities have transposed a conventional approach between several private and public parties which had been developed in the circular economy to create green deals. After recommending a ‘safe standardized digital infrastructure’, the national strategy for smart cities<sup>(64)</sup> points to the necessity of relying on ‘Public-private partnership with room to experiment’, calling for the creation of a new business model. Social cost-benefit analysis (SCBA) and Overview of Effects of Infrastructure (OEI) already used by the Dutch Government for several public projects shall be the reference tools for accessing costs, while exploring innovative procurement methods could be backed by a fund established to inspire confidence in the local governments.<sup>(65)</sup>

The French legal system offers a range of contractual solutions that may be relevant for smart cities projects, with some caveats. The town may pick a type of global public procurement contract, the solution recently retained by the town of Dijon and a regrouping of 24 municipalities, with the signature of a 12-year contract. The consortium several French companies such

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(63) See The Smart City Embassy Web site, founded by Amsterdam Smart City, Connekt and the Ministry of Infrastructure and Water.

(64) With a bottom-up approach, a large number of Dutch cities, companies and scientists have contributed to the preparation of the “National Smart City Strategy”, presented in January 2017 to Prime Minister Mark Rutte, who had requested a consolidated Smart City Vision.

(65) “National Smart City Strategy”, aforesaid, 65, pp. 48-49.

as Bouygues, Capgemini, Citelum and Suez, will be in charge of the design, construction, operation and maintenance of connected urban centers piloting several public services through connected goods such as (sensors on public vehicles, lighting, traffic lights, access terminals in downtown, video-protection or, even, security and BWM of the buildings of the communities), under the monitoring of a unique control center for a total cost of 105 million euros.<sup>(66)</sup> Half of these costs will be covered by the City of Dijon and Dijon metropolis – the city is also betting on the savings that may result from better management of the public lighting service. They also expect that the data collected, some of which should be made available to citizens free of charge, may be partly monetized.

French local governments are also familiar with certain PPP arrangements, such as ‘service concession contracts’ where the initial investment is financed by the private party who will be operating the infrastructure and its related (public) service for a long duration, bearing the demand risks, and paid by users’ fees. France has a long history with ‘concessions’ as being long term contracts entered into by a public body (such as a city) and a company in order to build an infrastructure or a network and to operate the (public/ utilities) service attached to it (ex: water sanitation in a city, electrical power or a gymnasium for sports). Although these contracts may encompass large projects, they were usually specialized in providing one type of service (ex: water access, electricity, or sports facilities) which could be referred to as ‘mono-service’. What is new in smart cities is that they require a cluster of infrastructures built and operated simultaneously for delivering ‘combined services’. Opportunely, the French Administrative Supreme Court, the *Conseil d’État*, held in 2016<sup>(67)</sup> that separate services could be bundled under one contract, with two caveats: the scope should not be grossly excessive, and the contract cannot bring together services that otherwise would be clearly unrelated to each other.

French local governments may also rely on the ‘*Marché de partenariat*’ which is a sort of B.O.T. (‘Build-Operate-Transfer’), although a more recent form of PPP in the French legal system, where the public entity is renting the facility or service delivered by the private investor, owner of the infrastructure until the end of this long-term contract. However, it is fair to say that if French local governments are used to working with companies for the delivery of traditional services, they are less prone to deal with new digital actors. If

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(66) G. GAMBERINI, “*Smart City* : Dijon Métropole se positionne en pionnière”, *La Tribune*, 7 September 2017; F. MAILLET, “Comment Dijon veut devenir la première *smart city* française”, *Le Monde*, 13 September 2017.

(67) CE, 21 September 2016, req. No. 399656.

not yet well developed, creating an ad-hoc company may also be considered, with public entities as shareholders coupled with private investors.

In France, local authorities and their groupings may also create local public development companies (SPLA), of which they hold the entire capital (Art. L. 327-1 of the Urban Planning Code), authorized to carry out any development operation within the meaning of the Code (Art. L. 300-1) exclusively on behalf of their shareholders and on their territory. These SPLAs are under control of the local authorities that create them. The latter are therefore not obliged to apply the competition rules relating, as the case may be, to concession contracts or procurement contracts (in-house) when they use these SPLAs. As regards the contracts entered into by these SPLAs for their purchases, it should be verified in each case whether the company concerned should be regarded as a buyer within the meaning of the provisions of Article 9 of the Ordinance of 23 July 2015 on public procurement.

French Urban Law has, for many years, developed a special development concession (*concession d'aménagement*) as “an umbrella contract granting the management of a whole town project to a private investor. The development concession is a public contract by which a public authority entrusts to a developer the carrying out of development operations, that is to say operations whose object is to implement an urban project, a local housing policy, organize the maintenance, extension or reception of economic activities, promote the development of leisure and tourism, build public facilities or premises research or higher education, to fight against [health hazards] and [dangerous] habitat, to allow urban renewal, to safeguard or enhance built or undeveloped heritage and natural areas” (Art. 300-1 of the urban planning Code). The development concession may provide for the concessionaire to obtain the property necessary for the operation by expropriation or to acquire it by pre-emption. The remuneration of the concessionaire is ensured by the “sale, lease or concession of real estate located within the concession perimeter” (Art. L. 300-4). The public authority may also participate in the financing of the operation through land contributions or financial contributions. For the adjudication phase, a mandatory advertising process must be organized. Based on the allocation of the economic risk, the agreement can be either classified as a procurement contract governed by the procurement rules or as a concession contract under the French Ordonnance of 29 January 2016 on Concessions transposing the 2014/23 European Directive on Concessions contracts. Although interesting for the physical infrastructures dimension, the urban development concession might not be the most suitable for smart cities initiatives which encompass multiple dimensions, including information technology, several services, and other virtual ingredients.

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### ***5. Contracts for Smart Cities Need to Find Smart Financing***

Investors in smart cities need stability, durability and profitability for their money. Risk allocation in a highly versatile environment is one of the many challenges the legal framework for smart cities should address. Thus, public contracts need to provide for a flexible and secure environment. These goals mandate long term arrangements balancing real estate rights, use of eminent/public domain for infrastructure, as well as rights for creating and developing new services that will provide direct sources of income for the entity in charge. The economic context of smart cities' contracts resonates with specific issues. As noted by J. Edler and L. Georghiou,(68) "the more radical an innovation, the higher the entry and switching costs. This relates to transaction and learning costs, to adoption of complementary equipment and to lock in and path dependency effects. Those problems of high entry costs are especially virulent in areas in which network effects occur".

Initial public financing may be the optimal solution for stimulating innovation. The U.S. federal government has made grant funds available for cities to pursue smart city projects. In addition, a number of other sources have provided smart city grant funding, often via challenges or competitions between cities to encourage the development of new ideas applicable to smart cities. In 2013, Philadelphia was awarded a \$1 million grant by the Bloomberg Philanthropies Mayors Challenge to implement its winning idea, FastFWD, which sought to engage entrepreneurs in offering solutions to the City's public problems while also promoting reform of the procurement system to encourage innovation.(69) Under FastFWD, the City gathered data across departments on a problem and then described it in a manner suited to creative solutions.

Under FastFWD in Philadelphia, an initial effort was designed to attract new companies/small businesses, with innovative ideas, along with private sources of funding. Working with new businesses and relying on private sources of funding is part of the promise and challenge of the program. Once a need was identified, a multi-phase process followed, with an initial request for solutions to the identified need.(70) The top proposals were selected to enter into a business accelerator program that refined those ideas through business development strategies, mentorship, and collaboration with city employees.(71)

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(68) J. EDLER and L. GEORGHIOU, "Public procurement and innovation – Resurrecting the demand side", *ScienceDirect – Research Policy*, 2007, pp. 949-963, esp. p. 956.

(69) "Procuring Innovation – Philadelphia's Bold New Model", Harvard Kennedy School Ash Center, Mayors Challenge Research Team, 26 February 2014.

(70) See the program "Fast Forward – Scaling Tech Nonprofits To Create Positive Social Impact".

(71) *Ibid.*, p. 71.

The city then selected two or three pilot projects to implement, evaluate, and refine.<sup>(72)</sup> After the accelerator process pilot projects and/or contracts could be awarded.

More than 70% of smart cities in France are publicly financed,<sup>(73)</sup> either through local, national or European funds. On this matter, European institutions have decided to finance several digital initiatives through various schemes for both sectoral and global projects: “Connecting Europe Facilities for Transport”, the “LIFE Program”, including Financial Instrument for the Environment and Horizon 2020 with smart cities and communities’ program. The European Fund for Strategic Investments and the ERDF can also support smart cities projects. Thus, the project design at the local level might depend on external financing, and may be impacted as well by European rules and constraints. At the French level, the *Caisse des Dépôts et Consignations* (CDC), a public financing institution created in 1816, is dedicated to support public projects, through the deployment of telecommunications infrastructures since 2000, and digital services. It is now expanding its activities to become a ‘smart city conceptor’ providing support and financing. However, municipalities tend to rely more on traditional grants, neglecting new financing such as bonds and shares in institutional public private partnerships or special purpose vehicles. Looking for new sources of financing, smart cities could mobilize green bonds. According to the EU’s 2030 climate and energy objectives, there is huge potential for further issuance of sovereign green bonds.

Moreover, given the size of the project (a neighborhood or an entire new city), and the integrating nature of these projects, private financing should also be mobilized. In the French IssyGrid project, mobilization of private funding took another direction: the entire initiative is carried on by a consortium led by Bouygues Immobilier with other private companies. This consortium brings together all the strategic and technical skills of the smart grid: Alstom, Bouygues Énergies et Services, Bouygues Télécom, EDF, ERDF, Microsoft, Schneider Electric, Steria and Total. Among this group some have created a joint-venture (EMBIX) in charge of launching the information system. The ten companies of the consortium have invested 250,000 euros each, without subsidies or public funding. The 2.5 million euros collected finance the purchase of equipment, works and services by third-party companies. Innovative start-ups also bring their expertise in energy management for eco-neighborhood projects, in participatory energy management, in interactive presentation of data (as part of Microsoft’s BizSpark program, which supports digital start-ups), and also in connecting objects that IssyGrid can now host. The town’s Web site

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<sup>(72)</sup> *Ibid.*

<sup>(73)</sup> TACTIS, 2015.

proclaims that the consortium has created an “economic model of the smart grid, based on the deployment of a software layer and sensors dimensioned to the fair, to provide monitoring services, steering and verification of the performance of eco-districts”. However, one may consider that is not a sustainable model: companies are only willing to initially invest in such a pilot project if they can further build on this expertise to obtain future commercial projects. Having demonstrated that they can create smart grids for a controlled cost, they are keen to mobilize these new skills in future bidding opportunities. Who is going to pay from a long-term perspective? If the experimental period benefits from the joint efforts of public and private partners, the smart city concept has to find a sustainable financing model, such as inventing combinations of sources that are not today considered in traditional procurement.

## *6. Special Clauses for Contracts in Smart Cities*

Designing these public contracts will have to take into consideration their two main characteristics: the issues related with data collection, protection and dissemination, and their special need for evolution. Satisfactory performance of such contracts will rely on a carefully crafted design of contractual clauses dealing with the data topic, including IP rights.

### 6.1. Data collection

Indeed, the new services and activities attached to smart cities process rely on massive data production. As mentioned by Jean-Bernard Auby in Chapter 2, Part II in this book,(74) data are the ‘fuel’ of smart cities. Indeed, in a circular approach, these data constitute the baseline for all virtual services and they also are their main products. As such, their identification as private or public data, their collection, diffusion and also potential sale raise several legal issues that will definitely impact public contracts design in the context of smart cities. Thus, the recognition that effective collection and use of data could enhance the effectiveness of Philadelphia departments led to its first steps in becoming a smart city. In 2011, Mayor Nutter issued an executive order establishing the Office of Innovation and Technology (OIT).(75) Philadelphia’s OIT has five components: IT Governance; Innovation; Infrastructure; Communications and Applications.(76) IT Governance seeks to ensure that “information technology is structured and employs a well thought-out, comprehensive strategy across

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(74) J.-B. AUBY, “Public Contracts and Smart Cities”, Chapter 6, in this book.

(75) See Executive Order No. 12-11, “Innovation and Technology”.

(76) See “Office of Innovation and Technology”, Philadelphia; “Trends in Smart City Development: Case Studies and Recommendations”, p. 22.

all City entities that includes risk management, performance, and security”.(77) Innovation focuses on “[d]eveloping and sustaining innovative technology practices within the City through engaging and empowering citizens, improving business processes, working collaboratively and constantly searching for new opportunities”.(78) Infrastructure provides services across multiple technical platforms, systems, and general technical services.(79) Applications is involved with “[b]uilding applications to enhance distribution of information, add convenience and automation to transactions, and increase access to city services”.(80) Each component has sub-units that focus on specific goals of the component.(81) The OIT was established as part of the effort to change the culture of the City’s operations to emphasize innovation.(82) Philly311 has also promoted a data-driven, customer oriented culture across the city government, which is an essential objective of a smart city. To promote its continued success, upgrades were made to the Philly311 system in 2014 to improve request submission and data tracking.(83) The 2016 NLC report notes that the creation of the OIT has enabled city leaders to have a more hands-on approach to ICT initiatives in the city.(84) With the establishment of the OIT, Philadelphia possesses an essential tool to pursue its smart city efforts through greater integration of its infrastructures and services to improve efficiencies.(85)

Data collection being central to any local innovation, effective implementation of data metrics to transform the way the City conducts business requires buy-in from all actors.(86) But data are not only collected, and stored in the cloud under specific contracts, they are also produced by the new interconnected services. Nutter in Philadelphia underscored the importance of openness and transparency in a data-driven smart city to engage both the general public and businesses: “There have been other very positive outcomes – entrepreneurs and the startup community are using some of that data and creating

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(77) See “Innovation and Technology”, *op. cit.*

(78) *Ibid.*, p. 78.

(79) *Ibid.*

(80) *Ibid.*

(81) See, “Innovation and Technology”, *op. cit.*, p. 78.

(82) P. THAKURIAH, N. TILAHUN and M. ZELLNER *Seeing, Cities Through Big Data: Research, Methods and Applications in Urban Informatics*, New York, Springer, 2017, p. 537.

(83) *Philly 311: Innovation that was worth the wait*, GCN, Derek Major, 15 October 2015.

(84) “Trends in Smart City Development: Case Studies and Recommendations”, *op. cit.*, 77, p. 10.

(85) As noted in a white paper of the International Electrotechnical Commission (IEC): “[t]echnology integration helps cities to improve efficiency, enhance their economic potential, reduce costs, open the door to new business and services, and improve the living conditions of its citizens”, International Electrotechnical Commission, “Orchestrating infrastructure for sustainable Smart Cities”, White Paper, p. 4.

(86) Including public employees. As M. Nutter put it about Philadelphia: “We made it clear we were going to start measuring employees on how well they are implementing these systems in the government”.

apps or new businesses”.(87) Then a smart grid can contribute in open data, accommodating contributions from individuals, head offices, operators, charging stations for electric vehicles, energy network operators, businesses, etc., who can, if they wish, make these data accessible in open data, provided that the interoperability (with standards?) of the data collection is made mandatory.

## 6.2. Data release policy

The very nature of the data, and the way their collection and use in the smart city environment is conducted, appear to render many existing laws, regulations and policies on data protection, outdated. The US report, *Open Data Privacy: A risk-benefit, process-oriented approach to sharing and protecting municipal data*, notes that the sharing of smart city data: “comes with inherent risks to individual privacy: released data can reveal information about individuals that would otherwise not be public knowledge. In recent years, open data such as taxi trips, voter registration files, and police records have revealed information that many believe should not be released”.(88) The authors cite a 2014 report of the President’s Council of Advisors on Science and Technology (PCAST), highlighting challenges such as “data mining and other kinds of analytics” and that “one can never know what information may later be extracted from any particular collection of big data”.(89) The authors further note that “while ensuring legal compliance is a natural starting point for crafting data release policies, cities must look beyond legal compliance when crafting data release procedures and strategies”.(90) Finally, the authors state that public support is an essential element of successful open data programs.(91) Engaging the public in the development of policies and practices builds critical support and will drive open data forward.(92) In the French IssyGrid project, a platform makes the neighborhood energy data available to the public free of charge.

(87) “Trends in Smart City Development: Case Studies and Recommendations”, *op. cit.*, p. 85.

(88) B. GREEN, G. CUNNINGHAM, A. EKBLAW, P. KOMINERS, A. LINZER and S. CRAWFORD, *Open Data Privacy: A risk-benefit, process-oriented approach to sharing and protecting municipal data*, Harvard, Berkman Klein Center for Internet and Society, 2017.

(89) Open Data Privacy at Executive Summary, citing: President’s Council of Advisors on Science and Technology, “Big Data and Privacy: A Technological Perspective”, 2014.

(90) Open Data Privacy at Executive Summary. Therefore, to promote the full and effective use of smart city data, the authors make four recommendations: “Conduct risk-benefit analyses to inform the design and implementation of open data programs; Consider privacy at each stage of the data life-cycle: collect, maintain, release, delete; Develop operational structures and processes that codify privacy management widely throughout the City; Emphasize public engagement and public priorities as essential aspects of data management programs”.

(91) “Open Data Privacy”, *op. cit.*, 90, p. 67.

(92) *Ibid.*, 91.

In France, the enactment of the *loi pour la république numérique* (Law on the digital Republic) in 2016, has created a framework for data dissemination which resonates with smart cities. The law creates a concept of ‘public data’, coupled with a new ‘Public service of data’, through datasets, *i.e.* for data with the greatest economic and social impact, available for reuse, so that companies can reuse them for their activities. In addition, Government data, *i.e.*, administrative documents that are of economic, social, health or environmental interest, will be published. Two decrees have been issued which specify the threshold above which a public body must implement this requirement, and which fix the list of licenses for the provision of public data. Another decree requires the publication of the essential data related to contracts allocating public grants. The aforementioned law also creates a concept of ‘data of general interest’, which impacts public contracts, since its Article 17 has amended the rules regarding concession contracts by creating a new obligation for the concessionaire on mandatory data transmission. Through amendments of the Energy Code, these same data will also have to be made available by the entities in charge of electricity service, or of the distribution of natural gas (utilities). From a contractual standpoint, clauses about data transfer to the public entity will have to be drafted, such as the ones sometimes mentioned in French concession (DSP) contracts.

Regulation of private data has also been enacted. Since 1978, with the law *Informatique et libertés* (on IT and Freedom), France has created an independent agency in charge of supervising data collection, the CNIL (*Commission nationale de l’informatique et des libertés*). It has recently underscored the vigilance commanded by the development of Artificial Intelligence in need of massive data collection. Overall, France will have to comply with the new EU’s General Data Protection Regulation (GDPR), which is entering into force on 25 May 2018, reinforcing the former 1995 EU Directive. According to this EU mandatory regulation, all companies, either established in or outside the EU, which are processing personal data of individuals based in the EU, shall comply with the EU data protection rules. On the matter of personal data protection in the ambit of public contracts, the GDPR states, in its recital 78:

“The protection of the rights and freedoms of natural persons with regard to the processing of personal data require that appropriate technical and organizational measures be taken [...] Such measures could consist, *inter alia*, of minimizing the processing of personal data, pseudonymising personal data as soon as possible, transparency with regard to the functions and processing of personal data, enabling the data subject to monitor the data processing, enabling the controller to create and improve security features. When developing, designing, selecting and using applications, services and products

that are based on the processing of personal data or process personal data to fulfill their task, producers of the products, services and applications should be encouraged to take into account the right to data protection when developing and designing such products, services and applications and, with due regard to the state-of-the-art, to make sure that controllers and processors are able to fulfill their data protection obligations. The principles of data protection by design and by default should also be taken into consideration in the context of public tenders”.

According to the new EU Regulation and its implementing rules, while public authorities must designate a Data Protection Officer (DPO), companies are only required to create such a position when collecting personal data is their core activity – if they monitor individuals systematically, for example, or process special categories of personal data – on a large scale. Other companies are encouraged on a voluntary basis to hire a DPO or to rely on DPO consultant.

As things go, public and private data collection and dissemination are now an essential part of any smart cities’ projects. In collaboration with the CNIL, the French IssyGrid has led to the development of a procedure for collecting housing consumption data while respecting the privacy of residents. For example, IssyGrid now receives hour-by-hour consumption data for lighting, heating, water and electrical outlets building by building without knowing the detail per dwelling.

As noted by the 2017 World Bank report on IoT: “Data are central to IoT, but there is inconsistent understanding of data’s value and management” (p. 13). Stating free access to public data and protecting private data is a policy decision taken by the French Government in the debate about the recognized ‘data market’. The free dissemination of public data is not only meant to implement the transparency and governance goals, but it is expected to stimulate the economy, allowing startups and companies to create new services based on the data available. Under such a scheme, only private data, under several constraints, could be considered as goods. First, data-driven experiments can be an economic asset for local governments, triggering cost savings. Second, the potential monetization of these private data is now on the table, since it will clearly affect the profitability of private investments deployed under smart cities project. This could even jeopardize some existing endeavors which have been designed, and balanced with the prospect of fees and revenues produced by the collected data (for example, in the French town of Dijon). If these constraints and limitations on the use of collected data may be acceptable under a public procurement arrangement, because it is based on direct public financing, such limitations will obviously

be one of the main concerns of any private investor before considering to participate in a public-private partnership related to smart cities.

Whatever the solution, in contracts related to smart cities projects, data recovery clauses should be introduced.

### 6.3. Data protection

Advocates for cybersecurity and privacy in smart city development, sometimes referring to the concept of SmartPrivacy,<sup>(93)</sup> note the importance of adopting protection measures early in the process, as they may be more difficult to introduce once the smart city systems have been established:

“Smart city privacy concerns will not be going away soon, but the real risk is that the really smart city arrives before the law catches up to it or we realize how powerful the data collection and processing has become. It would be much smarter and better to develop a set of comprehensive privacy rules to govern the advent of smart cities and to limit municipal collection, use and disclosure of user information before it is too late”.<sup>(94)</sup>

As of this writing, Philadelphia’s approach to privacy and cybersecurity, like its overall smart city effort, remains a work in progress. The issues of privacy and cybersecurity were discussed in a smart city planning workshop held in October 2017, as part of the effort to develop the City’s smart city strategic plan. City officials acknowledged that concerns over privacy are mentioned frequently in public forums, particularly with regard to how the information collected will be used. As one City official stated, the privacy issue is a great concern to the City and will be addressed in its strategic plan.<sup>(95)</sup>

## 7. Designing Contracts for Smart Cities

### 7.1. Global contracts for smart cities

Smart cities may actually require a web of contracts, with one main operator in charge of the whole project and several subcontracts and related contracts with companies, including startups, energy provider, plus other contracts signed with groups of citizens/users involved in local services. All of

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(93) The concept of ‘smartprivacy’, noted above, introduced by authors Cavnoukian, Polonetsky and Wolf, identifies a set of tools to promote the proper use and protection of smart city data. Much like the compliance mechanisms in a procurement system, ‘smartprivacy’ is a multi-faceted approach using familiar elements such as laws, regulations, independent oversight, transparency and accountability to promote the appropriate use and safeguarding of PII. A. CAVOUKIAN, J. POLONETSKY and C. WOLF, “SmartPrivacy for the Smart Grid: embedding privacy into the design of electricity conservation”, *Identity in the Information Society*, August 2010, Vol. 3, Iss. 2, pp. 275-294.

(94) A. GIDARI, *Smart Cities’ Are Too Smart for Your Privacy*, CIS, 20 February 2017.

(95) “Philadelphia Kicks Off Smart City Planning Workshop”, Government Technology, Skip Descant, 19 October 2017.

these contracts will need to be coordinated, with monitoring of private data collected.

The French Government has just released a new bill which, if voted by the Parliament, will offer new tools for smart cities development, although its scope is more about housing. Its drafted Article 1 creates a new contract, the ‘partnership development project’ (PPA) in order to support a new partnership adapted to the different territories in which the State and the intercommunality concerned or the metropolis of Lyon or Paris, can make their reciprocal commitments in favor of carrying out a complex project. If its first aim is to conduct large local development projects with different financing, private and different public entities (including the State, the region, the public body, public local companies, all mentioned above in this chapter but which would be able to join forces).

Furthermore, the traditional commercial relation between supplying companies and public buyers may become outdated in certain sectors such as the energy network with new schemes where a private operator (ex.: a community of residents) can also produce its own electricity and sell it to neighbors. For this sector, the European Parliament, the Commission and the Council are finalizing the development of a new regulation and a new directive on the organization of the electricity market, including the obligation to oblige Member States to Dynamic Pricing Contracts, which, through Linky smart meters, will allow consumers to choose to buy and resell electricity in real time, at market prices updated every 15 minutes.(96)

## 7.2. Specific clauses on technical adaptation are needed

Regarding the performance phase of the contracts needed by smart cities’ projects, the need for change and evolution is striking. In the first place, public contracts will have to adapt to the speed of change in the ‘smart city’ environment. Procurement procedures are lengthy in terms particularly in the areas of public procurement, concessions and partnership contracts. However, the smart city wants to be innovative and dynamic, considering the speed of innovation in this area of connected services and connected goods, the adaptability of the main contract (and its subcontracts) will be crucial. In its 2018 Report, the European Court of Auditors deplors that most of the six ICT projects

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(96) Commission’s proposal for a directive to the Parliament defining the energy community: “a legal entity based on voluntary and open participation, effectively controlled by shareholders or members who are natural persons, local authorities, including municipalities or small businesses and microenterprises. The primary goal of an energy community is to provide environmental, economic or social benefits to its members or local areas where it operates rather than financial benefits. An energy community can be engaged in electricity generation, distribution and supply, consumption, aggregation, storage or energy efficiency services, renewable electricity generation or other energy services to its shareholders or members”.

audited were hardly compatible with long-term contracts as they were exposed to rapidly evolving technologies.

Traditional contracts may be too rigid, although French procurement contracts, like U.S. federal contracts, allow for unilateral change if it is required by the public interest and if its negative financial impact on the private party is compensated. French concessions used to be very adaptable, in compliance with the continuity principle of the public service they are in charge of. However, the new EU package of 2014, in order to ensure competition and prevent any essential modification, has created rules and limitations on contracts' modification that may render technological (for example) evolution more difficult for smart cities. For them, it could be interesting to think about substantial innovation as being a case for unilateral change or termination.

One solution could be to integrate the inherent mutability of the 'smart city' model without requiring any changes to the contractual provisions. This would enable sustainable and mutable public contracts for the smart city. The price revision clauses for certain public contracts over periods longer than 3 months in reference to official benchmark world price indices to adapt the contract to economic fluctuations may serve as an existing inspiration. Mechanisms of unforeseen hardship are another way of making the public contract viable.

## ***8. Conclusion***

All the examples mentioned above, far from being exhaustive, considering the exponential speed of innovation without mentioning the new prospects open by artificial intelligence and smart contracts, force us to reconsider how public contracts could safely convey the smart cities movement. Smart cities may today require new forms of public contracts, transparent and allowing for performance oversight mechanisms conducted by third parties such as citizens. At this early stage, it could be argued that regulation and public contracts, comprising public procurement contracts but also more complex public-private arrangements developing new public service obligations to better serve the citizens (such as clear rules on data use), are still the best adaptable legal bedrocks for supporting the smart cities revolution.

# CHAPTER 8

## From Works Contracts to Collaborative Contracts: The Challenges of Building Information Modeling (BIM) in public procurement

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### 1. Introduction

Technology has deeply changed the procurement sector, as data analysis and data modelling can now play a crucial role within any phase of the procurement cycle. From a legal, economic, and technical standpoint one of the more promising resources in this regard is Building Information Modeling (BIM).

BIM has been described as a methodology allowing “the digital representation of physical and functional characteristics of a facility”. It can be regarded as a resource providing shared knowledge and information about a particular facility, constituting a reliable basis for decision making all through the facility life cycle, from its planning onwards.(1)

This design method enables the user to complete more analytical and effective evaluations than those possible relying on traditional design methods (such as computer-aided design). Furthermore, better design quality can be obtained at reduced costs and with shorter implementation times.

BIM is mainly used to implement “a more efficient planning, design, construction, management and maintenance process using a standardized information model in digital format for each new or existing building. That model contains all the data, either created or collected, on the building in question, in a format that can be used by all stakeholders during the whole life cycle of the building”.(2)

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(1) National BIM Standard – United States.

(2) National Institute of Building Sciences (NIBS) at National Building Information Modeling Standard (NBIMS), cited in T.A.R. Lombardia, Milan, 3 May 2017, No. 1210; G. DI GIUDA, S. MALTESE, F. RE CECONI and V. VILLA, *Il BIM per la gestione dei patrimoni immobiliari. Linee guida, livelli di dettaglio informativo grafico (lod) e alfanumerico (loi)*, Milan, Hoepli, 2017.

From a legal point of view, it is important to observe that information modelling may foster an optimal collaboration among the various actors involved in the design work because there is an increasing awareness of the need for an open and reusable data infrastructure. From the organizational and functional point of view, information modelling can ensure better coordination and monitoring at all times, from the planning phase to the contract award and execution phases. What is more, it can limit the possibility of modifications during the execution phase, which may be critical within a legal framework of alliances and cooperation. In that respect, information modelling may become an indispensable tool to create added value in any procurement procedure and, consequently, in the contracts deriving therefrom. On their part, contracts may become the key for project teams to get the best out of BIM insofar as they appropriately regulate the following issues: (i) deadlines and interfaces in respect of submission and approval of design information and other data; (ii) clash detection, early warning and risk management; (iii) intellectual property rights.(3)

Technology can even be used for drafting so-called ‘smart contracts’ (*i.e.*, contracts based on the blockchain methodology), in which data and information are collected in a chain of blocks and made available forever. These contracts can actually be like a ledger recording everything related to the parties involved.(4)

The BIM acronym has different meanings.

First, it can identify a ‘model’. In this case, BIModel is understood as a digital representation of the physical and functional characteristics of a building, and consists of digital objects with all relevant information.

Second, it can identify an E-modelling tool where BIModeling represents a methodology, the ensemble of all the collaborative processes required for creating and using an electronic model of a particular building.

Third, it can identify a management tool. In this case, BIManagement is a building management and control means, implying the use of a digital model for sharing information among all the subjects involved in the entire life-cycle of the asset in question.(5) Digital tools allow users to collect more precise information and better process that information so as to increase the effectiveness and rationality of the public administration’s response to the collective needs of their communities. They also allow planners to minimize doubtful information giving rise to uncertainties and interpretative problems, which

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(3) See *Enabling BIM Through Procurement and Contracts – A Research Report by the Centre of Construction Law and Dispute Resolution*, King’s College London, 2016, p. 11.

(4) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, Naples, Editoriale Scientifica, 2018.

(5) See *Journal of Building Information Modeling*, 2012, pp. 23 and ff.

often affect the completion of projects designed through traditional techniques, as errors and gaps wise in the execution phase, thus generating conflicts, extra costs, and/or delays.(6)

From a legal standpoint, the possibility of sharing information is the most important factor for ensuring the efficiency and integrity of the procurement process – from the definition of the public requirement through the contract award and management phases. Using BIM may produce an exceptionally positive outcome as meeting fundamental principles in public procurement, for instance transparency of the activities undertaken by public authorities, and control and containment of public expenditures.(7) BIM methodology allows access to common data that can be easily shared among the contracting entity and the different economic operators during the award procedure and with the chosen supplier that will implement the contract. This way, the coherence of data could really become an extraordinary instrument for ensuring efficiency and integrity as it will put an end to the discussion on material amendments, mainly due to gaps in the project phase.(8) In particular, considering the positive interactions existing between the use of the BIM model and the core principles on public procurement, the employment of a BIM-based project as a basis for tender of works contracts appears to be promising. Likewise, the use of BIM methodology for the development of a project in a public procurement procedure could be strategic, *inter alia*, for the assessment of the most economic advantageous tender.(9) Since the implementation of BIM methodology assures the rationalization of public procurement, it reduces risks and costs, as well as information asymmetries. The requirement of a BIM-based project and its enhancement through the tender assessment could foster the pursuit of adequate quality standards supported by technical specifications and high-quality works. Thus, permitting the choice of the better suppliers, thence optimally suited to their needs.(10) To this end, the BIM project planning should be endorsed by a BIM-design strategy report explaining key elements of the project plan (such as the risk management

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(6) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, *op. cit.*, No. 3.

(7) *Ibid.*

(8) G.M. RACCA and R. CAVALLO PERIN, “Material changes in contract management as symptoms of corruption: a comparison between EU and U.S. procurement systems”, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (G.M. RACCA and C.R. YUKINS eds), Brussels, Bruylant, 2014, pp. 247 and ff.; See also F.J. VÁZQUEZ MATILLA, “The modification of public contracts: an obstacle to transparency and efficiency”, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, *op. cit.*, p. 275.

(9) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, *op. cit.*, No. 3.

(10) A contrary opinion is voiced by a recent judgment of the Italian administrative tribunal. See T.A.R. Marche, Ancona, sez. I, 30 May 2018, No. 398 (recital 5 and ff.).

for project design incoherencies etc.),<sup>(11)</sup> the BIM award procedure and the subsequent execution.

Among their main purposes, the 2014 EU Directives on public contracts envisage simplification, to be achieved also by means of IT, though with a certain discretionary power of contracting entities.<sup>(12)</sup> In particular, the EU Directive on public procurement (classical sector) has the goal of simplifying procedures, thus reducing fragmentation among contracting authorities and ameliorating the assessment of quality price *ratio* of a tender. Nonetheless it is worth remembering that the EU Directives define procurement principles and procedures that apply to 28 different countries – which means 28 different implementations in 28 different legal systems rooted in diverse cultural and social traditions.<sup>(13)</sup>

The EU is therefore dealing with a vertical challenge. The Public Procurement Directives can be regarded as defining only a minimum common denominator for the 28 Member States, that then have to implement the provisions therein set forth in accordance with their own legal systems, thus using different languages and different approaches to procurement. As a result, although detailed provisions of EU Directives are directly applicable to any above-threshold EU procurement, to some extent their implementation is subject to variation anyway. However, as stated by the EU Court of Justice,<sup>(14)</sup> most of the rules set forth in the Public Procurement Directives are mandatory, and hence directly applicable if not implemented within the deadline or not correctly implemented.

Because of the considerable amount of below-threshold procurement, the applicability of the EU Procurement Directives is further limited, and so is their impact as a consequence. Also, cross-border procurement in the EU is still rare.<sup>(15)</sup>

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(11) G.M. DI GIUDA *et al.*, “Lean construction applied to a BIM process: how to control point attribution in MEAT tender process”, *Tema*, 2018; S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, *op. cit.*, No. 3.

(12) Dir. 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts; Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC; Dir. 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 Dir. 2004/17/EC.

(13) *Cf.* G.M. RACCA and R. CAVALLO PERIN, *Plurality and diversity of Integration models: the Italian unification of 1865 and the European Union ongoing Integration process*, forthcoming.

(14) The direct effect of European law was first enshrined by the Court of Justice in the judgement of *Van Gend en Loos* of 5 February 1963. 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*, C-148/78). ECJ, 10 November 2011, *Norma-A SIA – Dekom SIA v Latvales plānošanas reģions*, C-348/10, concerning the Remedies Directive (EU Dir. No. 2007/66).

(15) EU Comm., “Measurement of impact of cross-border penetration in public procurement”, Final report, February 2017.

European efforts to develop a more uniform procurement system could facilitate the creation of national procurement markets in contexts where ‘internal barriers’ still exist, for example between Northern and Southern Italy.<sup>(16)</sup> Another example are the German *Länder*.<sup>(17)</sup> A study published in 2011 revealed that only 1.6% of the public procurement contracts in the EU were won by economic operators from outside the country of the contracting authority.<sup>(18)</sup> More recently, the EU Commission has reported an increase of said occurrence to 3.5%.<sup>(19)</sup> The reason why that figure is still low could be that, despite the change pursued through the Directives mentioned earlier, the national procurement legal system of each EU Member State is different and separate from others. Hence, legal and language barriers produce a fragmentation of the public procurement market, with which economic operators are quite used. For this reason, Member States should be able to provide for a competitive dialogue, especially in cases where contracting authorities are unable to define the means of satisfying their needs, foremost when innovative projects are concerned. In this regard, the BIM strategy represents a design effort that might hasten and promote this dialogue in order to boost the synergy among the parties.<sup>(20)</sup>

The BIM may become a strategic methodology to overcome the aforementioned differences and barriers. This applies in particular to the award phase of public procurement, which, on account of the pooling of modelled information, could be turned into smart procurement through a coordinated group of smart collaborative contracts. The sharing of data and information describing the physical and functional characteristics of a facility through technology with all the parties involved in that process allows a deep-dyed assessment during the selection phase (for choosing the best suppliers), thus overcoming ‘information asymmetries’ – one of the main reasons for disputes and failures.

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(16) G.M. RACCA, “Public Contracts – Italy”, *Ius Publicum Network Rev.*, 2012, p. 4; A. MASSERA, “Italie/Italy”, in *Comparative Law on Public Contracts* (R. NOGUELLOU and U. STELKENS eds) Brussels, Bruylant, 2010, pp. 719-720.

(17) M. BURGI, “Public Procurement Law in the Federal Republic of Germany”, *Ius Publicum Network Rev.*, 2012, p. 6; U. STELKENS and H. SCHROEDER, “Allemagne/Germany”, in *Comparative Law on Public Contracts*, *op. cit.*, p. 320; A. RUBACH-LARSEN, “Selection and Award Criteria from a German Public Procurement Law Perspective”, *PPLR*, 2009, p. 112.

(18) Rambøll Management, “Cross-border procurement above EU thresholds”, Rambøll study for the EU Commission, May 2011, p. 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, p. 4.

(19) EU Comm., “Making Public Procurement work in and for Europe”, 3 October 2017, COM(2017) 572 final, p. 4. For further details on the matter, see also *Measurement of impact of cross-border penetration in public procurement*, Final Report, February 2017.

(20) See recital 42 and 43 of Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC.

As procurement is a matter of shared competence between the EU and its Member States, contract management mostly pertains to each EU Member State's sphere of competence. The EU Directive, therefore, does not govern contract execution, which is overseen differently by each Member State. As a consequence, executing a contract may turn out to be significantly different from what is outlined in the relevant procurement award.(21) Such an issue might undermine the meaningfulness of competitive selection and also the fair competition principle, which is at the heart of the EU model.(22)

Arguably, the reason for the separation established between procurement award and contract execution, as set forth in the EU Directives, stem from the Member States' will to maintain their own sovereignty on contract management. The result, however, is a degree amount of uncertainty among economic operators, which eventually jeopardizes the EU pursuit of a well-performing procurement system meeting the needs of all EU citizens. In that respect, the BIM is worthy of interest as it helps ensure that contract notices and all contract documents subsequently issued will be coherent and predictable. On the one hand, this enhances transparency and integrity among all the procurement phases, on the other hand, the BIM helps to overcome legal barriers that hinder contract amendments or make them unavailable during the execution and management phases.

The 2014 EU Procurement Directives introduced limits to 'material amendments' because, *de facto*, they constitute new awards given without contract notice.(23) Such limits show that contract execution monitoring is necessary, and any methodology that could help achieve that goal should be valued. For this reason, the new BIM tools embody a great potential and constitute an important resource in this sense. This has been acknowledged by the EU Directives on public procurement, which provide that for "public works contracts and design contests, Member States may require the use of specific electronic tools, such as building information electronic modelling tools or similar".(24)

(21) G.M. RACCA, R. CAVALLO PERIN and G.L. ALBANO, "Competition in the execution phase of public procurement", *Public Contract L.J.*, 2011, Vol. 41, No. 1, pp. 89-108.

(22) EU Comm., "Report from the Commission to the Council and the European Parliament", EU Anti-Corruption Report, COM(2014) 38 final, 3 February 2014, pp. 26-27; EU Comm., "Green Paper on the modernisation of EU public procurement policy. Towards a more efficient European Procurement Market", 27 January 2011, COM(2011) 15 final, p. 25; conference "*La transizione digitale in Europa per il settore delle costruzioni. Gli effetti delle strategie e dei mandati governativi sul settore delle costruzioni*", Camera dei Deputati, Rome, 18 February 2016.

(23) EU Dir. 2014/24, Art. 72-73; EU Dir. 2014/25, Art. 89-90; EU Dir. 2014/23, Art. 43-44; G.M. RACCA and R. CAVALLO PERIN, "Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption", *EPPPL*, 2013, pp. 287-290.

(24) EU Dir. 2014/24/EU, Art. 22, § 4. This provision was implemented in the Italian Public Contracts Code (Legisl. Decr. No. 50 of 2016) on the rules related to the design of public works (Art. 23, 31, 113). For UK, *see* UK Infrastructure and Projects Authority, "Government Construction Strategy 2016-20", March 2016.

A great advantage of using BIM since the very beginning of the definition of public demand is that it could ensure the same project data for different users (contracting entities, suppliers, monitoring agencies, citizens) allowing them to fully understand each other and cooperate in the project implementation.

The fostering of cooperation and the implementation of the BIM can be carried out initially for the enhancement of the existing public works, even before the creation of new ones. The U.S. experience highlighted how a first use of BIM with this purpose has made its introduction into the public works sector simpler and more efficient. This allowed public employees to become more aware of the potential of BIM through its use on already known projects.

In some EU Member States, the introduction of BIM clashes with the low rate of digitalization in the construction sector and with the difficulty in demonstrating the benefits of the BIM.(25)

In the United Kingdom, the BIM statement in the governmental strategy has been in place (i.e., thanks to a recession of the market), while currently, in an expanding cycle, operators appear more reluctant to continue on this path, in part because its benefits are not always demonstrable. A recent study published by the Centre of Construction Law and Dispute Resolution of King's College (London) showed that BIM has increased the scope and speed of data exchange, while at the same time enabling more integration and collaboration for a better asset performance over the full project life-cycle. Nonetheless, some uncertainties remain in relation to the reliability of BIM computer software programs and defensive contractual approach to legal liability encouraged by BIM models.(26)

In Germany, despite a great 'buzz' both at the federal and State levels, the same positive trend of the market induces, beyond a formal adhesion, many subjects to postpone the implementation of digital procedures: analyses carried out by PwC point out that less than 10% of economic operators (in the construction field) are already working in this direction.

In France a special platform called KROQI was developed by the *Centre scientifique et technique du bâtiment* as part of the *Plan transition numérique dans le bâtiment*(27) with the aim to create a reference context in which actors can find themselves in everyday life.

In Italy, the recession, although it advanced selective processes among the organizations and even generated a transformation of the relevant market, did not push actors to seriously introduce, in an autonomous manner,

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(25) Conference "*La transizione digitale in Europa*", *op. cit.*, No. 15.

(26) "Enabling BIM through procurement and contracts – A Research Report by the Centre of Construction Law and Dispute Resolution", King's College London.

(27) A.L.C. CIRIBINI, "L'Italia del BIM", [www.ingenio-web.it](http://www.ingenio-web.it).

significant innovations in terms of digitalization.(28) All the same, the recent reform and the enactment of the new Public Contracts Code have entrusted a paramount role to the use of digital tools and methods, with the aim of rationalizing design and project activities – as well as improving the control on the timeframes and costs of execution – for public works.(29) The new Public Contracts Code makes explicit reference to the progressive implementation of digital methods such as BIM so to achieve an integrated design phase enabling the creation of a comprehensive database and the 3D modelling of the designed products.(30) Nonetheless, a certain level of uncertainty in the use of BIM has already shown in the Italian legal system, as proved by a recent case before the Italian Administrative Judge, called upon to rule on the compliance of the projects presented in the offer with the requirements provided by the contracting authority.(31) Such case law has clarified that there is not a single BIM model, as BIM is essentially a working method: “the BIM is not a thing or a type of software but a human activity involving extensive modifications in the building sector [...] in order to introduce a more efficient process of planning, projection, construction, management and maintenance through a standardized model for digital information referring to each single building”.(32) The lack of adequate capacity in the use of digital tools has thus become apparent.

That acknowledged, the 2016 Italian Public Contracts code(33) favours collaboration and qualification of public demand(34) with the purpose of efficiency and integrity. The Italian provisions on Public Contracts provide for the rationalization of design activities (for works) and the related monitoring activities through the progressive use of specific electronic instruments such as modelling for buildings and infrastructures.(35) Guidelines provided by the Italian Anticorruption Authority refer, for the first time in the national legal

(28) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, op. cit., No. 3.

(29) *Ibid.*

(30) *Ibid.*

(31) T.A.R. Lombardia, Milan, 3 May 2017, No. 1210. The case concerns the award procedure launched by the Municipality of Milan for an integrated contract (demolition, remediation and reconstruction of a school building) that had to be awarded with the criterion of the most economically advantageous tender. The appeal focused on the illegitimate admission to the tender of a party, which should have been excluded for having submitted a project not compliant with the *lex specialis* of the tender. After the technical verification, the Judge affirmed the compatibility of the project presented with the BIM model.

(32) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, op. cit., No. 3.

(33) Legisl. Decr. No. 50 of 2016, enacted in 19 April 2016.

(34) *Ibid.*, Art. 37-43.

(35) *Ibid.*, Art. 23(h). See ANAC, Resol. No. 138 of 21 February 2018, Guidelines No. 1, “*Indirizzi generali sull’affidamento dei servizi attinenti all’architettura e all’ingegneria*”, updated to the Legisl. Decr. No. 56 of 19 April 2017.

order, to the person ‘responsible for the procedure’ as a ‘project manager’.(36) Planning and management skills are emphasized, as well as the coordination of the work activities, the achievement of the objectives in time and at the expected costs. These skills may derive from the specific training of public officials and from the coordination of all available resources, which in turn allows the administration to establish a support unit for the procurement official appointed as ‘responsible of the procurement procedure’.(37)

In this regard, the Italian Ministry of Infrastructures and Transport recently adopted a regulation(38) implementing the Code(39) aimed to define the methods and timeframes for the progressive introduction of electronic methods and tools by Italian contracting authorities and economic operators, such as those for building modelling and infrastructures, in all phases of the design, construction and management of works and in the related monitoring activities.

From 2019, use of BIM will be mandatory for all works above 100 million euros of value and, by 2025, also for contracts of smaller amounts, until this method will be introduced throughout the whole public works sector. Even though this regulation details the timing for the national implementation, a great effort on capacity development is nonetheless required. The progressive extension of the mandatory use of BIM in the public sector will take longer compared to other Member States: unfortunately, this is in line with the information provided by the European Commission showing that Italy is a country in which, generally speaking, the application of digital tools in the relationship between the citizen and the public administration is still very limited.

In a procurement market that is really fragmented, the fear of restricting access to the most equipped operators is halting a real and effective competition.(40)

## ***2. Collaborative and integrated processes in public works contracts***

The effective implementation of BIM, also in the private sector, requires collaboration among stakeholders involved in the different phases of a work life cycle. BIM implies at the same time three types of projects: the architectural project, the structural project and the plant design. The introduction of a BIM

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(36) Italian Anticorruption Authority, Resol. No. 1007 of 11 October 2017, Guidelines No. 3, “*Nomina, ruolo e compiti del responsabile unico del procedimento per l'affidamento di appalti e concessioni*”.

(37) Legisl. Decr. No. 50 of 2016, Art. 31.

(38) Min. Decr. No. 560 of 1 December 2017.

(39) Legisl. Decr. No. 50 of 2016, Art. 23 (13).

(40) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, op. cit., No. 3.

methodology in the public procurement sector under the EU directive requires a further analysis, as such introduction would as a minimum imply the design of specific clauses or protocols, while at the same time representing an opportunity to define specific contractual models.

Collaborative processes are strategic, also in the private sector, because the fragmentation may lead the Architecture Engineering and Construction (AEC) sector towards a paralysis in terms of productivity.

During the past years, many studies on this topic have been carried out in the U.S. and in European countries, especially on the explanation of the contract structure and regarding how Architecture Engineering and Construction operators might adopt collaborative processes.

Analyzing the Architecture Engineering and Construction macro-economics,(41) one of the main points which stands out is that the productivity of the sector(42) did not change in the period between 1964 and 2000. In fact, by comparing the productivity index of construction and non-farm labour in the U.S. market, it can be noticed that the latter has doubled its productivity, but on the contrary, the former remains approximately unvaried.

Analyzing ISTAT's (Italian National Institute of Statistic) reports of the last two decades, the 2008 crisis had a stronger effect on the Architecture Engineering and Construction sector (-30% productivity) than on the manufacturing sector, in which the decrease was a little more limited (-20% productivity and tool work, which is the actual time spent working). Still at present, the gap between these two branches remains wide (around 200 points).

Some U.S. studies stated that almost "half of all construction activities are non-productive and disclose the ineffectiveness of many projects".(43) It is possible to declare that poor performance related to the design and construction industry are not just a U.S. phenomenon, rather it is spread across all developed countries.

The data from the UK, the U.S. and Scandinavia showed, as a result, that 30% of construction is reworked, the efficiency of labour is just around 50%, accidents absorb 3-6% of construction costs and at least 10% of all the materials are wasted.(44) This fact means that the construction sector has surely

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(41) C.M. EASTMAN and R. SACKS, "Relative Productivity in the AEC Industries in the United States for On-Site and Off-Site Activities", *J. Constr. Eng. Manag.*, 2008, 134, pp. 517-526.

(42) H.C. HOWARD, R.E. LEVITT, B.C. PAULSON, J.G. POHL and C.B. TATUM, "Computer Integration: Reducing Fragmentation in AEC Industry", *J. Comput. Civ. Eng.*, 1989.

(43) A. SCHWARTZ and R.E. SCOTT, "Contract theory and the limits of contract law", *Yale L.J.*, 2003, 113, pp. 541-619.

(44) H.-S. PARK, S.R. THOMAS and R.L. TUCKER, "Benchmarking of Construction Productivity", *J. Constr. Eng. Manag.*, 2005, 131, pp. 772-778.

received a certain amount of innovation, but not as much as other industry sectors. Therefore, the concern is how to make the construction companies more competitive.

In the public procurement sector, it is well known that the high number of SMEs is related to the fragmentation of public demand.<sup>(45)</sup> The collaborative contracts might surely help in this regard.

The main goal of collaborative contracts is to solve the construction industry's low rate of productivity, high rate of inefficiency and excessive costs caused by the organizational process (*i.e.* reworking of information lost during the process).<sup>(46)</sup> As already noted, one of the main reasons for this inefficiency is the fragmentation in the Architecture Engineering and Construction sector.<sup>(47)</sup>

Collaborative contracts reduce fragmentation and provide an integrated approach to innovate in the sector. Specifically, according to the abovementioned study,<sup>(48)</sup> there are three different mechanisms that are typical of the Architecture Engineering and Construction sector and only through an integrated hierarchical organization is it possible to achieve a complete exchange of information between different stakeholders without losing anything.<sup>(49)</sup> Collaborative agreements (the so-called *alliancing*), in fact, may be a valid alternative to the disputes characterizing the execution phase, which often slow down, halt or make it impossible to attain the goals underlying the procurement procedure. Those kinds of contracts do not replace the typical contractual schemes linking contracting authorities and economic operators for the governance and execution of the contract. Rather, collaborative agreements play a complementary role, as they regulate mutual interactions in a way that is beneficial for all parties involved.<sup>(50)</sup>

(45) A.N.AC., *Annual Report 2016*, 6 July 3027, p. 155; R. CAVALLO PERIN and G.M. RACCA, "La concorrenza nell'esecuzione dei contratti pubblici", *Diritto Amministrativo*, 2/2010, pp. 325-354; G.M. RACCA, R. CAVALLO PERIN and G.L. ALBANO, "Competition in the execution phase of public procurement", *Public Contract L.J.*, 2011, Vol. 41, No. 1, pp. 89-108; G.M. RACCA and R. CAVALLO PERIN, "Material Amendments of Public Contracts during their Terms: From Violations of Competitions to Symptoms of Corruption", *EPPPLR*, 4/2013, pp. 279-293; G.M. RACCA and R. CAVALLO PERIN, "Material changes in contract management as symptoms of corruption: a comparison between EU and U.S. procurement systems", in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, *op. cit.*

(46) C. THOMSEN, "Managing Integrated Project Delivery – Concepts and Contract Strategies", *Cmaa*, 2007, 35, p. 52.

(47) I. EL-ADAWAY, "Relational contracting and high-performance project outcomes", *Proceedings*, Annual Conference, Canadian Society for Civil Engineering, 2011.

(48) A. SCHWARTZ and R.E. SCOTT, "Contract theory and the limits of contract law", *op. cit.*

(49) R. LEVITT, M. FISCHER and A. SMITH, "Assessing the Impact of IPD on Adoption of Innovations Related to Energy Efficiency", San Francisco, 2012.

(50) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, *op. cit.*, No. 3. The author references an interesting example of *alliancing*, promoted by the British Ministry of Justice for the construction of a new wing of the *Cookham Wood* penitentiary for minor inmates. In

Collaborative agreements were first used in Asia as ‘gentlemanly principles’ and were informally and legally non-binding agreements between two or more parties, but they were based on people’s honour.(51) Later on, after this first attempt at introducing a collaborative process, there have been many trials in America. At present, the two most important experiences with regard to collaborative agreements are the Integrated Project Delivery (in the United States) and the so-called *alliancing* (an umbrella-term for many different models of cooperation among stakeholders, typical of the British procurement scenario, whose spearheads are the PPC2000 and the FAC-1). Before embarking on a detailed explanation of the two approaches (*see infra*, par. 5), it seems useful to understand how collaborative contracts and BIM can be complementary in enhancing efficiency in public procurement.

This idea is the core concept on which BIM is based: indeed, Integrated Project Delivery is the perfect environment to obtain strong development of advanced management methods.(52) Thus, it will provide substantial benefits in efficiency and safety, as well as integration: statistics on Integrated Project Delivery projects under construction confirmed the results of the abovementioned studies.(53)

A second main point that should be emphasized, as previously noted, is the fragmentation in the diffusion of information among stakeholders involved in the construction chain. Individualism causes information asymmetry, because some people inevitably have more information than others and they do not want (or do not have the interest) to share it. This occurs because every participant wants to pursue his own interest instead of the interest of the project.

The change of perspective from an individual’s goal to a team’s goal, trying to achieve a better result, is possible only if everyone makes the best both for himself and for the team at the same time;(54) cooperation is able to fill the gap between design, construction and maintenance phases. The missing piece, as

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that case, BIM was combined to the PPC2000 – *Project Partnering Contract*, i.e. an embryonic model of collaborative agreement which involved in the first phases of the project all the parties having a role in the realization of the construction. This experiment led to 20% savings and to a reduction of timeframes from 50 to 44 weeks.

(51) One of the first attempts to compare contractual forms was made by Lahdenpera, who analyzed some early endeavors of multi-party agreements, project partnering, project alliancing and integrated project delivery, in P. LAHDENPERA, “Making sense of the multi-party contractual arrangements of project partnering, project alliancing and integrated project delivery”, *CMEJ*, No. 30, 2012, pp. 57-79.

(52) D.C. KENT, BECERIK-GERBER, „Understanding Construction Industry Experience and Attitudes toward Integrated Project Delivery”, *J. Constr. Eng. Manag.*, 136, pp. 815-825; P. LAHDENPERA, “Making sense of the multi-party contractual arrangements of project partnering, project alliancing and integrated project delivery”, in *Constr. Manag. Econ.*, No. 30, 2012, pp. 57-79.

(53) H.W. ASHCRAFT, “The IPD Framework”, *Hanson Bridg. white Pap.*, 2012, pp. 1-28.

(54) R.B. MYERSON, “Nash Equilibrium and the History of Economic Theory”, *J. Econ. Lit.*, No. 37, 1999, pp. 1067-1082.

many studies have demonstrated, is the contractual form allowing the sector to be more competitive. Only with these changes in the sector's mindset, as a consequence of the introduction of cooperative contracts, the construction sector might prove able "to see quality projects that deliver excellent whole life value, that excellence in design and that encompass excellence in design and functionality that are safely built and are on time, on budget and defect free".(55)

From a legal perspective, in the public procurement sector this might simplify cooperation among different suppliers in the execution phase and favour monitoring activities for a correct execution. Furthermore, the inefficiency and integrity issues related to the acceptance of a performance lower than promised might be overcome.

Indeed, 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.(56) Collaborative contracts might overcome such an adversarial perspective and favour positive results for the procurement and a correct execution of the public contracts.

In public contracts, unlike in private contracts, any amendment to the contractual conditions due to the contractor's underperformance also affects third parties, including – but not limited to – unsuccessful tenderers.(57) By having a substantial interest in the conformance of the contractor's performance to what was promised at the award stage, losing tenderers should be able to report infringements to challenge the contractor's lower-than-promised performance as set in the contract awardee. As a consequence, losing tenderers 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.

BIM substantially reduces the risks of modifications during the execution of the contract(58) increasing the level of coherence of the project and solving possible clashes among disciplines. In any event, any required modification should be correctly evaluated and agreed in full transparency among all concerned stakeholders. As already mentioned, BIM has been introduced

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(55) B. WILSON, UK Construction Minister.

(56) G.M. RACCA and R. CAVALLO PERIN, "Material changes in contract management as symptoms of corruption: a comparison between EU and U.S. procurement systems", in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, *op. cit.*, p. 247.

(57) H. SCHRÖDER and U. STELKENS, "EU Public Contract Litigation", in *EU Public Contract Law, Public Procurement and Beyond*, *op. cit.*, p. 443.

(58) Dir. 2014/23/EU; Dir. 2014/24/EU; Dir. 2014/25/EU.

in the Italian Public Contracts Code(59) by the Italian legislator with the expression “methods and electronic instrument, through open format, not proprietary”. This is very close to the original EU provision which states: “specific electronic tools, such as building information electronic modelling tools”.(60)

BIM is not just software but, actually, it is a thinking process, a methodology. This process is characterized by a strong partnership between the employer, on the one hand, and all the tenderers and bidders (*i.e.* suppliers, designers, constructors, facility manager and everyone who is involved in the process), on the other. Through this methodology, it is possible to achieve an analytical and objective observation of the project.

From a public procurement perspective this method allows the qualification of contracting authorities(61) and increase of the coherence among the requirements of the different phases of the design and the subsequent award and execution of a work.

BIM allows also the *ex-ante* definition of the life cycle cost of the work according to the tendered design, so that it can reduce the risks of modification of the contract during its term.

While it is commonly accepted that competition must be ensured among economic operators beyond their mere access to the market,(62) the idea that the respect of the competition principle ought to be ensured also during the performance of a public contract of works, goods and services has not yet been appropriately considered.(63) To avoid having value for money to remain as an abstract concept, the contractor’s actual performance should coincide with what was promised at the competitive stage.

A substantial modification can occur in case of “changes in the economic balance of the contract or framework agreement in favour of the contractor in

(59) See Art. 23 (13), *Legisl. Decr. No. 50/2016*, aforesaid, contracting authorities equipped with trained staff can request the use of specific electronic methods and tools for recovery, redevelopment or alteration interventions, primarily for complex works; in fact, these tools use interoperable platforms with non-proprietary open formats, in order to avoid the limitation of competition between the technology suppliers and involvement of specific projects among the designers; in the *Min. Decr. 560/2017*, aforesaid, published on the MIT Web site on 12 January 2018, procedures and times for the gradual introduction of the compulsory nature of the aforementioned methods are defined for the contracting stations, the granting administrations and the economic operators. They are assessed in relation to the type of assigned works, the digitalization strategy of public administrations and the construction sector. Using these methods is considered as yardstick of the rewarding requisites, *ex Art. 38, Legisl. Decr. No. 50/2016*.

(60) *Dir. 2014/24/EU*, Art. 22, par. 4.

(61) On Italian provision on qualification and professionalization of contracting authorities, see *Legisl. Decr. No. 50 of 2016*, Art. 37-43.

(62) G. NAPOLITANO and M. ABRESCIA, *Analisi economica del diritto pubblico*, Bologna, Il Mulino, 2009, p. 95.

(63) R. CAVALLO PERIN, G.M. RACCA and G.L. ALBANO, “The safeguard of competition in the execution phase of public procurement”, *Quaderni Consip*, VI, 2010.

a manner which was not provided for in the initial contract”.(64) 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.(65)

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, by distorting bids ranking *a posteriori*, thwart the competitive selection process.(66)

The ability to collect *and* interpret information (easily, where all the data are defined in a BIM model) during the execution phase can make losing tenderers, together with the procuring authority, the most effective ‘supervisors’ of the contractor’s compliance with contractual terms and conditions. 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 extended 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 at the same time 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.(67) However,

(64) EU Dir. 2014/24, Art. 72, par. 4(b).

(65) ECJ, *EU Commission v. Federal Republic of Germany*, Case C-160/08, aforesaid, paras. 98-101. The amounts of the extension of the contract was quantified in €673,719.92. This case concerned the award of contracts for public ambulance services where it has been considered substantial due to the extension of the subject matter of the contract to a ‘district association’ non-indicated in the contract; G.M. RACCA, R. CAVALLO PERIN and G.L. ALBANO, “Competition in the execution phase of public procurement”, *Public Contract L.J.*, 2011, Vol. 41, No. 1, pp. 89-108.

(66) Concerning the principle of Transparency, see C.H. BOVIS, *EU Public Procurement Law*, Cheltenham, Edward Elgar, 2007, p. 67. See also *id.*, “Regulatory Trends in Public Procurement at the EU Level”, *EPPPPL*, 2012, pp. 225-226.

(67) G.M. RACCA, “The role of third parties in the execution of public contracts”, in *Contrôle et contentieux des contrats publics – Oversight and remedies in public contracts* (L. FOLLIOU-LALLIOT and S. TORRICELLI eds), Brussels, Bruylant, 2017, p. 415.

monitoring the correct implementation of the contract may be a useful tool to prevent potential illegal or collusive behaviour among economic operators and to better ensure competition throughout the entire public procurement cycle and in the procurement sector. Any misconduct during the performance phase constitutes a distortion of competition and within the EU this can entail 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.

The information provided through the BIM approach and its implementation seem to become fundamental to ensure the key goals of efficiency and integrity.<sup>(68)</sup> The perspective of cooperation contracts implies a different set of relationships among the different private suppliers and the contracting entities, that should find a correct form of incentivization to reach the goal of a prompt and effective implementation of the agreed goal of the procurement.

An external monitoring might be useful and might be provided in the cooperation contract. Nonetheless, the effective incentives for correct behaviour should be internal to the cooperation contract.

### ***3. Construction procurements and contracts models in different legal systems***

It seems interesting to make a comparison between U.S. and European approaches and their experiences in collaborative contracts mainly, but not only, in the private sector, as well as to analyze the different types while highlighting the main problems dealing with the specification of the main characteristics which transversally affect each collaborative contract.

A 'project' may be defined as "what a person has the intention to make happen". Based on this concept, a project delivery system should reliably deliver projects capable of satisfying the owner's needs in an efficient, effective and sustainable way. In the public procurement sector 'the owner' is the public administration that acts as contracting entity and requires the procurement of work. At the international level, it is possible to refer to several contractual models for establishing the contractual relationships between awardees and public entities in the work sector. Each contractual model produces different

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(68) National BIM Guide for Owners, contracting authorities must to apply their existing data security standards to BIM protocols. "The Owner should consider the security risks in terms of the protection of data. The Owner may wish to consider including data restrictions procedures, such as check-out and check-in, as well as stipulating the degree of access control for project participants. The Owner should require the Project BIM Team to complete a Data Security Protocol that complies with defined data security requirements at an international level".

effects on the content of the contractual documents that will be the basis of the award procedures and in the management of the subsequent contract (division of costs, accountability and risks).

In the U.S. system, the Project Management Institute(69) divides contract types in three main categories, based on the sharing of the risk between sellers and buyers.

The first category is Cost-reimbursable contracts, in which seller receives payment for actual costs to complete the work, plus a fee representing its profit, having Cost Plus Fixed Fee (CPFF), Cost Plus Incentive Fee (CPIF), and Cost-Plus Award Fee (CPAF).

The second one is Time and Materials (T and M) contracts: their characteristics are similar both to cost-reimbursable and fixed-price contracts.

The third category is Fixed-price contracts, which involve setting a fixed total price for a defined product, service, or result to be provided. The categories are: Fixed Price Contracts (FP), Fixed Price Incentive Fee Contracts (FPIF) and Fixed Price with Economic Price Adjustment Contracts (FPEPA).

One of the most used forms of procurement is Design Bid Build (within the CPFF category): it is so popular all around the world because it divides the process into three steps and, in particular, many public administrations (PA) impose a mandatory division. This form allows fragmentation in the Architecture Engineering and Construction sector, in fact designers base their work on the quality of the project in terms of comfort, performances and beauty of spaces, but they are not evaluated on costs and schedules, which are a burden of the contractor.

In this way, many projects can be evaluated and rebates can be obtained. This result could appear as an ideal achievement for the contracting entity but, looking at the statistics, is noticeable that more than 40 per cent of the traditional processes finish over budget and delayed.

Under the EU procurement Directive, the award criteria may be the Most Economically Advantageous Tender (MEAT),(70) which provides for evaluation of the quality of the offers with a view to ensuring the final quality of the project. Nonetheless, it is important to emphasize that subjective and not measurable quality criteria may be included inside the Most Economically Advantageous Tender criteria, which can, in a worst case, turn the process

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(69) Project Management Institute, 2008, *PMBOK*, 5th ed., Project Management Institute, Newton Square, Pennsylvania.

(70) G.M. DI GIUDA, V. VILLA and L. LORETI, "Il BIM per la gestione di una gara con il criterio dell'offerta economicamente più vantaggiosa – BIM to manage public procurement with award criterion Most Economically Advantageous Tender", *ISTeA*, 2015, pp. 1-4.

into arbitrary evaluations.(71) This issue could be faced in an innovative way through the modelling of all the data concerning the project.

Construction Management at Risk (CMAR)(72) is a contract based on an owner (contracting entity) protecting its assets and building construction time. Specifically, Construction Management at Risk is able to accomplish the construction of a project, previously designed, as scheduled and at the defined price. This conceptualization gives the owner assurance of the execution in terms of costs, reducing uncertainty and minimizing opportunism, because the owner, on the one hand, knows how much the project is going to cost as there is typically a guaranteed maximum price. On the other hand, Construction Management at Risk does allow the contractor to be involved in the design phase, but it does not provide a fruitful collaboration with the design team, because each improvement will benefit only the constructor. This contractual form does not improve the conceptualization of the project and each saving in the construction phase will benefit only the Construction Management at Risk. The final product will fit the owner's requests imposed by the project, but there may not be any optimization of the design choices.

A third type of delivery method is Design Build (DB),(73) which could be considered as a sort of collaboration contract set in a traditional environment. This is because the Design Build method is able to ensure a strong communication between designers and constructors, which most of the time is unbalanced since the latter used to hire the former. For this reason, just one participant collects all the advantages of the project optimization and the others are not driven to improve their work. A fixed price imposition is something that protects the owner, but statistical data shows a large volume of litigation created by this methodology of contract, mainly caused by delay and impact claims in fixed-price and guaranteed-maximum-price projects, which suggests that these project methods do not bring price or schedule certainty.(74) Most of the largest projects around the world are executed on fixed price contracts, and statistics also show a high index of litigation related to the number of delays and over-budgets.(75)

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(71) G.M. RACCA, R. CAVALLO PERIN and G.L. ALBANO, "Competition in the execution phase of public procurement", cit., pp. 89-108; D.I. GORDON and G.M. RACCA, "Integrity Challenges in the EU and U.S. Procurement systems", in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, op. cit., p. 117.

(72) G.M. DI GIUDA and V. VILLA, "Collaborative Design and Collaborative Contracting a Defiant Challenge", in *Digitizing the Analogical Thoughts in Architecture: A Menace or a Promise?* (B. ANGI, M. BATTISTI and S. MASTROLEMO eds), San Marino, IMREADY – Ingenio, 2016, p. 10.

(73) *Design-Build Institute of America, 2015. Design-Build Institute of America, 2013, State Statute Report.*

(74) M. KONCHAR and V. SANVIDO, "Comparison of U.S. Project Delivery Systems", *J. Constr. Eng. Manag.*, 1998, 124, pp. 435-444.

(75) E.M. MERROW, *Industrial Megaprojects: Concepts, Strategies, and Practices for Success*, Hoboken, John Wiley & Sons, 2011

Through this analysis, attention will focus on the third level of collaboration defined by the National Association of State Facilities Administrators (NASFA).<sup>(76)</sup> Three different collaboration stages can be recognized: (i) traditional, (ii) enhanced and (iii) multi-party contract. The first level means that collaboration is not contractually required. The second one means that there are some requirements of contractual collaboration in the contract, and the last requires collaboration in a multi-party contract.

The inability of the industry to move from sequential to integrated design seems to reside in the adversarial business context created by transactional contracting methods.<sup>(77)</sup>

#### ***4. Collaborative Contracts: Relational Project Delivery Arrangements (RPDAs)***

Relational Project Delivery Arrangements (RPDAs) are contracts based upon a relationship built on trust and transparency principles. This kind of delivery system promotes collaboration among all parties involved. The historical antecedents to this approach are hereby presented to analyse the evolution of the different Relational Project Delivery Arrangements types.

As described before, over the recent decades, some traditional project delivery systems have emerged claiming to fill the gap between the design and construction projects, but they have been shown to be not efficient enough. In this context, collaborative contracts (e.g. AIA C191, PPC2000, FAC-1, NEC4, JTC) were developed in many countries and present basically the same principal characteristics.<sup>(78)</sup>

Due to their structure and composition, traditional contracts unavoidably create a conflict of interest, which cannot be solved and impose a rigid division of the stakeholders' works. The new working organizational models outlined though collaborative contracts upgrade the optimization of the project through an integrated approach executed under Lean principles.<sup>(79)</sup> The main

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(76) M. KENIG, M. ALLISON, B. BLACK, L. BURDI, C. COLELLA, H. DAVIS and M. WILLIAMS, "Integrated project delivery for public and private owners", National Association of State Facilities Administrators (NASFA), Construction Owners Association of America (COAA), The Association of Higher Education Facilities Officers (APPA), Associated General Contractors of America (AGC) and American Institute of A, 2010.

(77) G. BALLARD and L. KOSKELA, "On the agenda of design management research", IGLC.net, 1997.

(78) G. DI GIUDA and G.L. ALBANO, "Framework Agreement and Collaborative Procurement in Italian Legislation Enhancing a BIM Approach", *New Frontiers of Construction Management Workshop*, forthcoming.

(79) G. BALLARD and G.A. HOWELL, "Competing Construction Management Paradigms", *Construction Res. Congr. Wind. Chang. Integr. Innov. Constr. Proc. Congr.* 1, 2003, pp. 321-328: these complementary approaches are melded in a report, which concluded that an integrated approach has to respect the five key Lean principles of value, value stream, flow, pull, and perfection.

points which diversify collaborative contracts from other ones are listed in the following paragraphs.

The analysis of data concerning the last decades in the U.S. and in Europe(80) shows that the expected trend for the next years is going to be a severe mutation from the perspective of traditional tenders, such as Design Bid Build, to a collaborative view.

It has been noted how the early involvement of key participants has increased productivity both in design and construction phase.(81) Extending these considerations, the combination of competences from different participants may provide many benefits to Architecture Engineering and Construction sector, which is moving in this direction.

In the next paragraphs, the main characteristics of the Relational Project Delivery Arrangements are presented, starting from the more generic assumptions and proceeding to the more specific ones.

#### 4.1. Multi-party and Poly-party contracts

The integrated agreement creates a system of shared risks, with the aim of decreasing the total risk of the entire project.(82) That could happen if most of the consultant and sub-contractors join the agreement; the general rule is to have at least half of the construction cost discussed at the decision table. The contract could be set in two different ways.

These two kinds of agreements are based on the procedure of setting the first contract through three main figures (Owner, Designer and Constructor).

One of the possible configurations of the collaborative agreement involves just the three main key participants, which sit at the decision table. The other participants are involved in the decisions through an elected member; in this way, there is just one representative for the owner, one for the designer, one for the constructor and the others are in any case part of the risk-reward structure. The abovementioned sub-agreements do not just give duties to the subjects involved, they also provide them with the same rights (with the exception of a limitation in the vote) in terms of sharing profits. On the contrary, in the other case, the core group is composed of all the people in the risk-reward structure: this kind of solution is achievable in relatively small projects due to the limited number of people involved. A new member – which becomes part of the collaborative contract – has the choice to enter either in a risk-reward position, or as a traditional consultant/

(80) M.S. SINGLETON, *Implementing Integrated Project Delivery on Department of the Navy Construction Projects*, www.researchgate.net, 2010.

(81) D.D. MCWHIRT, *A comparison of design-bid-build and design-build project delivery methods on military construction projects*, Iowa State University, 2007.

(82) W.A. LICHTIG, “The Integrated Agreement for Lean Project Delivery”, *Improv. Healthc. through Built Environ. Infrastruct*, 2010, pp. 85-101.

subcontractor, which only requires the accomplishment of his duties without a strong collaboration.

One of the main reasons why it is important for collaboration to ensure the sharing of both profit and losses is to account for the risks of the entire collaboration. In the corporate economy, the company's overall risk can be broken down into economic risk, financial risk and asset risk. This means that if a component of a team participates as an active member of the collaboration, it has to guarantee benefits for all the participants involved and face all the consequences. These two kinds of collaborative models are possible both within the Integrated Project Delivery and within a framework alliance as will be described further on.

#### 4.2. Early Involvement of Key Participants

This collaborative form of contract lets team members express their full potential, but, considering the increasing complexity of projects,(83) it increasingly requires an Early Involvement of Key Participants (EIKP) in the projects.

This fact also imposes a change in the investment structure:(84) there is an anticipation of the choices and therefore an early discovery of potential problems, which, in a traditional process, could be found later. The Early Involvement of Key Participants has many benefits.

One of them is that the project team can work together at the same time on the assignment by sharing information and resolving the traditional lack of communication.(85) This way of working, combined with the use of a BIM, removes ambiguity in the documents and optimizes the project quality.(86) The concept of 'Big Room',(87) as a place where all the stakeholders, including the client, can share their knowledge is key to create a joint team that will pursue the same goals, defined together in terms of costs, time and quality. The anticipation of the stakeholders' involvement helps not only in the success of the final project, but also assures mutual sharing of experiences while dealing with the problems so that they can be seen from different perspectives and be solved in the best way possible. This way of collaborating does not reduce the

(83) S. GOKHALE, "Integrated Project Delivery Method for Trenchless Projects", *ICPTT Sustain. Solut. Water, Sewer, Gas, Oil Pipelines*, 2011, pp. 604-614.

(84) According to P. MacLeamy's curve, *BuildingSMART International*, HOK presentation, session "BIM promise and challenge", 8 March 2018.

(85) F.D. LANCASTER and J. TOBIN, "Integrated project delivery: Next-generation BIM for structural engineering", *Structures Congress*, 2010.

(86) M. MIHIC, J. SERTIC and I. ZAVRSKI, "Integrated Project Delivery as Integration between Solution Development and Solution Implementation", *Procedia - Soc. Behav. Sci.*, 2014, 119, pp. 557-565.

(87) B. LOSTUVALI and B. ALVES, "Learning from the Cathedral Hill Hospital Project during the Design and Preconstruction Phases", *Int. J. Constr. Educ. Res.*, 2014, 3-10, pp. 160-180.

number of stakeholders and people involved but optimizes their work. In just a few phases of the project, some people try to command, because they used to behave in this way in a traditional process. This habit has to stop, because it is unproductive.

In a new way of conceptualization of jobs, there are so many aspects and consequences involved in a decision that it is not possible to have a single person who is able to understand the impacts on each branch of knowledge.

Through EIKP, it becomes possible to understand all these aspects: it is a common interface which relates to all the collaborative contracts in general. It is also particularly useful in complex projects that require many project participants to be integrated into a virtual organization. The Key Participants are contractually engaged at the earliest moment. This conclusion is consistent with the research indicating that higher performance is achieved when teams are assembled before, at least, 20% of design has occurred.(88)

#### 4.3. Goals validation and global optimization

One of the best ways to achieve this type of contractual relationship is the alignment of the project goals. It means that everyone in the project has the same aim, so that in order to improve the project, there are no excuses not to propose ideas for development.

One of the main changes brought by Relational Projects Delivery Arrangements focuses on the team: in a traditional vision, a team is seen as sum of people who have to work together but everyone has a different task.

In a collaborative perspective there is a different conception of team, but the main goal is the same: an optimized project. This is the reason why it is fundamental to change from a traditional approach, in which each party follows its own goal to obtain the best for itself even where the project does not enhance. In a collaborative approach – at the beginning – there is a starting phase in which the main objectives are set, so all team members know the final scope. In a collaborative approach the design team, the construction team and the facility management team collaborate in the design and construction phases.

An efficient project uses the minimal amount of labour and material necessary to achieve project goals.(89) The sequencing of objectives and their consequent validation by the team makes the case for a solid and joint teamwork, where everyone acts as a part of a single firm.

The sum of perfect projects is not the best one. This sentence could be explained by a simple verification: an architectural choice of having an

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(88) M. KONCHAR and V. SANVIDO, "Comparison of U.S. Project Delivery Systems", *J. Constr. Eng. Manag.*, 1998, 124, pp. 435-444.

(89) H.W. ASHCRAFT, "The Transformation of Project Delivery", *Constr. Lawyer*, 2014, 34, pp. 1-8.

over-insulated building is the best choice in a winter season, but it is the worst in summer. In fact, this choice will bring to the Mechanical Electrical Plumbing (MEP) system a lot of unnecessary costs. This situation could be solved simply by using a collaborative approach.

A second advantage could be identified in the use of the BIM to make further considerations on the suggested operational proposals. Complexity is an essential theme in the Architecture Engineering and Construction industry. This aspect, which should be taken in consideration, makes design choice difficult, because it is not based on the best solution, but on what better fits a specific project. Strategies, defined each time, also have to take into consideration the European Procurement Directives of 2014.

BIM has already played an important role in the United Kingdom for several years with the aims to capitalise on the success of UK programme based on the BIS BIM Strategy and to take on a global leadership role in BIM exploitation, enhancing the global image of UK designers, contractors and product manufacturers which in turn will translate into winning new work, growth opportunities and increased employment.<sup>(90)</sup> Such strategies are aimed at increasing the authorities' freedom of choice, but in the meantime, they are affording them more empowering skills. In this way, the owner (helped by his consultants) defines criteria upon which to evaluate the design choices, based on specific and promptly defined needs. In this way, a solution is selected by making a decision based not on a single aspect but on a multi-criteria analysis.

This technique is able to provide the best solution – in terms of building techniques and costs – through a BIM approach automatically tailored to the owner's needs.

One of the main aspects related to BIM is the correlation between graphical and non-graphical information, in this way the project could be validated through an index created on particular requests of the owner. This fact could lead to obtain a specific but objective evaluation of the project (such as cost, time, energy efficiency and so on). These evaluations can provide a continuous overview of the evolution of project, not based on the remaining time until the completion, but rather on the owner's satisfaction.

#### 4.4. Shared risk and rewarding

The sharing of the profits, at least in the U.S. and British experience, seems to provide a monetary reason to collaborate.<sup>(91)</sup> In other countries, such as

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<sup>(90)</sup> HM Government, "Industrial strategy: government and industry in partnership – Building Information Modelling", 2012.

<sup>(91)</sup> Association of Consultant Architects, 2010, 10 Years of Partnering Contracts: PPC2000/TPC2005.

in Italy, the sharing of savings and profits would be contrary to the general principles of administrative action (such as cost-effectiveness), but the award of a so-called *premio di accelerazione* (a sum of money to be awarded in case of early completion of a work on the basis of the agreement concluded between the contracting authority and the constructor) would be considered as a good incentive to collaboration.<sup>(92)</sup> Even though the monetary remuneration is not the primary driving principle, without this factor collaboration is still possible.<sup>(93)</sup> One of the main points of Relational Project Delivery Arrangements is the sharing of pain and gain. This is possible thanks to an initial agreement that all the people involved in the contract have to sign. This imposes an ‘open book’ policy: in other words, it means that all the involved subjects have to share with the owner their ‘books’ so he need only reimburse the actual costs. This condition creates transparency in the teamwork. It also allows work to proceed safely and peacefully, because it is unfair to work below costs and the open book rule puts at risk only the profits which are under contract.

Risks are also present if the project goes in the wrong direction. In this case, all the stakeholders are responsible for the failure or incomplete success of the project. The concept, at bottom, is to accept these shared risks, in order to choose a good project team based on integrity, character competency and trust.<sup>(94)</sup>

The process starts from a business case, in which, at the beginning, the project costs are set at the validation stage. With the evolution of the planning phase, some improvements can be made and, this way, some savings can be produced. This is an iterative process, conducted by the Key Participants, aiming to maximize the global performance of the project. According to the validated goals, in order to maximize profits, the introduction of a change affects the whole project. The new benchmark is set to the lowest price, which becomes the final target cost for the construction phase.

When the contractor starts building the project, there could also be an incentive to the execution related to the site, which can produce a profit gain or loss. The division of the additional profit is based on a supplementary effort provided by the Key Participants and by the owner.

According to the conceptual models of Relational Contracts and Reputational games,<sup>(95)</sup> an actor should do his best if he will receive the same

(92) The so-called (speed prize) *premio di accelerazione* is provided for in Art. 145 of the new Italian Code of Public Contracts, Legislative Decree 50/2016.

(93) T. AMABILE, “A Model of Creativity and Innovation in Organizations”, *Res. Organ. Behav.*, 1988, pp. 123-167.

(94) O. MATTHEWS, G.A. HOWELL and P. MITROPOULOS, “Aligning the lean organization: a contractual approach”, *Lean Conference*, 2003, pp. 1-12.

(95) D.G. DE MAIO, “Relational Contracts and Reputational Games The Role of Informal Agreements”, *Supporting Business Relation*, 2013.

amount, just because he performed work that is compliant with laws and not at the best of his ability. However, it should be also noted that on the basis of the administrative principles of effectiveness and fairness, each party should cooperate in good faith and to the best of its knowledge.(96) The owner finds himself in a situation in which he pays a person just because he achieves his scope using the minimum of his capacity, therefore the concept of meritocracy should also be introduced in the remuneration aspect of contracts. Reputational contracts are able to introduce this aspect and inspire people to truly believe in their work.(97)

If the importance of reputation inside the group of participants under the cooperative contract is evident in the U.S. and British experience, it nevertheless recalls some key issues on the ability to evaluate reputation and past good performance in the EU procurement system.

From the EU public procurement standpoint, the EU Directives limit the ability to evaluate vendors' reputation in relation to procurement award criteria, as assessing past performance could turn into a procuring entities' discrimination. Such rules carry a risk of compromising the quality of the performance.

Indeed, a significant difference between the EU and the U.S. approaches to the evaluation of tenders/candidates concerns the relevance of past performances and the objectivity or subjectivity of the choice of the winning tender. From the EU standpoint, pre-qualification along with evaluation of the tenderers' capabilities (quality requirements of the economic operators(98)) constitutes the first phase of the award procedure, completely separate from the evaluation of the tenders/candidates.

In the EU, the choice has been to fix some grounds of exclusion (some of which may be optionally implemented by Member States)(99) and minimum standards of economic and financial standing and technical and/or professional ability, related and proportionate to the subject matter of the contract ('selection criteria')(100) in order for the tenderer to be allowed to participate in the contract competition. Any economic operators that meet or exceed the minimum requirement threshold must be admitted,(101) the reason for such a rule was the existing concern about the risk of discrimination in favour of

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(96) In this sense, *see* Art. 30 of the new Italian Code of Public Contracts, *Legisl. Decr. No. 50/2016*.

(97) J. LEVIN, "Relational Incentive Contracts", *Am. Econ. Rev.*, Vol. 93, No. 3, 2003, pp. 835-857.

(98) EC Dir. 2004/18, Art. 45-52, for the criteria for qualitative selection of the tenderer. In the 2014/24 EU Dir., *see* Art. 58.

(99) EU Dir. 2014/24, Art. 57.

(100) EU Dir. 2014/24, Art. 58.

(101) 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. *See* EU Dir. 2014/24, Art. 28.

national undertakings, and led to the exclusion in the EU Directive of the possibility to rate past performances and, in particular, the possibility of evaluating past performances with scores, rather than the pass/fail approach implicit in the EU approach to the assessment of potential contractors' eligibility.

The result, though, is that the EU neglects an important characteristic of contractors, their performance records on prior contracts. As a consequence, companies with poor records 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 risk has been considered unjustified, as not proportional and potentially discriminatory.<sup>(102)</sup> This lack of evaluation and the consequent inability to choose on the basis 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 in integrity.<sup>(103)</sup>

In the U.S., the order of evaluation is often reversed: first the tender is evaluated and only at a later stage the tenderer is assessed for 'responsibility' (qualification), 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).<sup>(104)</sup> That responsibility determination, however, is undertaken only with respect to one firm, the apparent winner of the competition.

The difference mainly concerns the EU's preference for objective, mechanically applied award criteria and the U.S. tolerance of subjectivity, both in the evaluation factors and in the trade-off between price and non-price factors.

In the EU legal framework, the objective evaluation of tenderers and tenders, especially in case of lower price award criteria, boosts the risk of poor

(102) UK Government, "Buying and managing government goods and services more efficiently and effectively", published 20 February 2013. EC Dir. 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 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*, case C-599/10; ECJ, 12 November 2009, *Commission v Greece*, case C-199/07; ECJ, 24 January 2008, *Lianakis v Dimos Alexandroupolis*, case C-532/06; ECJ, 3 March 2005, *Fabricom S.A. v Belgian State*, jnd cases C-21/03 and C-34/03.

(103) EU Comm., "Green Paper on the modernisation of EU public procurement policy towards a more efficient European Procurement Market", *op. cit.*, p. 18.

(104) S. TREUMER, "Exclusion, Qualification and Selection of Candidates and Tenderers in EU Procurement", in *Qualification, Selection and exclusion in EU Procurement* (M. BURG, M. TRYBUS and S. TREUMER eds), Copenhagen, Djøf Publ., 2016, pp. 13 and ff.

performance linked to the need to reduce costs during execution. Moreover, as already highlighted, the EU objectivity is often only mere appearance.(105)

In the U.S., during the evaluation of tenders, however, the tenderers' past performances 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 tenderers seems both anti-competitive and inefficient, since it requires the contracting authority to judge all firms on a pass/fail basis, thus allowing the contracting authority to eliminate firms from the competition before they have had the opportunity to submit a tender.(106) 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 approach, mechanical award criteria are applied.(107) According to EU public contracts rules, the award of a contract should be objective(108) in order to ensure non-discrimination among economic operators of different Member States.(109) Such a choice can be implemented with the simplest and most objective award criterion, that is the criterion of lowest price. The problem that the EU faces is to ensure objectivity in the evaluation of any other criteria, particularly when their use normally requires 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.

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(105) D.I. GORDON and G.M. RACCA, "Integrity Challenges in the EU and U.S. Procurement systems", in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally op. cit.*, p. 117.

(106) *Ibid.*; S. ROSE-ACKERMAN, *Corruption and government: Causes, consequences and reform*, Cambridge, CUP, 2010, p. 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".

(107) EC Dir. 2004/18, recital 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 Dir. on public procurement, *see* the recital No. 90.

(108) Dir. 2004/18/EC, recital 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* Dir. No. 2014/24/EU, recital 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".

(109) C.H. BOVIS, *EU Public Procurement Law*, Cheltenham, Edward Elgar, 2007, pp. 63-80.

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 kilometres, 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 numerical scores.<sup>(110)</sup> 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 in the case of assigning points based on the number of days needed for delivery), the trade-off between those factors and price is inherently subjective: if one tender would have the goods delivered in fifteen days and the other would take 20 days, how many additional euros 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 have induced some Member States<sup>(111)</sup> to provide for the use of mathematical formulas in the award of public contracts.<sup>(112)</sup> That is, the contracting authority has to determine a mathematical formula for both the assessment of the different criteria and the relative weightings used to determine the most economically advantageous tender.<sup>(113)</sup> 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 favour of one tenderer or another. The jury's assessment thus continues to have a discretionary (or arbitrary) content, and the mathemat-

(110) J. SCHULTZ and 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"; G.M. RACCA, "The Risks of Emergencies in Public Procurement", *J. Publ. Finance & Publ. Choice*, 2013, p. 105; G.L. ALBANO, "On the Problem of Quality Enforcement in centralized Public Procurement", *J. Publ. Finance & Publ. Choice*, 2013, p. 145.

(111) Art. 83, § 5, Law No. 163 of 2006, Italian Public Procurement Code, 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 (Presid. Decr., 5 October 2010, No. 207), Annex P.

(112) F. DINI, R. PACINI and T. VALLETTI, "Scoring rules", in *Handbook of public procurement*, *op. cit.*, p. 304.

(113) P.S. STILGER, *Formulas for Choosing the Most Economically Advantageous Tender – a Comparative Study*, thesis, Utrecht University, 2011.

ical formulas mainly serve to give a semblance of objectivity to a subjective evaluation.(114)

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.(115)

BIM could foster the EU public procurement system to ensure a more objective evaluation of tenders. Collaborative contracts should provide new requirements for groups of economic operators (temporary associations, joint ventures)(116) and a new set of award criteria for the evaluation of their offers. This choice might turn into a better monitoring of all the procurement cycle and in particular the final goal of the procurement selection that is a correct execution.

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(114) 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; *See*; Italian Authority for the Supervision of Public Contracts for works, services and supplies, *Determinazione*, 24 November 2011, No. 7; F. DINI, R. PACINI and T. VALLETTI, "Scoring rules", *op. cit.*, pp. 309-310.

(115) G.M. RACCA, "Collaborative procurement and contract performance in the Italian health-care sector: illustration of a common problem in European procurement", *PPLR*, 2010, pp. 119-133; G.M. RACCA, R. CAVALLO PERIN and G.L. ALBANO, "Competition in the execution phase of public procurement", *cit.*, pp. 89-108.

(116) In the UK, consortium bidding constitutes a particular form of collaborative contracts, in which two or more economic operators come together to submit a bid for a contract in a public procurement process either through an already established consortium or through a looser, dedicated group of bidders coming together for a specific contract and becoming formalized structures (such as special purpose vehicles) after the award of a contract. For more guidance on consortium bidding, *see* also Crown Commercial Service, "Procurement Policy Note – Reforms to make public procurement more accessible to SMEs", February 2015, No. 03, and PPN 2016, No. 08, which replaced PPN 2205 No. 03, to provide guidance on the Standard Selection Questionnaire, including how this should be completed and evaluated to ensure consortiums are not disadvantage.

#### 4.5. Decision making in Relational Projects Delivery Arrangements

From the private sector perspective, as recalled by the American Institute of Architects (AIA), “Integrated Project Delivery allows all team members to better realize their highest potentials while expanding the value of the provider throughout the project lifecycle”. It is therefore possible to deduce that integration is the key element.(117) All decisions should be based on (i) the best quality, (ii) the lowest cost in general and (iii) the least impact on the project. After signing the contract, everyone in the team has the same power to make decisions, even the owner. The same logic is used to fill in all the available positions, using the most suitable person from any of the Primary Team Members (PTM). Joint Project Control (JPC) requires collaboration between stakeholders. When problems arise, they must be thoroughly explained to the parties, in order that they understand how to solve the issues. In this way, the resolution is handled through a discussion and agreement between Primary Team Members.

A Collaborative Contract has the ability, due to its form, to align the participant goals and reduce project variability in terms of cost and performances.(118) AIA also underlines how important it is to change the way of looking at the construction industry, because now the project has a scope of quality and the project management team has the scope to lead the parties toward the achievement of the agreed objectives. The ‘policy of age’, in which the eldest rules, undermines the relationship between team members and forces the group apart. The owner is involved in the project, because, much like the other parties, he has an interest and he should collaborate to obtain the best result possible. The owner still has the power, but all decisions have to be discussed ‘democratically’. This change in the mind-set, especially for the owner, is very difficult, due to a tradition in which the owner has a great power and its words and opinions correspond to the rules, even if its decisions are not for the best interest of the operation. The involvement of the owner in the Integrated Project Delivery gives major advantages to this collaborative contract.

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(117) N. AZHAR, Y. KANG and I. AHMAD, “Critical Look into the Relationship between Information and Communication Technology and Integrated Project Delivery in Public Sector Construction”, *J. Manag. Eng.*, 2014, p. 31; N. AZHAR, Y. KANG and I. AHMAD, “Factors Influencing Integrated Project Delivery in Publicly Owned Construction Projects: An Information Modelling Perspective”, *Procedia Eng.*, 2014, No. 77, pp. 213-221.

(118) G. BALLARD, R. AZARI, Y.-W. KIM and S. CHO, “Starting from Scratch: A New Project Delivery Paradigm”, in *Construction Research Congress* (D. CASTRO-LACOUTURE, J. IRIZARRY and B. ASHURI eds), Atlanta, ASCE, 2014, pp. 2276-2285.

#### 4.6. Liability among Contract Parties

While there is no need for contractual exclusions or limitations of liability by reason of adopting BIM,(119) there are factors linked to BIM that, in practical terms, reduce liability: increased communication, greater creativity and reduced contingencies.(120)

In this way, some studies have underlined how liability adds hidden costs to the project as a consequence of the self-defence mechanism of every participant and induces people to use common and tested theories or materials which are – in most cases – more expensive. Increased communication through BIM forces participants to take responsibility for the project, instead of blaming others for any errors or failures in the project. In this way, all parties can either benefit or suffer from the results of the project and eliminate the anxiety in and around communication. The reduced liability is a condition that forces participants to take responsibility for the project, rather than attempting to blame others trying to avoid the impact of the problem caused.

One of the main causes of errors is disinformation triggered by incorrect communication, provided by one party to another. It is important that the flow of data is correct. In Relational Projects Delivery Arrangements, all the Key Participants have the duty to communicate and transmit all their knowledge for their own benefit.

Project participants (particularly the design professionals) have become keenly aware of the importance of providing early and complete information to contractors, as the builders cannot effectively plan without an understanding of where the designers are headed.(121) It is possible to assume that designers try to deliver data as complete as possible in order not to receive a claim by the constructor, but without allowing a continuous exchange of information. Key participants should be continuously informed of the project evolution in order to update and inform the others of potential unforeseen consequences. BIM might provide the solution to achieve a coordinated collaboration in real time through an oriented software, which would also allow a continuous evaluation of the project.

A direct consequence of the sharing of information among the participants to a specific project is the problem of the intellectual property rights in each set of data included in the model shared between different companies. Sharing

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(119) See *Enabling BIM Through Procurement and Contracts – A Research Report by the Centre of Construction Law and Dispute Resolution*, London, King's College, 2016, p. 7.

(120) Association of Consultant Architects, 2010, 10 Years of Partnering Contracts: PPC2000/TPC2005.

(121) D. MOSEY, *Early Contractor Involvement in Building Procurement. Contracts, Partnering and Project Management*, Hoboken, Wiley Blackwell, 2009.

policies could have huge consequences for the owner, which could not receive the product in a digital way. However, since most of the work delivered to a customer is tailored to its needs, the digital delivery of a project does not imply selling the knowledge of a firm. In this sense, BIM is better described as a container of information allowing the owner to better manage its building than as a way for the owner to enrich its own knowledge.

From an EU public procurement perspective, contracting authorities have to ensure the compliance of data and information sharing with EU principles of transparency, equal treatment and non-discrimination in terms of prior involvement of economic operators and for the benefit of the award procedure. In fact, even if early involvement in the construction sector mainly involves the post-award phase, in which the designer/constructor may decide to open a competition among different providers – another profile which would deserve a thorough analysis in terms of compliance with EU public procurement law – it is nevertheless true that contracting authorities should be clear from the outset with regard to the intention to use electronic tools in the award of the contract when engaging with economic operators.

This requires that a possible phase of preliminary market consultation<sup>(122)</sup> should not distort competition and that the same information is accessible to all economic operators and its outcomes are disseminated. The lack of transparency in the contracting authority's activity from the very beginning can make it challenging for economic operators (especially innovative SMEs) to identify the demand for innovation and the ability to propose the best solutions.

Contracting entities should define the requirements of participants and the kind of early cooperation they aim to settle with all the subjects involved in the design execution and management of the subject matter of the procurement. The BIM methodology should require further efforts in this perspective, especially because BIM could affect duties of care agreed under contract or imposed by law. It is therefore necessary to frame appropriate and enforceable legal commitments accordingly.<sup>(123)</sup>

During the award procedure, all communication and information exchange should be performed using electronic means of communication in accordance with the requirements of EU Directives on public contracts, and in the construction sector this could evolve into the use of BIM methodologies. Such tools might provide the necessary environment to start the sharing of information for the purpose of the selection of teams for the collaboration contracts. Such instruments should be non-discriminatory, generally available

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(122) EU Dir. 2014/24, Art. 40.

(123) See *Enabling BIM Through Procurement and Contracts – A Research Report by the Centre of Construction Law and Dispute Resolution*, *op. cit.*, p. 7.

and interoperable with the ICT products in general use and should not restrict economic operators' access to the procurement procedure.(124) The rapid evolution of technologies would overcome such barriers, and also provide a technical environment that could leave legal obstacles among EU Member States and favour collaboration also in cross-border procurement.

#### 4.7. Teamwork and New Project Delivery Phases

The concept of teamwork should be revisited and adapted to the perspective of collaboration contracts, also in the private sector, and then tailored to public procurement needs. This consideration suggests a cautious choice of the members of the group. The aim is efficiency,(125) but most of the time a disagreement can compromise the entire collaboration. It is really important to carefully select the participants of the group, because the impact on the development of the project in a collaborative teamwork environment is very different compared to a traditional process due to the continuous changes caused by the other components of the team. The differences that persist between teamwork working in the manufacturing and in the AEC sectors is that in the former the components work together for an extended period of time, while in the latter, the components change from one project to another.(126) This fact entails a high risk of lack of cooperation between people who do not truly believe in the collaboration itself.(127)

Increased collaboration is transforming the nature of project delivery. This is the reason why Integrated Project Delivery is a collaborative and trust-based process. It is innovative both in the structure and in the delivery phases, as it also requires a contribution of knowledge and experiences from different stakeholders. This change is caused by working simultaneously, having the same data available through BIM.

The first phase is called 'Conceptualization', where key participants identify the main objectives related to costs, performances, time and preliminary analysis. During the following step, 'Criteria Design', the project takes shape in terms of design, while all the activities that have been commenced continue. In the 'Detailed Design' all the decisions are finalized including finishes, fixtures and equipment and the subcontractors are integrated in the process. The 'Implementation Documents' phase is an implementation of the previous one in terms of information related to the project.

(124) EU Dir. 2014/24, Art. 22 (1).

(125) H.W. ASHCRAFT, *Location, Location, Co-location*, San Francisco, [publisher?], 2016.

(126) F. DANIEL, K. LAURI, D. FORGUES and L. KOSKELA, "The influence of a collaborative procurement approach using integrated design in construction on project team performance", *Int'l. J. Manag. Proj. Bus.*, 2009, 2, pp. 370-385.

(127) M. OH, J. LEE, S.W. HONG and Y. JEONG, "Integrated system for BIM-based collaborative design", *Autom. Constr.*, 2015, 58, pp. 196-206.

BIM could be developed in parallel during the process, providing the digital representation of the physical and functional features of a building essential to develop a collaborative process exchanging information among parties and to resolve conflicts.

A traditional way of design is not compatible with this innovative collaborative process due to its own foundation, because it includes key figures that do not allow for working together, sharing information and optimizing the project.

The next two simultaneous phases are 'Agency Review' and 'Buyout': the former allows reviewing and validating the design process according to the laws in force and the latter is the payment of the key figures. At the end, the building is built in the 'Construction' phase, where all the benefits of the integrated model are delivered to the owner.(128)

Recently, Integrated Project Delivery has become a milestone for some companies, which were established a few years ago, even if it is still an 'infant', as defined by AIA. Therefore, with the help of these companies, it is possible to discover more data to better understand the real performances and limits of Integrated Project Delivery, inferring as much as possible information from completed projects that are still underway.

#### 4.8. Building Information Modeling challenges

The BIM methodology is the easiest way to perform an effective collaboration between all the stakeholders, allowing a permanent coherence through all the project parties. According to the International Council for Research and Innovation in Building and Construction,(129) it is one of the key elements to perform an Integrated Process. To this end, the very first step is to identify the stakeholders' roles and the project goals and to define an implementation strategy accordingly. The more BIM is aligned with the project goals, the more it can maximize the value of a project within the constraints of available time and resources over its lifecycle.(130)

BIM is an actual collaboration of people involved in the construction process. With the evolution of technologies, all team members have the ability to interact with each other in a Common Data Environment (CDE), which is the virtual space where the work group shares information and data related to the

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(128) R. CHENG, K. DALE, A. ASPENSON and K. SALMELA, *IPD Case Studies*, American Institute of Architects, San Francisco, American Institute of Architects, 2012.

(129) IDDS, *Research Roadmap Report*, International Council for Research and Innovation in Building and Construction, 2013. The dissertation represents the legal framework in which Building Information Modeling can be applied.

(130) D. SHEPHERD, *BIM Management Handbook*, Newcastle Upon Tyne, RIBA Publ., 2010, p. 9.

evolution of the project<sup>(131)</sup> following predefined procedures. This space allows all team members to be updated with project information, which is uploaded by each member and permits not only the sharing of information, but also the monitoring of the process, with a structured workflow.

To emphasize the spirit of collaboration of BIM and according to the mandatory requirement of the MIDP,<sup>(132)</sup> the project manager should appoint the people responsible for the various activities, who would be expected to be informed about what is going on and responsible for validations and signatures.

In 2011, the UK Government Construction Clients group published a report, in which it required small changes in the copyright law and contract form to facilitate the introduction of Level 2 of BIM maturity. It stated that collaboration should be mandatory in a BIM environment, but this methodology did not affect the procurement scenario. This CIC/BIM protocol defined a series of supplementary contractual documents, which constitute the basis of a legal framework, such as: (i) Employer's Information Requirements (EIR), (ii) BEP (BIM Execution Plan) pre and post contract and (iii) Project Procedures. The Employer's Information Requirements (EIR) has the double scope of (i) specifying the ultimate aim of the asset, with the consequent development of the Project information Model (PIM), and (ii) informing the Asset Information Requirement (AIR). The Organizational Information Requirements (OIR) – the compensation of the Plain Language Questions in the Asset Information Model (AIM) – generates the AIR, and all is then merged in the Asset Information Plan. The initial contract can be located in the documents' sphere drawn up by the client, upon which it relies for the professional management of work through BIM.

In 2013, the Construction Industry Council (CIC) developed Publicly Available Specifications (PAS) aimed at meeting an immediate market need following guidelines set out by British Standards Institution: the PAS 1192:2 and the PAS 1192:3. The first specifies the requirements for achieving 3D environment-based BIM during the capital/delivery phase of projects throughout the stages of the information delivery cycle, culminating in an as-constructed asset information model (AIM), thus identifying the downstream uses of information at the outset to ensure its re-use during the whole building life cycle. The latter lays down "Specification for information

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(131) British Standard Institution (BSI), PAS 1192-2:2013, "Specification for information management for the capital/delivery phase of construction projects using Building Information Modelling", *Br. Stand. Inst.*, 2013.

(132) Construction Industry Council, *Building Information Modelling CIC | BIM Protocol*, 2013, Cic 1–15.

management for the operational phase of construction projects using building information modelling”.

For managing the delivery of the project, the PAS 1192 foresees a BIM Execution Plan (BEP), which is divided in pre-contract BEP and post-contract BEP. The first one is developed by each potential contractor and defines the potential added value that it can provide to answer the Employer’s Information Requirement. The last one is drawn up after the conclusion of the contract, confirming the ability of the supply chain and providing a Master Information Delivery Plan (MIDP).<sup>(133)</sup> Further, Project Procedures explain all the correct workflow and methodology to follow during the project development stages. For instance, the Project Information Model (PIM) developed on the basis of the Exchange Information Requirements (EIR) during the design and construction phase – consisting of a federated building information model, non-graphical data and associated documentation – contributes to the creation of the Asset Information Model (AIM), which compiles the information necessary to support asset management providing all the data related to, or required for the operation of an asset.<sup>(134)</sup>

In this process, the BIM Information Manager plays a key role, since it ensures the quality of the provided data, and realizes value through its management. His work is based on the Project Information Plan and Asset Information plan, enabling the integration of information in the Project Team. The transformation of pre-BIM contractual forms needs to be defined to accommodate the methodology in several regards: (i) liability and insurance – insofar these are not dealt with when working in a BIM environment; (ii) the ownership of BIM model and data; (iii) integrity of model and data; and (iv) secure storage of data. These points should be resolved, otherwise the contract itself would leave the parties subject to liability. The use of traditional contracts such as JCT or other forms not specifically designed to work with BIM may lead to the possibility of its incorrect use, with all the consequent issues.

From a public procurement perspective, the advantages in terms of efficiency and integrity seem evident and might be outlined as long as the contracting authority actually has precise control of all the phases, especially the definition of needs and of public demand, but also in the selection of participants (tenderers/candidates) and of the group that will cooperate in the contract execution.

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(133) *I.e.* a primary plan, which sets out when project information is to be prepared, by whom, using what protocols and procedures.

(134) According to the PAS 1192-3 the operation of built assets shall ensure continuity and consistency in the management of information for both planned and unplanned events that may occur during the operation, maintenance and management of an asset, and it covers the data transfer process required for the creation of the AIM.

The different EU and U.S. perspectives on the modalities of cooperation are flanked by a parallel variety in public procurement objective/subjective selection of contractors. From this perspective, the use of BIM methodologies may have a huge impact in terms of transparency and effectiveness of the selection.

The U.S. federal government now routinely allows ‘trade-off’ contracting decisions (called ‘best value’ decisions), in which contracting officers are allowed to make subjective selections among competing tenders, rather than selecting only on the basis of price.<sup>(135)</sup> U.S. government agencies are permitted to use price as the sole criterion in selecting among acceptable tenders, and they sometimes do so. Nevertheless, non-price selection criteria are also permitted. What is even more noteworthy is that the U.S. system grants agencies broad discretion in selecting and assessing non-price criteria.<sup>(136)</sup>

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,<sup>(137)</sup> without objective criteria. Generally, 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 performances was often based solely on prior work identified by the bidders in their tenders. In their submissions, 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 government officials to identify prior contracts without reliance on the tenderer, thus reducing the risks posed by the vendors’ sometimes biased disclosure of contracts where past performance was good.<sup>(138)</sup>

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(135) D.I. GORDON and G.M. RACCA, “Integrity Challenges in the EU and U.S. Procurement systems”, *op. cit.*

(136) 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 *Corruption and Conflicts of Interest. A Comparative Law Approach* (J.-B. AUBY, E. BREEN and T. PERROUD eds), Cheltenham, Edward Elgar, 2014, pp. 42-43.

(137) In a 2012 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 a 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.*, 1 May 2012.

(138) 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 – FAPIIS) and may be used in future

Second, the U.S. system allows trade-offs between price and non-price factors to be subjective. The acceptability of subjective trade-offs has been recognized at least as far back as the 1970s, when GAO declared that contracting officers had discretion in making trade-offs among competing bids, as long as their decisions were consistent with the publicly announced evaluation criteria and met the test of rationality.<sup>(139)</sup> That means, for example, that, where a solicitation advised that the government would have weighted price and past performance equally, two contracting officials could reach different – but both permissible – trade-off 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 was not 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 has chosen the winner). Nonetheless, the award is subjected 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.<sup>(140)</sup>

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source selection decisions. See K.M. MANUEL, Congressional Research Service Report for Congress, *Evaluating the “Past Performance” of Federal Contractors: Legal Requirements and Issues*, 4 February 2013, [www.fas.org/sgp/crs/misc/R41562.pdf](http://www.fas.org/sgp/crs/misc/R41562.pdf).

(139) The seminal GAO decision establishing this principle was *Grey Advertising, Inc.*, 55 Comp. Gen. 1111 (1976), 76-1 CPD 325.

(140) D. DELLA PORTA and A. VANNUCCI, “Corrupt exchanges: Empirical themes in the politics and political economy of corruption”, paper prepared for conference, Bielefeld, 2001, classify the need for 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*, Bergen, Chr. Michelsen Institute, 2002, p. 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, op. cit.*, p. 18. “Whenever regulatory officials have discretion, an incentive for bribery exists”.

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The BIM methodology could allow further monitoring systems related to the collaborative contracts that might permit a check on all the phases and possible criticalities, and to settle them with greater transparency and efficiency. In the end, successful use of BIM is very much related to the ability to align its use with the procurement model and contract terms.

### ***5. Integrated Project Delivery and Culture of Collaboration***

Collaborative contracts in the US started a long time ago, as a method distinct from the traditional Design-Bid-Built. Even public administrations started using a different form of tendering. This new form is called Integrated Project Delivery. Integrated Project Delivery still does not have a final and unique definition. There are a few definitions, just as a reminder, by the American Institute of Architects (AIA) and the National Association of State Facilities Administrators, but they all include the same principles: (i) multi-party contract; (ii) early involvement of all the parties; (iii) shared risk and reward; (iv) collaboration; (v) reciprocal trust; (vi) joint development.

The American Institute of Architects defined Integrated Project Delivery as a “method distinguished by contractual agreement between a minimum of owner, design professional and builder where risk and reward are shared and a stakeholder success is dependent on project success”. The transformation from a traditional contract to an Integrated Project Delivery agreement imposes an additional shift in order to fulfil the contract.(141)

Due to their structure and composition, traditional contracts unavoidably create a conflict of interest and they impose a rigid division of the stakeholders’ works.

The two main standard contracts developed in the US, which can help establish a real collaboration through a multi-party integrated project delivery agreement, are AIA C191 and Consensus Docs 300 series. The integrated agreement creates a system of shared risks, with the aim of decreasing total risks of the entire project.(142) In Integrated Project Delivery most of the consultant and sub-contractors have to join the agreement. A general rule is to have at least half of the construction costs discussed at the decision table. There are two ways to add new subjects to the team: the first is through sub-agreements, as part of the Integrated Project Delivery contract but with the

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(141) N. AZHAR, Y. KANG and I.U. AHMAD, “Factors Influencing Integrated Project Delivery in Publicly Owned Construction Projects: An Information Modelling Perspective”, *Procedia Eng.*, 2014, No. 77, pp. 213-221.

(142) W.A. LICHTIG, “The Integrated Agreement for Lean Project Delivery”, *Improving Healthcare through Built Environment Infrastructure*, pp. 85-101.

same rights, duties and just a limitation in the voting rights. The second is through joining the agreement, with a consequent amendment to the original version.

The American experience has demonstrated how public administrations prefer a joint entity before a contract is stipulated in which the party is entrusted to design and/or build a project. This is one of the main reasons why framework alliancing was created.

### 5.1. A Focus on the European Experience on Collaboration

The analysis of the European experience on collaboration should follow three key elements:(143) (i) integrated processes, (ii) inter-operable technologies, and (iii) collaborating people. Integrated Design and Delivery Solutions need collaborative work processes and enhanced skills, with integrated data, information, and knowledge management to minimize structural and process inefficiencies and to enhance the value delivered during design, build, and operation, and across projects.

Collaborative contracts could reflect different schemes, depending on the specific legal order and on the types of relationships that suppliers would intend to enter into, given the competition rules that govern the market and the procurement terms. Generally, consortium bidding might imply a mandate, a temporary association, a consortium or a joint venture, whether corporate or contractual.

That acknowledged, the implementation of BIM might require a significant societal, technological and legal change, especially in the procurement sector, and a step further in collaboration in order to include all the relationships between suppliers under a common framework alliance.

An alliance is a collaborative and integrated team brought together from across the supply chain. The team shares a set of common goals aligned with customer and client outcomes and work under common incentives.(144) During the past years in the United Kingdom many proposals were made to ensure a well-structured collaboration through the supply chain. English contract law constitutes the historical basis of the American contract law. In the same way, it is possible to affirm that both cultures created a series of standard contracts to support collaboration. (FAC-1, NEC4, JTC)

In Europe, the collaborative approach is quite new in the Architecture, Engineering and Construction sector. Actually, it would be more accurate to say

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(143) According to Integrated Design and Delivery Solutions, 2013, on the International Council for research and Innovation in Building and Construction, 2009.

(144) Infrastructure Client Group Alliancing Code of Practice.

that there is no such thing as a European approach, as many European countries are trying to import in their procurement systems the British approach to collaborative contracts. A new standard of contract, PPC2000(145) was created at the beginning of this century: used in the last few years, it had a great usage in the private sector and it was also validated by many companies and by the UK government. This document is close to IPD conceptualization, as it is a contract which includes (i) the aggregation of the team, (ii) the entrusting of the project, and (iii) the construction phase. Sometimes, a last point is added: maintenance.

Shared objectives, success measures, targets and incentives are the core of the framework alliance, especially in the FAC-1, which can take a multi-party or poly-party configuration according to a case-by-case evaluation. This collective agreement model was introduced in 2016 in the United Kingdom and has been used for many public and private projects, such as in the case of the construction of popular homes in the *Epping Forest* district for a total value of GBP 25 million.(146) The alliance has a joint aim, the realization of a project guarded by the governance structure of a core group. FAC-1 has been the first contractual model in Europe able to accommodate all the characteristics of this methodology and combine the Architecture Engineering and Construction sector in a single entity. It was adopted in its first year in over 12 B£ of procurements. At present, some States such as Brazil, Bulgaria, Germany and Italy are adopting this contractual form. Actually, among these States Italy is the only country that has imported FAC-1 in its legal system, thanks to the collaboration among different universities.(147) However, still at present in Italy there are some obstacles that are deeply rooted in the stakeholders' mindset regarding the underlying logic and actual implementation of collaborative agreements: on the one hand, the standardization of contracts is undervalued; on the other, economic operators do not often see the contract as a tool capable of facilitating economic and commercial relations.(148) This is even truer if the collaborative agreement is based on the English and American model of hyper-detailed contracts with many annexes and definitions. Since economic operators are not yet used to collaborative agreements and a unified approach is still lacking in the construction sector, the scenario is fragmented in as many contracts as the professions involved in the project; static, as it is focused in the

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(145) Association of Consultant Architects, 2010, 10 Years of Partnering Contracts: PPC2000/TPC2005.

(146) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, op. cit., No. 3.

(147) *Ibid.* For more information, see also the Web site of the Center of Construction Law and Management and the Italian reference point for FAC-1.

(148) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, op. cit., No. 3.

individual contractual relationship, losing touch with the surrounding context; occasional and not qualified, as the content of the contract and its clauses are uniquely determined by the contracting authority for its own advantage.<sup>(149)</sup> By encouraging the process of *alliancing* – which would include all the parties in a unique contractual framework containing goals, aims and timeframes, without substituting the individual service contracts signed by each professional involved – the legislator can seek to safeguard the legality of the contractual relations, the control over public expenditure, the reduction of variants and errors, and the emergence of extra costs in the execution phase.<sup>(150)</sup> The framework alliance is able to accommodate any potential change in the collaboration from the addition of a new member to the sharing of benefits, through a standard format. The benefit which derives from a pre-defined standard is to have all the possible situations already assessed by the drafters.

## **6. Comparison among different Contract Procedures in the Private Sector and challenges for their application in Public Procurement**

The aim of a collaborative contract is to enable and develop collaboration between the owner, the designer and the builders.

In this private sector perspective, the evolution of new technologies and of collaborative processes used in the US and the UK has generated an increase in productivity and a decrease in time wasted in the design, construction and operational phases. That is the reason why BIM and collaborative contracts are conceived to work on the same project, reducing the Architecture Engineering and Construction industry fragmentation. The basic concept underlying these three forms of collaboration is essentially the same, the difference consists in the timing.

Project partnering is an alliance among different parties, typically designers, participating in the tender processes. After that, a second contract is signed to make the construction or the design, but it does not impose a strict collaboration and a complete change of mind-set in the conception of the model. It could be applied to a Design Build process and the collaboration made transversally to the supply chain. It does not require any of the previously described characteristics. This contractual form could be the closest form of traditional approach to a Relational Projects Delivery Arrangement. The advantages of

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<sup>(149)</sup> *Ibid.*

<sup>(150)</sup> *Ibid.*

this contractual form are that the counterpart is known in advance. Conversely, in the partnering there are no advantages in improving the project to better tailor to meet the owner's needs, as there is no alignment of goals nor other collaborative practice.

The second type of collaborative procurement is Integrated Project Delivery, a method that was developed in the late 1980s in the United States, and it was the first complete collaborative contract, which fits all the parties involved within a single scope, which is the construction of an asset. Integrated Project Delivery is a contract that can work alone without any other agreement. It is designed as a collaboration form defined in any part. This method was also imported into the UK in the form of PPC2000 as a concept, but it was very difficult to import it in public tenders. The reason is that with a single contract there is a group of key participants, who know each other in advance, and combine themselves in a single group, making the implementation of a classical tender process harder. A further evolution of this contractual form is framework alliancing, which is an agreement able to link more contracts together even if they were initially designed as traditional bilateral contracts. It basically is an alliance, which crosses the individual agreements. Therefore, this approach is more adaptive and can be applied in many cases and to most of the current standard forms. Collaboration can be added as a value to contracts that are not originally thought of as collaborative. At the beginning, traditional contracts have a process flowchart, which starts from the owner, through the design team and, only at the end, builders engage with the project. It is a linear and unidirectional process and team members do not have other ways to communicate. In contrast, the collaborative approach requires that participants work together when issues arise. Everyone should pursue the same scope. The framework alliancing introduction, in our system, is the way to engage the constructor role from the beginning of the project, hence all the team members can work to obtain a better building in a cheaper way. In the coming years, every country will have to deal with the problem of introducing this contract typology in order to solve the construction paralysis. Relational Project Delivery Arrangements establish a new approach to the management of construction procurement.

The two approaches analysed so far represent two completely different methods. In particular, the former, represented by Integrated Project Delivery, is an all-embracing contract between all the parties and it can subsist by itself. On the contrary, the second one, represented by FAC-1, is a meta-contract that encompasses the pre-existing ones; hence it cannot subsist by itself. The former needs to be created in a bureaucratic system that would allow it (e.g. the State of Massachusetts does not). On the contrary, the second one could be applied to

create a legal status that includes previous contracts and allows all the parties involved to communicate and have interactions.

In the public procurement perspective, a pressing need is therefore to reorganize the tender process to accommodate a BIM approach in the relevant legal order.<sup>(151)</sup> This restructuring should take into account a computational view of the contracts based on collaborative processes instead of a traditional opportunistic scheme (*i.e.* DBB). This change leads to a transformation of behaviour and improves the performances of the sector.

BIM methodology thus requires a drastic modification of traditional approaches to the construction sector in all the process stages, especially in the contract framework. To accomplish this digital transition, the Architecture Engineering and Construction sector has to accommodate different contract procedures, either in the private and public sector, in order to reduce the risks of litigation and projects' variants.

There is a cultural gap that slows down the collaboration, which needs to be filled and requires clarification to be addressed.

Although the experiences in the private sector seem to be much more advanced in comparison with those in the public sector, the perspectives opened by BIM methodology and collaborative contracts appear to fit to the issues that arise in the public procurement sector and thus might favour a quick adoption of such new contractual models that overcome the opportunistic divergences between the public and private parties.

In the EU legal system, as initiated in the UK, the public procurement sector should adapt procurement policies and strategies to such a perspective and favour cooperation with the purpose of obtaining the correct execution of the contract and not only a formally compliant award procedure.<sup>(152)</sup> To this end, the UK Government, pursuant to its 2011 Government Construction Strategy as subsequently updated in 2016, initially recommended the following procurement models: (i) *Cost-Led Procurement*, implying the use of a framework mini-competition to obtain proposals for savings and improved value, within stated cost ceilings, prior to team selection and appointments; (ii) *Two Stage Open Book*, implying the use of pre-construction phase conditional

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(151) As per UK legal order, see UK Government Trial Projects, as reported in *Enabling BIM Through Procurement and Contracts – A Research Report by the Centre of Construction Law and Dispute Resolution, op. cit.*, Chap. 10, “Evidence of links between BIM, procurement and contracts”.

(152) The recent publication of the regulation UNI EN ISO 19650-1 and -2, which in addition to EIR – Exchange Information Requirements has introduced AIR – Asset Information Requirements and OIR – Organization Information Requirements, shows that the direction is more and more to consider any single procurement as part of long-standing investment plans pursuing public purposes within budget constraints. This way the logic behind the drafting of a provisional budget should be adjusted to comply with Digitally Enabled Portfolio & Programme Management too. The contracting authorities are then expected to meet such changes and prepare to accommodate BIM methodologies into their procedures.

appointments of the team to obtain proposals for cost savings and improved value, within a stated budget, after selection but prior to construction phase appointments; (iii) *Integrated project insurance*, implying the use of project insurance without recourse, including cover for design problems and cost overruns, to create a no blame culture and obtain additional proposals for savings and improved value.(153)

The so-called FAC-1 model was developed to let the private and public sector introduce framework alliancing – which can work with different contract forms – in standard procedures. Its aim is to directly connect different parties, allowing transparency, which fits in BIM and in joint work, being essential in a collaborative system.(154) BIM cannot be applied to every form of contract though. FAC-1 provides a way to link in a single multi-party agreement the content of each bilateral contract. This means that any kind of two-party agreement, stipulated in a traditional form, can bring collaboration to a project. This framework alliance can be defined as an adaptable form. If project stakeholders are not ready to establish a full multi-party framework alliance, they might enter into a linked FAC-1 with each appointed consultant, contractor, supplier or provider. Generally, such a model should be compatible with any project procurement model that would use its direct award procedure and competitive award procedure.(155)

The framework alliance model has benefited from errors that occurred in other frameworks and alliances. In particular, it builds the improvement of PPC-2000, with the aim of including collaboration through different projects, supporting the improvement of working practice.(156) According to a report published by the Centre on Construction Law and Dispute Resolution, the new standard introduced two main differences compared to the previous one. The first is the introduction of BIM in the public procurement procedure with its technological advantages. The second is the possibility of introducing a transversal supply chain. Such a model might be developed in a more sophisticated system of integrated framework agreements, to evaluate and incentivize the participant suppliers (foremost SMEs). Specifically, this strategy could be realized through a structured division in lots of the contracts that might be included in a framework agreement, or defining, within the agreement, the

(153) See *Enabling BIM Through Procurement and Contracts – A Research Report by the Centre of Construction Law and Dispute Resolution*, op. cit., pp. 29-30.

(154) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, op. cit., No. 3, that refers to a recent tender by the *Unione dei Comuni Adda Martesana*, in Italy, for the construction of a new school in the Municipality of Liscate.

(155) D. MOSEY, “FAC-1 Framework Alliance Contract Briefing Paper”, London, King’s College, Centre of Construction Law, 2016, p. 6.

(156) Architects, T.A.I. of, 2007, *Integrated Project Delivery: A Guide*, Canada Mortgage and Housing Corporation.

inter-relationship between the private operators and the sub-suppliers in order to manage the supply-chain at tendering stage. This alliance, like other collaborative contracts, might allow the parties to achieve a target shared between team members.

The best practice is the line guiding the evolution of the project. The idea behind such alliance models seems to be the improved value and improved working practices as a result of the use of systems of supply chain collaboration that include in the framework agreement different, yet coordinated contracts, so that the strong negotiating position of the private economic operator upon the subcontractors can be coordinated at the very first phase, and better conditions and incentives for the timely and correct execution of the contract can be ensured. The development of adapted models of alliances could in fact establish mutual commitments related to each lot of the framework agreement.<sup>(157)</sup> Different models might be developed according to National legal systems, providing different sets of relationship among the suppliers included directly in the framework agreements. Such model might favour SMEs in entering directly the multiple framework agreement obtaining directly their role in the contract execution and reducing the sub-contracting issues.

In such models a key role might be played by the Alliance Manager, with the task to coordinate all the participants in the framework agreement. The Alliance Manager should be an impartial subject characterised by a strong commitment with the public administration to solve the problems of the core-group and pursuits to efficiently carry on the execution of the contract. The success of the project is connected to the selected actors, while the maintenance of the working relationships can increase the group productivity and their index of productivity, being understood that the termination of any of such working relationships would provide a further incentive for the execution of additional lots of the framework.

Obviously, such contractual models should be consistent with the public procurement principles of transparency and non-discrimination and be able to face the challenges of innovation and smart contracting that imply technologies and capacity as recently outlined by the EU Directives. Such a perspective might also favour horizontal administrative cooperation among procurement agencies that could define a new strategy of cross-border procurement and overcome legal barriers for the benefit of EU citizens.

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(157) D. MOSEY, "FAC-1 Framework Alliance Contract Briefing Paper", *op. cit.*, p. 2; S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, *op. cit.*, No. 3.

## 7. Conclusions

Technologies are shifting the way public procurement is implemented, making it simpler to develop aggregations both on the demand and the supply sides, with an important increase of the level of transparency, efficiency and predictability – thanks to the possibility of sharing data and information that could eventually limit the risks of information asymmetries. In this trend, BIM methodology plays a crucial role insofar as it pushes the adoption of collaborative contracts. In the EU, technologies are considered tools potentially capable of improving the internal market of public procurement, in so far as they could ensure greater participation, objectivity of the evaluation and efficiency in the execution phase.<sup>(158)</sup> The advanced use of digital tools, such as BIM, might lead to an effective revolutionary change in the procurement sector as it might make available a significant volume of data as never before. Because of that, the definition of public demand could be more precise, and the selection of participants more transparent and substantially objective. The significant volume of data acquired through the BIM and the coherence of the consequent information flow could even allow the structuring of smart contracts to coordinate the different relationships that would characterize the project implementation. This emphasises that the most strategic form of procurement for the effective use of BIM are those schemes, which give rise to greater coordination among all the procurement phases, from the design to the execution and maintenance. Furthermore, such an approach allows purchasing agencies to apply the MEAT paradigm also during the execution stage, where a team-dialogue among the parties, functional to the achievement of the best result, is fostered. To this extent, information becomes a pivotal element, where data interaction and integration serve as tools for describing the organizational structure of the operators and define the share-out responsibility of the parties involved. BIM methodology will thus allow the creation of digital infrastructures that are able to communicate and bring out the effectivity of such information flow, so that they will constitute the basis of any relevant decision-making process of the public administration. This highlights that BIM-based e-procurement may reduce the time and effort variables related with information management activities that have heavy contractual and administrative procedures and documentation.<sup>(159)</sup>

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(158) G.M. RACCA, “The Electronic Award and Execution of Public Procurement”, *Ius Publicum Network Rev.*, 2012, pp. 13-22; S. ARROWSMITH (eds), *EU Public Procurement Law: an Introduction*, Nottingham, U. Not., 2011, p. 248.

(159) A. AGUIAR COSTA and A. GRILO, “BIM-Based E-Procurement: An Innovative Approach to Construction E-Procurement”, *Scientific World J.*, Hindawi Publ. Corp., 2015, p. 10.

Accordingly, BIM model becomes a unique repository for all technical, managerial, administrative, and contractual information about the project both to the owner, contractors, designers, or subcontractors. Hence, the BIM-based project significantly improves information management and synergies among these parties aimed at the optimal meeting of the citizens' need also in a circular perspective.

In the new contractual models of cooperation and alliances the public entity should select the best team, as a coherent and efficient group of suppliers ready to work together and with the same goals as the public administration and the citizen, which require the prompt and efficient execution of the procurement. This way, apart from the public-private partnership, the competitive dialogue procedure could be the most appropriate to conduct the selection phase in an open book context.

All in all, these models would allow a real cooperation among contracting authorities and the suppliers, therefore a greater mutual trust, that would be encouraged and improved through the recourse to digital tools and methodologies capable of sharing information and evaluation methods at a reduced cost and with optimized processes. Such an evolution would require training and capacity building both for public procurers and private undertakings to fully grasp the potential of BIM and of collaborative contracts and to find the best way to involve contracting authorities into authentically integrated framework alliances. The adoption of new BIM methodologies and of collaborative contracts would eventually change the traditional aggregation schemes between suppliers and, in accordance to that, require new drafts of the procurement documents, the definition of the professional requirements of the tenderers, the establishment of mutual relationships inside the group and the identification of their common interest in improving their reputation of capacity and efficiency. In this perspective, it would be useful to provide *ad hoc* training to officials involved in the public procurement process and the definition of specific contractual models in conformity with the BIM methodology.(160)

Where correctly addressed, BIM,(161) in the perspective of Legal Information Modelling (LIM), might improve participation and an open comparison of offers by groups of suppliers aggregated in teams, alliances

(160) S. VALAGUZZA, *Governare per contratto. Come creare valore attraverso i contratti pubblici*, *op. cit.*, No. 3.

(161) Dir. 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 Comm., "Report from the Commission to the Council and the European Parliament", EU Anti-Corruption Report, COM(2014) 38 final, *op. cit.*, pp. 31-32; EU Comm., "Evaluation Report Impact and Effectiveness of EU Public Procurement Legislation", *op. cit.*, p. 24; G.M. RACCA, "The role of IT solutions in the award and execution of public procurement below threshold and list B

or consortia that could ensure the coordination of their intervention and the continuous monitoring of the work progress under a common framework. Collaborative contracts could indeed align the different goals of the project participants and hence strengthen the relationships along the project lifecycle. Hopefully opportunistic behaviours would decrease and public interest would once again be central. On this understanding, as BIM methodologies develop the dynamic character of the construction project, they would become strategic in order to better enforce efficiency, non-discrimination and transparency principles and favour cross-border participation, especially with regards to major projects aimed at addressing transversal issues. This potential shall thus be borne out by suitable procurement strategies such the “early involvement of key participants”, where the main actors collaborate together at preliminary project study phase. The different models of framework agreements represent a strategic tool for the effective use of BIM innovative way of contracting.

To conclude, BIM methodologies might allow the planning, award, execution and management of the complete cycle of life of the public works at reduced costs and enhanced integrity and efficiency. This seems to change the perspective on the work of procurement though, turning it into a wide ‘service contract’, that provides a flow of cooperation in the execution phase and cooperation for the management and maintenance contracts during the years of the evolving ‘life’ of the infrastructure over time. BIM methodologies cannot be considered any longer as confined to the design phase, they should instead be thought of as a new way of thinking about procurement implemented through collaborative contracts throughout the project cycle.

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services: overcoming e-barriers”, in *Outside the Procurement Directives – inside the Treaty?* (D. DRAGOS and R. CARANTA eds), Copenhagen, Djøf Publ., 2012, pp. 385-389.



**PART III**

**Encouraging Innovation**

BRUYLANT



## CHAPTER 9

### Public Procurement as a Strategy for the Development of Innovation Policy

BY

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#### *1. The European reform of public procurement's main objectives*

The revision (not just an update) of the Public Procurement Directives is part of an overall program aimed at an extensive modernization of the European Union public procurement system in order to be more efficient, and at designing policies that allow greater growth in a context of economic globalization.<sup>(1)</sup> This does not mean an ‘unlimited’ liberalization of public procurement policy. It suffices to recall the content of the European Parliament’s resolution of 12 May 2011, on equal access to public sector markets in the EU and in third countries and on the review of the legal framework for public procurement, including concessions (published in the *OJEU*, 7 December 2012) – which insists on the comments included in its resolution of 18 May 2010 on new aspects of public procurement policy – that, while strongly rejecting protectionist measures in the field of public procurement on a worldwide level, firmly supports the principles of reciprocity and proportionality. In that spirit and accordingly, it called on the Commission to carry out a detailed analysis of the

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(1) *Evaluation Report: Impact and effectiveness of EU law on public procurement* ([ec.europa.eu/internal\\_market/publicprocurement/modernising\\_rules/evaluation/index\\_en.htm#maincontentSec1](http://ec.europa.eu/internal_market/publicprocurement/modernising_rules/evaluation/index_en.htm#maincontentSec1)) gathers the opinions and recommendations of more than six hundred experts on the effectiveness of the current directives ruling procurement in public bodies. The report explains that the public procurement directives have fostered openness and transparency, leading to an increase of competition. This has rendered either cost savings or additional public investment, quantified at 20 million euros, a five percent of the 420 million euros tendered annually in public procurement at European level. It also reflects the unanimous desire to cut back, to speed and to ease the bureaucratic procedures. This is crucial for small and medium-sized enterprises (SMEs) that are currently having trouble completing the huge number of administrative requirements for the bidding processes. This analysis has served as a starting point for Directives revision, which was undertaken to maintain a balanced policy to support the demand for both environmentally and socially responsible, as well as innovative, goods services and works, providing the contracting authorities with simpler and more flexible procedures and ensuring easy access for businesses, particularly SMEs. A prior version of this piece was published in Spanish through the *Ius Publicum Network Review* ([www.ius-publicum.com](http://www.ius-publicum.com)), issue 1, 2018.

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potential benefits and problems linked to the implementation of proportionate and specific restrictions on access to certain sectors of the EU public procurement markets, an impact assessment to analyze when they can be applied, as well as an assessment of the legal basis that this instrument would require, for those trading partners who benefit from the opening of the EU market but who have not shown any intention to open their markets to EU enterprises, while encouraging EU partners to offer European companies reciprocity and proportional access to the market, before proposing any new regulation in the field of public procurement. The Parliament also called on the Commission to evaluate the problems linked to abnormally low tenders and to propose adequate solutions. It recommended that contracting authorities provide early and accurate information to other tenderers in the event of abnormally low tenders so that they can assess whether there are grounds to start an appeal procedure. The Parliament also considered it urgent that the EU achieve greater consistency between its common external trade policy and the Member States' practice of accepting abnormally low tenders from companies whose countries of origin are not signatories of the Government Procurement Agreement (GPA), at the expense of European Union companies and the Member States' employment, social and environmental standards.(2)

## ***2. The European public procurement reform's areas***

In this context, the approach to the specific scope of this European reform requires previous explanations that, though already well known, are worth commenting on. The first one is that the main objective of this European regulation is to ensure the efficiency of the public funds. To that end, the transparency obligation is the main instrument to guarantee, to the benefit of all the potential tenderers, an adequate publicity to ensure competition in the services market and to monitor the impartiality of the awarded procedures (Judgement of the European Court of Justice, 7 December 2000, ARGE). This principle finds its main practical expression through an adequate publicity of

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(2) On 23 March 2013, the European Commission presented the proposal for the Council decision on the formal conclusion of the Protocol amending the Government Procurement Agreement (GPA), the only WTO legally binding agreement on public procurement. Regarding the update of the EU's public procurement policy, it supported the request to rank by priorities the issues dealt with in the Green Paper and, in this regard, called on the Commission to: first, study the simplification of rules, the balanced access to public sector markets and the improvement of the SMEs access, and secondly to undertake the review of public procurement and concessions in order to obtain the necessary and full participation, not only of the European Parliament and the Member States, but also of citizens and businesses. On 7 March 2014, the Protocol amending the Government Procurement Agreement, done at Marrakesh on 15 April 1994, was published in the *OJEU*. Specifically, it replaced the Preamble, Art. I to XXIV and the Appendices in the 1994 Agreement, with the provisions set out in its Annex.

the awardable contracts in the *Official Journal of the European Union (OJEU)*, in a twofold way: (a) As an administration's audit mechanism, advertising is a great help for fair play in the administrative life and a monitoring opportunity available to administrators and potential procurers; b) As a means of promoting competition among the economic agents involved. This publicity must generate competition or competition amongst companies, as the Judgement of the European Court of Justice of 15 October 2009 *Acoset* recalls, stating that the principles of equal treatment and non-discrimination based on nationality imply a transparency obligation, which allows the awarding public authority to ensure that such principles are respected. The authority's transparency obligation is a means to guarantee, in benefit of any potential tenderer, an adequate publicity to ensure competition in the award of services and to monitor the impartiality of the award procedures (see in particular the Judgement of the European Court of Justice of 6 April 2006, *ANAV* section 21). Thereupon, the doctrine established by the Judgement of the European Court of Justice of 16 September 2013 (*Commission v Kingdom of Spain*) is the *leading case*, and generally applicable to every public tendering procedure.

The idea is to prevent the arbitrariness of the decision.(3) It is necessary to emphasize the importance of these European principles, which have transformed public procurement's national practice and which are based on the Treaties, as the Directive 24/2014 of public procurement recalls in its first recital.(4)

On the other hand, public procurement must be regulated from the perspective of an effective and efficient achievement of the services demanded.(5) Special attention to the implementation phase of the contract, which must be understood from the perspective of the need to achieve the services demanded, is required. Here lies the fulfilment of the public goals that the Public Administration must provide. Therefore, the contracting regulation must have a 'full view' of all the contract's different phases. Moreover, the new set of directives focuses now on this issue, regulating the modification of the contracts, the subcontracting situation and the termination of the contract, while stating that its principles have effects in every stage of the contract.(6) A very useful instrument in this regard is preliminary market consultations.

(3) ECJ, 2 June 2016, *Pippo Pizzo v CRGT Srl*, case C-27/15.

(4) It suffices to recall the doctrine of the ECJ, as a main example, its judgment of 16 April 2015 in the case C-278/14.

(5) One of the tools that exist to achieve efficiency in public procurement is a preliminary market consultation prior to the preparation of public contracts. On this aspect, see C. DE GUERRERO MANSO, "Las consultas preliminares del mercado: una herramienta para mejorar la eficiencia en la contratación pública", in *Estudio sistemático de la Ley de Contratos del Sector Público* (J.M. GIMENO FELIU ed.), Cizur Menor, Thomson-Reuters Aranzadi, 2018, pp. 1047-1072.

(6) Dir. 2014/24/EU, Art. 18.

### 3. Public Procurement as a Strategy

Public procurement – and its basis – have changed dramatically in recent years. From a bureaucratic view of public procurement, designed from an accounting perspective and scarcely future-oriented, it has evolved towards the idea of public procurement as a “legal tool at the public authorities’ service for the effective fulfilment of their purposes or their public policies”.(7) In other words, public procurement can be – and should be – a technique that grants social, environmental or research objectives, in the firm belief that these goals entail an adequate understanding of how public funds should be channeled. A strategic vision of public contracting, away from the rigid architecture of the administrative contract and from excessively bureaucratic or formal approaches, is therefore demanded. The efficiency principle, inherent to public procurement, cannot be exclusively interpreted from an economic point of view, but must be ensured through an adequate quality standard in the provision of the service.(8) That is, the principle of efficiency must be aligned according to social, environmental or research objectives, in the firm belief that these goals introduce an adequate understanding of how public funds should be channeled.(9)

It is in this context that the objectives set in the ‘EU 2020 Strategy’ should be understood.(10) The new legal and economic reality of public procurement requires a strategic vision in a globalized economic context.(11) A proper use of the public contract, as an instrument at the service of public policies, should enhance the reinforcement of the inherent principles of the European social model and ensure its sustainability in an increasingly strained geopolitical situation caused by the Eastern markets, which forces one to rethink and reinforce the European internal market strategy.

(7) I refer to my work, J.M. GIMENO FELIU, “Compra pública estratégica”, in *Contratación pública estratégica* (J. PERNAS GARCÍA coord.), Cizur Menor, Aranzadi, 2013, pp. 45-80.

(8) Regarding the meaning of efficiency – and its independence from a low price economic idea – I refer to my study, J.M. GIMENO FELIU, “Reglas básicas para mejorar la eficiencia y la transparencia en la contratación pública”, monographic issue of the journal *Presupuesto y Gasto Público sobre Calidad institucional, transparencia y buen gobierno*, No. 82, 2016, pp. 137-158. Also, T. MEDINA ARNAIZ, “Más allá del precio: las compras públicas con criterios de responsabilidad, Papeles de relaciones ecosociales y cambio global”, *Actualidad administrativa*, No. 121, 2013, pp. 87-97.

(9) J. PONCE, *Deber de buena administración y derecho al procedimiento administrativo debido. Las bases constitucionales del procedimiento administrativo y del ejercicio de la discrecionalidad*, Valladolid, Lex Nova, 2001, p. 479.

(10) “Europe 2020 A strategy for smart, sustainable and inclusive growth”, COM (2010) 2020. The Europe 2020 strategy is based on three cornerstones. It supports first, smart growth, *i.e.* the development of an economy based on knowledge and innovation. Second, sustainable growth that promotes an economy that uses its resources more efficiently, as well as being greener and more competitive. And third, inclusive growth, which means the development of an economy with high levels of employment, characterized by social and territorial cohesion.

(11) J.M. GIMENO FELIU, *El nuevo paquete legislativo comunitario sobre contratación pública. De la burocracia a la estrategia. (El contrato público como herramienta del liderazgo institucional de los poderes públicos)*, Cizur Menor, Aranzadi, 2014, p. 213.

This indicates that public contracts are not only a means of supplying raw materials or services under the most advantageous conditions for the State, but also a way for public authorities to carry out an intervention policy in the economic, social and political life of the country. Thus, turning public procurement into a guiding instrument for the economic agents involved: those who want to access public contracts must necessarily meet the requirements made by contracting authorities.<sup>(12)</sup> As T. Medina points out, this public procurement instrumental view reinforces the idea of using public procurement to guide and consolidate business behaviour benefiting the general interest and not necessarily linked to the direct contract's satisfaction.<sup>(13)</sup>

The instrumental perspective of public procurement lends itself to requiring and evaluating compliance with the European regulation on environmental and social policy in the selection phase.<sup>(14)</sup> Doing otherwise means to abandon a powerful public policy consolidation tool and to allow a potential offshoring of the business network to regulations that do not include these policies, which obviously incorporate other costs hardly translatable into profitability terms.<sup>(15)</sup>

In this regard, we must recall that the introduction of environmental protection-related conditions (such as eco-labels, recyclable products and wastewater treatment systems) has already been validated by the European Institutions (Commission communication of 28 November 2001 on the Community law applicable to public procurement and the possibilities for integrating social considerations into public procurement). They are accepted because these possibilities are related to the environmental policy acknowledged in Article 2 of the Treaty on the Functioning of the European Union.<sup>(16)</sup> The same applies

(12) J.M. GIMENO FELIU, *La nueva contratación pública europea y su incidencia en la legislación española*, Cizur Menor, Civitas, 2006, pp. 15-21; *id.*, "Nuevos escenarios de política de contratación pública en tiempos de crisis económica", *El Cronista del Estado Social y Democrático de Derecho*, No. 9 9, 2010, pp. 50-55.

(13) T. MEDINA, "Comprando para asegurar nuestro futuro: la utilización de la contratación pública para la consecución de los objetivos políticos de la Unión Europea", in col. book, *Observatorio de los Contratos Públicos 2010*, Cizur Menor, Civitas, 2011, pp. 43-94. Also J. RODRIGUEZ ARANA, "La contratación del sector público como política pública", in *Contratación Pública Estratégica*, *op. cit.*, pp. 31-44.

(14) S. ARROWSMITH, "The E.C. procurement Directives, national procurement policies and better governance: the case for a new approach", *Eur. L. Rev.*, Vol. 21, 1/2002, pp. 11-13, supports an opposite position in the evaluation of the contracting criteria related to other European Union policies – such as social or environmental clauses.

(15) As highlighted by G. VARA ARRIBAS, "Novedades en el debate europeo sobre la contratación pública", *Revista Española de Derecho Comunitario*, No. 26, 2008, p. 128: a sustainable public procurement that adequately combines economic criteria with social and environmental criteria is feasible. Also of interest are the suggestions made by B. PALACIN, "A la responsabilidad social por la contratación pública", available at [www.obcp.es](http://www.obcp.es).

(16) For all, see J. PERNAS GARCIA, "El uso estratégico de la contratación pública como apoyo a las políticas ambientales", in *Observatorio de políticas ambientales 2012* (F. LÓPEZ RAMÓN, coord.), Cizur Menor, Civitas, 2012, pp. 299-323; and his monographic issue, "Contratación Pública Verde",

to the social clauses, admitted as long as they provide an economic advantage linked to the product or service covered by the contract (Interpretative Commission communication of 10 November 2001),(17) which reflects the idea of public procurement as a tool for public policy effectiveness.(18) In any case, its use requires an appropriate balancing and the preservation of the tendered service's identity.

This means – always keeping in mind the GATT agreements – that it is possible to regulate a public procurement system, which while respecting the European principles, prevents precarious working conditions,(19) discourages corporate offshoring and does not punish either European companies or SMEs, as well as promotes the European circular economy goals.(20)

On the other hand, public procurement must be regulated from the perspective of an effective and efficient delivery of the service demanded, which obviously includes quality aspects linked to a certain social 'sensitivity'. This demands a special attention to the implementation stage of the contract, which should be understood from this perspective of the ultimate goal – the demanded service. Here lies the fulfilment of the public purposes that must be provided by the public administration. For this reason, procurement regulations need to have a 'full view' of all the contract phases and procurement goal viewed as a 'public investment' rather than as an expense.

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*La Ley*, 2011. With regard to the ecological considerations related to public procurement, it is also of interest the EC Comm., COM(2008) 400/2, "Public procurement for a better environment", available at [ec.europa.eu/environment/gpp/pdf/com\\_2008\\_400.pdf](http://ec.europa.eu/environment/gpp/pdf/com_2008_400.pdf), and "Commission Service document, Buying Green – Handbook on Green Public Procurement", available at [ec.europa.eu/environment/gpp/pdf/Buying-Green-Handbook-3rd-Edition.pdf](http://ec.europa.eu/environment/gpp/pdf/Buying-Green-Handbook-3rd-Edition.pdf).

(17) In a case examined by the Commission, the contracting authority relied mainly on the following elements in order to award a contract to the local transport enterprise: the company's establishment in the city meant, on the one hand, tax implications and, on the other hand, the creation of stable jobs. In addition, it forced the supplier to acquire a significant volume of material and services in that same locality which in turn guaranteed a great number of local jobs. The Commission considered that contracting authorities could not rely on such criteria to evaluate bids since it did not allow assessing an economic advantage inherent to the contract and benefiting the contracting authority. This first objection was based on a breach of the procurement rules contained in Art. 36.1 of Dir. 92/50/EEC. See T. MEDINA ARNAIZ, "Social Considerations in Spanish Public Procurement Law", in *PPLR*, Vol. 20 (2), 2011, pp. 56-79.

(18) See T. MEDINA ARNAIZ, "Comprando para asegurar nuestro futuro: la utilización de la contratación pública para la consecución de los objetivos políticos de la Unión Europea", in col. book *Observatorio de los Contratos Públicos 2010*, Cizur Menor, Civitas, 2011, pp. 43-104.

(19) It should be recalled that ILO (International Labour Organization) labour standards forbid forced labour (Conventions 29 and 105) and child labour (Conventions 138 and 182) and establish the right to freedom of association and collective bargaining (Conventions 87 and 98) and non-discrimination in terms of employment and occupation (Conventions 100 and 111). The labour standards' legal bases are the eight ILO main conventions aforementioned, ratified by all 27 EU Member States.

(20) The remarks made by M. COZZIO are of interest, "Le nuove direttive appalti e l'accesso delle piccole e medie imprese al mercato degli appalti pubblici" (prima parte), Osservatorio di Diritto Comunitario e Nazionale sugli Appalti Pubblici, on [www.osservatorioappalti.unitn.it](http://www.osservatorioappalti.unitn.it). Id., "Le scelte del legislatore europeo per favorire la partecipazione alle gare delle piccole e medie imprese", *Rivista Diritto e pratica amministrativa*, May 2014 (spec. iss.), pp. 8-21.

This explains why the public procurement legislation's reform is one of the twelve priority actions included in the Single Market Act adopted in April 2011 (IP / 11/469).(21) Indeed, the effectiveness of the public ordering system has become a priority for all Member States, given the current budgetary constraints. It is therefore necessary to have flexible and user-friendly instruments, which allow public authorities and their suppliers to award transparent and competitive contracts as easily as possible in order to be able to buy the best value for money.(22)

In short, one of the main examples of this strategic vision of public procurement are social and environmental conditions as well as the promotion of innovation. As a result, we can readily state that the EU institutions admit and encourage them, since public procurement is not an end in itself, but rather a power in the service of other general interest purposes (such as job stability, environment, social integration, improving investment in innovation). Moreover, these conditions do not restrict or limit competition, enabling, on the contrary, the higher principles currently included in the TFEU, to be effective.(23)

#### ***4. Public Procurement as a tool to promote innovation***

The new Community legislative package, as explained at the beginning of this paper, is based on a training approach that provides the contracting authorities with the tools required to achieve the strategic goals of Europe 2020. This approach links public procurement to other sectoral policies by

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(21) EU Comm., "Towards a Single Market Act. For a highly competitive social market economy. 50 proposals for improving our work, business and exchanges with one another", 27 October 2010, COM (2010) 608 final.

(22) This concept emphasizes the need that the goods acquired through public procurement meet the public needs, but also the contractor's obligation of complying with the contract's condition in its own terms. See for all S. ARROWSMITH, J.Y. LINARELLI and D. WALLACE, *Regulating Public Procurement: National and International Perspectives*, The Hague Kluwer Law International, 2000, pp. 28-30. The preliminary market consultation tool also makes it possible to better identify, from an early stage, the aspects that must be taken into account in order to achieve a correct value for money. On this aspect, see C. DE GUERRERO MANSO, "La necesaria revisión del artículo 115 del Proyecto de Ley de Contratos del Sector Público", in *Observatorio de los Contratos Públicos 2016* (J.M. GIMENO FELIU dir.), Cizur Menor, Aranzadi, 2017, pp. 143-173.

(23) Public procurement policy is, in short, one of the many elements of the Internal Market Policy, which has a number of strategic objectives (notably, the free movement of goods, persons and services). It aims to contribute to the completion of the internal market by establishing the necessary competition conditions so that public contracts can be awarded without discrimination and by allocating public resources in a rational way by choosing the best offer. Applying these principles enables contracting authorities to obtain the greatest return by following certain rules regarding the object of the contract's definition, the candidates' selection according to objective criteria and the exclusively price-based award or, optionally, on a series of objective criteria. Supporting this view, C. TOBLER, "Encore: women's clauses in public procurement under Community Law", *Eur. L. Rev.*, Vol. 25, No. 6, pp. 624-627.

using their purchasing power to acquire goods and services that promote innovation, respect for the environment and the fight against climate change while improving the labour conditions, the public health and the social conditions.(24)

Research and innovation play a main role in the Europe 2020 strategy for a smart, sustainable and inclusive growth.(25) Europe 2020 has as its motto “From the idea to the market”, emphasizing the need of supporting projects in greater proximity to the market, in order to avoid what is currently happening: several hundred million euros of European funds never reaching the market. An active innovation policy through public procurement can encourage the funds’ leverage for business activities, as well as support the commercialization of the R&D&I business (being the first customer and thus a reference client).

That is why Directive 2014/24 clearly enables public procurers to acquire innovative products and services that promote future growth and improve the efficiency and quality of public services.(26) This Directive takes a further step in public procurement for innovation by helping Member States to make tendering procedures more flexible and in the interest of other public policies by:

- a) Research and innovation, which are essential for achieving smart, sustainable and inclusive future growth.
- b) The advocacy of European innovation associations, through the intervention of agents of both the public and the private sectors, with the aim of accelerating the assimilation of innovation, creating a business interest.
- c) Greater SME access to the public procurement market, due to its potential to adapt to the environment.
- d) Drafting technical specifications that allow technical solutions’ diversity.

Keeping this goal in mind, the Directive formulates a broad concept of innovation, which avoids differing interpretations across Member States.(27)

(24) Due to its interest, I refer to the collective book coordinated by J. PERNAS, *Contratación Pública Estratégica*, *op. cit.*

(25) “The Green Paper From Challenges to Opportunities: Towards a Common Strategic Framework for EU Research and Innovation funding”, COM (2011) 48 final, 15 February 2011, states that achieving the broadly supported objectives of smart, sustainable and inclusive growth in Europe 2020 depends on research and innovation, as key drivers of social and economic prosperity as well as environmental sustainability.

(26) The recital 47 of the Dir. 2014/24/UE specifically states that “Research and innovation, including eco-innovation and social innovation, are among the main drivers of future growth and have been put at the centre of the Europe 2020 strategy for smart, sustainable and inclusive growth. Public authorities should make the best strategic use of public procurement to spur innovation”.

(27) We can already find soft law supporting this new scenario: 1. EC Comm. to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, “Pre-commercial Procurement: Driving innovation to ensure sustainable high quality public services in Europe”, COM (2007) 799 final. 2. EC Comm. to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, “Europe 2020 Flagship Initiative, Innovation Union”, COM (2010) 546 final. 3. “Horizon 2020 – research and innovation framework programme”, COM (2011) 808 final, from 30 November 2011. 4. Regul. (EU) No. 1290/2013

Its article 2.22 defines it as “the implementation of a new or significantly improved product, service or process, including but not limited to production, building or construction processes, a new marketing method, or a new organisational method in business practices, workplace organisation or external relations inter alia with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth”.(28)

To this end, the Directive introduces the ‘Innovation Partnership’, a new special procedure for the development and further procurement of new and innovative products, works and services, which must nevertheless be provided within the performance requirements and agreed cost.(29) The new regulation improves and simplifies the competitive dialogue procedure and facilitates cross-border joint procurement, an important tool for innovative procurement. The objective set by the Commission is to reach an investment of 3% of EU GDP in R&D by 2020, which can be done for example, through public procurement.(30)

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of the European Parliament and of the Council of 11 December 2013 laying down the rules for participation and dissemination in “Horizon 2020 – the Framework Programme for Research and Innovation (2014-2020)”, and repealing Regul. (EC) No. 1906/2006. A brief explanation of how innovation has become important in EU public procurement rules is in the paper by P. VALCÁRCEL FERNÁNDEZ, “The relevance of promoting collaborative and joint cross border public procurement for buying innovative solutions”, *Ius Publicum*, Iss. No. 1, 2017, pp. 1-50.

(28) In the context of the Directive, innovation refers not only to what is new – whether a product, service or process – but also to what has been significantly improved. About the procedure and its justification, see M.A. FERNÁNDEZ SCAGLIUSI, “Un nuevo procedimiento de adjudicación de contratos públicos: la asociación para la innovación”, in *Observatorio de Contratos públicos, Las nuevas Directivas de contratación pública* (J.M. GIMENO FELIU dir.), Cizur Menor, Thomson Reuters/Aranzadi, 2015, p. 341.

(29) Of special interest is the paper by T. MEDINA ARNÁIZ., “Comprando para asegurar nuestro futuro: La utilización de la contratación pública para la consecución de los objetivos políticos de la Unión Europea”, in *Observatorio de Contratos Públicos 2010*, pp. 43-101. Also of interest the paper by M. RODRIGUEZ BEAS, “La compra pública innovadora en la nueva Directiva de contratación pública”, in *Observatorio de los Contratos Públicos 2014, Las Directivas de Contratación Pública*, Cizur Menor, Aranzadi, 2015, pp. 305-328; and the mentioned paper by P. VALCÁRCEL FERNÁNDEZ, “The relevance of promoting collaborative and joint cross border public procurement for buying innovative solutions”, *op. cit.*, pp. 1-50.

(30) The aforementioned data is the one used by the Commission in its EC Comm. to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, “Europe 2020 Flagship Initiative – Innovation Union”, COM (2010) 546 final, 6 October 2010, p. 4. These figures can be compared, following P. ZAGAMÉ and L. SOETE, “The cost of a non-innovative Europe”, [ec.europa.eu/research/social-sciences/policy-briefs-research-achievements\\_en.html](http://ec.europa.eu/research/social-sciences/policy-briefs-research-achievements_en.html), 2010, with the amounts that other countries currently dedicate to innovation such as the United States, whose innovation expenditure reaches up to 2,6% of its GDP, or Japan that allocates 3,4% of its GDP. EC Comm. to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, “Pre-commercial Procurement: Driving innovation to ensure sustainable high quality public services in Europe”, COM (2007) 799, 14 December 2007, also offers some figures, which show how the main EU trade partners (the United States and Japan) have already boosted innovation, using public procurement of R&D as an important incentive to give an answer to public needs for which the market does not offer solutions. In this regard, the United States’ public sector allocates 50 billion dollars a year for R&D procurement, an amount twenty times higher compared to European

The success of public procurement for innovation requires that the public procurers behave as clients with a strategic vision and plan what they will need to buy and how to buy it. In this regard, one of the first steps to take is to identify which sectors or areas of action are more likely to promote a procedure aimed at the procurement for innovation. In order to do so, political forces, smart specialization strategies and the goals set by the managing authorities, must be taken into account.

This European public procurement for innovation strategy designs two types of measures: an increase in the innovative products and services' demand and the so-called 'pre-commercial procurement', which belongs to the research and development phase (R&D) prior to marketing and which covers activities such as the solutions' scanning that are characteristic of the design, prototyping, testing and pre-production phases, stopping before commercial production and sale.<sup>(31)</sup>

The sharing of risks and benefits according to market conditions is a special trait of pre-commercial procurement (defined as a business excluded from public procurement regulation as it fosters R&D). This happens because the public procurer does not keep the R&D results for its exclusive use, but shares with the private sector the risks and benefits of the R&D needed to develop innovative solutions that exceed those available in the market. R&D services can be provided without being subject to public procurement rules when the public procurer allocates risks and benefits at market prices, according to one of the exclusions set out in the EU Public Procurement Directives. Namely article 16.f) Directive 2004/18/EC which states that "This Directive shall not apply to public service contracts for: [...] f) research and development services other than those where the benefits accrue exclusively to the contracting authority for its use in the conduct of its own affairs, on condition that the service provided is wholly remunerated by the contracting authority", and article 24.e) Directive 2004/17/EC which explains that "This Directive shall not apply to service contracts for: [...] e) research and development services other than those where the benefits accrue exclusively to the contracting

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spending, which approximately represents half of the global difference between R&D investments in the United States and in Europe. Increasing European spending on research and development could create 3.7 million jobs and increase the annual GDP close to 800 billion euros by 2025. As we mentioned, it would help to establish the European Union (hereafter EU) in a world leadership position in economic and social terms again.

(31) On pre-commercial procurement, *see* EC Comm. to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, "Pre-commercial Procurement: Driving innovation to ensure sustainable high quality public services in Europe", COM (2007) 799, 14 December 2007; and European Parliament Resol., 3 February 2009, 2008/2139 (INI), *OJEU*, C 67E of 18 March 2010. Regarding its impact in the Spanish legislation, Á. CORTÉS MORENO, "La contratación precomercial y la Ley de Contratos del Sector Público. Su reflejo en la Ley de Economía Sostenible", *El Consultor de los Ayuntamientos y de los Juzgados*, No. 9, 2011, pp. 1109-1119.

entity for its use in the conduct of its own affairs, on condition that the service provided is wholly remunerated by the contracting entity”.

The main novelty for the implementation of the innovation’s promotion through public procurement strategy is the regulation in the Directive of a new procedure to purchase the innovation results.<sup>(32)</sup> This specific and ground-breaking procedure should enable contracting authorities to establish a long-term innovation partnership for the development and further acquisition of new innovative products, services or works, not having to call upon an independent procurement procedure to actually acquire the innovation.<sup>(33)</sup> Although it has certain similarities with the negotiated procedure, the nature of this new approach means that it stands apart, with its own meaning. It is thus, needed to make this distinction (which requires knowing when and how to apply the negotiated procedure).

In the innovation partnership, since the procedure is an integrated whole, the partner that offers the best technological bid will be the successful tenderer of the work, supply or service. In its first phase (pre-commercial), innovation partnership is similar to a pre-commercial procurement in its minimum degree, since the technology sought either already exists – and just needs to be improved – or can be developed successfully in the short term. However, in its second phase (commercial or contractual) the nature of the contract will be determined by the type of final product demanded by the contracting authority.<sup>(34)</sup>

Directive 2014/24/EU emphasizes what must drive the contracting authority, which concerns three elements: the need for innovative products, the procedure’s selection and the requirements demanded in order to participate

(32) M.A. BERNAL BLAY and A.I. PEIRÓ BAQUEDANO, “Public Procurement Reform in Spain: the Forthcoming Regulation”, in *EPPPLR*, Vol. 12, Iss. 1, 2017, pp. 73-74.

(33) This new procedure should not be mistaken with pre-commercial procurement. Pre-commercial procurement was expressly excluded from the scope of Community procurement regulation (Art. 16.f of Dir. 2004/18/EC). Innovation partnership is a single procedure divided into two main phases, whereas pre-commercial procurement ends with the design of the goods or services demanded by the contracting authority. Its manufacturing or supply will be tendered in a separate procedure. This technique is analyzed in the 2/2010 Report of 17 February of the Consultation Board of Administrative Contracting of the Region of Aragon: Traits that highlight the singularity of these contracts are: a) The pursued public interest in obtaining resources and promoting research. b) The general rule is the randomness of the contract, which does not respond to a previous need of the public entity. c) As the promotion and initiative of the contract come from outside the Administration, it is not possible to promote concurrence and its lack does not compromise administrative goals. As A. LOPEZ MIÑO, “La compra pública innovadora en los sistemas europeo y español de contratación pública”, in *Contratación pública estratégica, op. cit.*, pp. 213-248, who has analysed in an excellent way the variety of public procurement for innovation modalities, warns, the lack of a European legal framework on pre-commercial procurement increases the possibilities of incompatible public aid. It is easy to take advantage of the variable nature of the different protocols that develop it on a case-by-case basis in the different Member States and therefore, an utmost care in selecting this contractual modality must be taken.

(34) “Supplies, services or works”, Dir. 2014/24/EU, Art. 31(2).

in it. This motivation cannot be brief and must be reasonable and rational (the procedure's selection is ultimately justified, as far as the innovation partnership is concerned, in the need for technology and innovative products and in its absence in the market).

Regarding the procedure, the contracting authority will begin by publishing the call for tender. Consultation of the market is desirable in order to obtain information about the structure and capacity of a market (regulated in Art. 40 of Dir. 2014/24). It also informs market players about the public procurers' projects and procurement requirements. However, these preliminary contacts with market participants should not lead to unfair advantages and distortions of competition.(35)

In the tendering documentation, the contracting authority will first state 'the need for innovative products, services and work which cannot be met by the procurement of products, services and works already available on the market'. In other words, contrary to ordinary procurement, which defines a specific object, this procedure foresees an open requirement. That is why it does not include among its documents a typical Technical Specifications Document, but instead it provides a list of functional prescriptions.(36) Preliminary market consultation prior to the launch of the innovation partnership procedure will serve to motivate the choice of such a procedure. If carried out correctly, the information obtained in the preliminary market consultation will allow a reasoned response to the need to use the innovation partnership to purchase innovative goods, products or services that are not yet available on the market.(37)

Economic operators will have at least 30 days to submit their requests to participate. This period will start from the date of the publication of the contract notice.

(35) In this regard it is of interest the description made in the already mentioned paper of A. LOPEZ MIÑO, "La compra pública innovadora en los sistemas europeo y español de contratación pública", *op. cit.*, pp. 229-237.

(36) On 20 November 2013 a new Standard UNE-EN 16271:2013 was published: "*Gestión del Valor. Expresión funcional de necesidades y pliego de especificaciones funcionales. Requisitos para la expresión y validación de las necesidades a satisfacer por un producto en el proceso de adquisición u obtención del mismo*". This Standard is the official Spanish version of the European Standard EN 16271:2012, and has been prepared by the technical committee AEN / CTN 144 *Gestión del Valor. Análisis del Valor. Análisis Funcional*, whose Secretariat is carried out by IAT. The Economic and Financial Plan is compatible with the public procurement regulation and provides great value for the mechanisms of Public Procurement for Innovation, defined as an administrative action, which encourages innovation aimed at promoting the development of new innovative markets from the demand side. This can be achieved through the public procurement tool, as the bids must express the needs required in functional terms.

(37) In order to see a complete and systematic study of the preliminary market consultations and their relationship with the public procurement of innovation, see two different but complementary works already mentioned, C. DE GUERRERO MANSO, "Las consultas preliminares del mercado: una herramienta para mejorar la eficiencia en la contratación pública", *op. cit.*, pp. 1047-1072; and *id.*, "La necesaria revisión del artículo 115 del Proyecto de Ley de Contratos del Sector Público", *op. cit.*, pp. 143-173.

In Directive 2004/18/EC, the selection criteria include the authorization to pursue professional activity, the economic and financial solvency, and the technical and professional skills. The enterprise and its human resources experience are admissible as part of the technical and professional solvency criteria. The contracting authority must prioritize the selection criteria related to candidates' skills in the field of research and development, as well as the development and application of innovative solutions. Moreover, the Directive foresees the possibility to reserve these kinds of contracts in favor of innovative SMEs in order to further the strategic vision of this procedure.

After the selection process, only the prequalified candidates are invited to present a bid (bearing in mind that it is possible to set the maximum number of prequalified bidders provided that they should not be less than three.). The Directive refers to the rules of the negotiated procedure in order to award the contract. The technical specifications must be formulated in a functional way so as not to unduly limit innovation solutions, as the technical aspects must be decisive in the award of the contract.

As a principle inherent in all public procurement, confidentiality must be specially monitored, in order to avoid unfair competition policies or inappropriate use of information obtained in the procedure.(38)

A special feature – and quite likely difficult to assume by the less experienced decision-makers – is that there might be several successful tenderers. Indeed, the Directive encourages the selection of several candidates – who will develop the innovative solutions in a parallel and competitive way. The assessment of innovation will require taking into consideration criteria other than the lowest price. It is inconsistent with the valuation of innovation to give the price an excessive weight, since innovative solutions are usually more expensive if we only pay attention to the price. However, this does not imply that their cost is higher. For example, it could mean that the solution requires less maintenance or has a longer lifespan. Therefore, instead of the price (or as well as the price), procurement for innovation should consider, not only the current costs but also the whole life cycle costs of the contract's object, which include the costs of product development, its purchase and potential shipping and deployment, maintenance costs and products or services' disposal with the

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(38) As the judgement of the ECJ of 14 February 2008, VAREC reminds, the entity that has access to this information must adequately guarantee the bidders' proposals' confidentiality and secrecy. The requirements of the Dir. 2016/943/ EU of the European Parliament and of the Council of 8 June 2016 on the protection of undisclosed know-how and business information (trade secrets) against their unlawful acquisition, use and disclosure (*OJEU*, 15 June 2016) must be particularly safeguarded. Its Art. 2 defines the concept of trade secrets. It is information unknown to the majority of agents who might find it of interest, has trade value and is under measures to keep it secret. Even though it does not refer to industrial secrets, nothing suggests that they are excluded, and therefore business secrets can include both commercial and industrial secrets.

related costs, as well as other important aspects such as the quality and the technical worthiness of the offer. Consequently, it will be possible to allocate the optimum combination of life cycle costs' set and of quality considerations, linked to the price. In short, it is about giving more value to innovative aspects than to the price in relative terms.

At the end of each of the research phases and after evaluating the results achieved by each of the tenderers, the contracting entity may terminate the individual contracts of those who have not reached the objectives set and thus reduce the number of tenderers. The contracting authority can also retain the right to reduce the number of partners. Obviously, this right, as well as the procedure to make it effective, must be clearly stated in the procurement documentation.

In order to acquire the supplies, services or works, the contract's value and duration must be kept within the appropriate limits (without the rigidities of the ordinary procurement), taking into account the need to recover the costs, particularly those related to the development of an innovative solution, as well as a reasonable profit.

On the grounds of this procedure's basis and function, the new European regulation has foreseen the need to regulate the intellectual property rights rules that will apply during the Innovation Partnership's implementation and closing. For the purposes of the principle of equal treatment of the tenderers, the contracting authority will determine these rules in the preparatory tender documentation, so that every tenderer is aware of them when submitting its bids. This is a key element because the success of the Innovation Partnership depends on it. In addition, in a risky procedure, such as this one, security regarding the remuneration is an absolute must.

It may be advisable to foresee an arbitration option in the contract in order to settle as soon as possible the incidents arising from the implementation phase.

In any case, despite the potential of this new procedure, it is important to note that there is a certain reluctance due to: a) unawareness of social economic benefits, b) lack of legal clarity regarding the possibilities of procuring for innovation c) lack of information and tools, as well as the implementation of non-uniform criteria, d) lack of an adequate exchange of experiences, and professionalization, and e) absence of political support.

In order to achieve the goal of making public procurement for innovation a practical strategy, the training of the contracting units' technicians must be improved, so that they can demand the market technological solutions adapted to their needs (which is known as 'early demand' and is very useful). Good practices regarding public procurement for innovation would be the following:

- 1) Improving the tenders' technical specification documents (functional requirements) in order to facilitate the participation of innovative companies in the awarding of public procurement for innovation procedures;
- 2) Exploring the possibilities of joint procurement: in this way, it is possible to limit the private sector risks;
- 3) Analysing and encouraging the dissemination of good practices regarding the procurement for innovation in the public sector;
- 4) Reporting the long-term procurement plans to the market, in order to give it time enough to react and develop innovative solutions that respond to the defined need;
- 5) Having a well-trained procurement staff in place, capable of managing the procurement for innovative solutions;
- 6) Identifying the innovative solutions already available in the market by consulting potential suppliers as long as transparency is respected and competition is not hindered;
- 7) Identifying and planning the risks, since they are inherent in the procurement for innovative solutions and it is very important to assess their potential impact on the project;
- 8) Deciding on the risks' distribution between the administration and the tenderer (business participation must be encouraged);
- 9) Establishing the treatment of intellectual and industrial property rights treatment, which usually arise when innovative products are developed;
- 10) Including in the contract incentives for additional innovative solutions;
- 11) Designing a planned contract management system, which should be included in the Technical Specification Documents, published in the call for bids, so that the parties are clearly aware of their respective duties;
- 12) Tracking and learning from the implementation: this can help support future innovations;
- 13) Establishing evaluation procedures to improve innovation in public procurement procedures;
- 14) Assessing arbitration systems in implementation matters.

In conclusion, we can emphasize the idea that the strategic vision of public procurement has an obvious impact on the design and effectiveness of State public policies. That is why the idea "we have always done it this way" must be overcome, as well as the inclination to self-indulgence and the strict "administrative" vision of public procurement must be avoided. The new European regulation is an opportunity to consolidate a new business model that values innovation and boosts the innovative SME model.

It is an opportunity to change the economic model and the ‘business vision’. The administration accepts the offer for new products or, in the absence of solutions, requests the market for collaboration. This requires a high level of expertise (in short, of professionalization), in order to place value in public innovation.<sup>(39)</sup>

The current context allows for a thorough review of our public procurement model (it is an opportunity) to move from a bureaucratic procurement model to a strategic public procurement model that encourages the purchase of innovative solutions. Because as Albert Einstein already warned, “we cannot hope for things to change if we always do the same”.

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(39) The European Union’s choice regarding this professionalization policy is indeed reflected in the EU Comm. Recomm. 2017/1805 of 3 October 2017 on the professionalisation of public procurement. Building an architecture for the professionalisation of public procurement. (*BOE* of October 7). This important Recommendation reminds Member States to develop and implement public procurement long-term strategies, adapted to their needs, resources and administrative structure, either in an autonomous way or as part of broader public administration professionalization’s policies. The aim is to attract, develop and retain competencies, focus on performance and strategic results and make the most out of the available tools and techniques. To this end, the States are urged to develop adequate training programs.

# CHAPTER 10

## State Aid and Procurement for Research, Development and Innovation

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### *1. Introduction*

Promotion of research, development and innovation also known as R&D&I, is one of the most important prerequisites of supporting competitiveness in the European Union, and, at the same time, a guarantee for its economic growth and sustainable development.(1) Innovation is also a solution to modern challenges such as the financial crisis and its effects on the banking system, the need to redesign sectors such as energy, transport and environment to reduce climate change, the difficulties and challenges of the health system, the compelling need of finding talented scientists in the pharmaceutical industry, and many more, which must all be quickly and efficiently overcome.

The purpose of innovation in the modern economy is not always to produce something new. Sometimes innovation means changing something the society already has, and making it memorable. When we look at the example of modern earphones, we notice that in the beginning of the 21<sup>st</sup> century all earphones were functional and black. Apple made history in 2001 by changing the shape and the color without changing the production mechanism.

Innovation is more about reaching it than defining it. However, some attempts at defining it exist. For instance, it was defined as “the creation of

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(1) According to the Europe 2020 strategy, an agenda which aims to give an overall view of where the EU should be on key parameters by 2020, 3% of the EU's gross domestic product (GDP) shall be invested in R&D&I by that time. EC Comm. to The European Parliament, The Council, The European Economic and Social Committee and The Committee of The Regions, “Europe 2020, Flagship Initiative Innovation Union”.

new (or the efficient reallocation of existing) resources which contribute to progress”.(2)

Research, development, and innovation are concerned with strong roots in the history of Europe and their first official legal framework is represented by the 1986 Single European Act (SEA), which was not only the biggest revision of the 1957 Treaty of Rome, but also an important step towards the process of recognizing the need for innovation. This was a key moment, when Europe started thinking big and realized that profound innovation was needed in the way that services in EU were designed and delivered in the direction of solving the new challenges that had emerged. The contribution of the SEA was even more important in the field of R&D&I since it was the first to establish the well-known objective of “strengthening the scientific and technological basis of European industry and of encouraging it to become more competitive at international level”.(3)

Innovation is different from research and development, but R&D can lead to innovation. Research and development is the process used for obtaining knowledge, which will be further used to create innovative new products, services, or technologies. When comparing research and development with innovation, it is confirmed that R&D is more about improving technologies of production, whilst innovation is more concerned with developing the process of bringing those goods or services on the market in the most original and the fastest possible way. R&D is a part of innovation, which is more of a process that uses R&D. Whereas R&D uses money to achieve knowledge and new technologies, innovation, which includes a commercialization phase, uses the knowledge to create new business.

But how can the EU reach innovation, research, and development? Do EU laws and regulations stimulate enough innovation in the economy of Member States? Which are the proper instruments and other existing policy programs that Member States can use to achieve R&D&I? Article 180(4) and

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(2) M. GRANIERI and A. RENDA, *Innovation Law and Policy in the European Union: Towards Horizon 2020*, New York, Springer 2012, p. 4.

(3) Art. 130, SEA, unmodified since 1986, provides that the Community shall carry out the following activities, complementing the activities carried out in the Member States: implementation of research, technological development and demonstration programmes, by promoting cooperation with undertakings, research centres and universities; promotion of cooperation in the field of Community research, technological development, and demonstration with third countries and international organizations; dissemination and optimization of the results of activities in Community research, technological development, and demonstration; stimulation of the training and mobility of researchers in the Community.

(4) Art. 180 (ex Art. 164 TEC): In pursuing these objectives, the Union shall carry out the following activities, complementing the activities carried out in the Member States: (a) implementation of research, technological development and demonstration programmes, by promoting cooperation with and between undertakings, research centres and universities; (b) promotion of cooperation in the field of Union research, technological development and demonstration with third countries and international organisations; (c) dissemination and optimisation of the results of activities in Union research, technological development and demonstration; (d) stimulation of the training and mobility of researchers in the Union.

Article 181(5) from the Treaty illustrate and explain the activities to be carried out for promoting research and development, but further legal instruments are needed in order to achieve these objectives.

In this paper, we look at State aid and public procurement for R&D&I as legal instruments to foster innovation in the EU and attempt to assess the interactions between the two legal and policy instruments. We look at State aid for R&D&I and procurement for innovation in terms of advantages and disadvantages for public authorities, and based on secondary data we analyze their use in the European Union.

## ***2. Conceptual Background – Instruments for State Intervention on Public Markets***

The role of the State is to ensure, defend and promote the public interest and well-being of both the individuals and constituent groups of a society. When speaking of State intervention on public markets, the questions are: Why do States intervene? What is the reasoning behind this intervention? When do States intervene and which instruments of intervention are used?

States usually intervene in public markets not only when their resources are not optimally distributed, but also to fight against inefficiency and market failures. Market failure in the process of allocation of funds, unequal distribution of income between the members of society, as well as the need for regulation of the economy, can also determine the State's intervention on public markets.(6)

The general justification for governments' intervention is to achieve efficiency or other goals which are important to society and its members. If the private sector and the public sector followed totally different directions, then the private sector might gain more autonomy, the two sectors would experience far too many discrepancies and differences between these two sectors. Worse, the State might lose control and supervision, which is considered worldwide as a state prerogative.

A balance and developed economy involves encouraging competitiveness and an active collaboration between private and public sectors in delivering the needed infrastructure for a well-functioning society. The relationship

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(5) Art. 181 (ex Art. 165 TEC): 1. The Union and the Member States shall coordinate their research and technological development activities so as to ensure that national policies and Union policy are mutually consistent. 2. In close cooperation with the Member State, the Commission may take any useful initiative to promote the coordination referred to in paragraph 1, in particular initiatives aiming at the establishment of guidelines and indicators, the organisation of exchange of best practice, and the preparation of the necessary elements for periodic monitoring and evaluation. The European Parliament shall be kept fully informed.

(6) G. MANKIW and M.P. TAYLOR, *Economics*, London, Cengage Learning EMEA, 2006, p. 5.

between public and private sectors in delivering public services relates to the concept of public-private partnership.(7) The collaboration of the public sector with the private operator brings multiple benefits to both sides, such as value for money, lower costs and innovative outcomes.

There are various policy instruments available that Member States may use for fostering innovation, either by spending public funds or by using the resources of the private sectors. State aid, for example can be granted for R&D&I in multiple forms. The State may also use public procurement for innovation. The choice between these two legal instruments should be based on an understanding of their respective functionalities and how effective they can be in achieving the innovation goals. It is also important to keep in mind that there may be other, better instruments that can lead to innovation, such as an increased funding in public research and education or general fiscal measures.(8)

### ***3. Public Procurement for Innovation***

#### **3.1. From classical procurement to strategic procurement**

Public procurement across the EU Single Market is defined as a process of buying works, goods, or services, by contracting authorities from private actors in a transparent, fair, and competitive manner, which generates business opportunities, increases competition, and drives economic growth on the Single Market.(9) Public procurement policy must ensure an efficient use of public funds and open EU-wide procurement markets. Of these goals, the most important public procurement goals are achieving value for money by promoting competition and ensuring the integrity and transparency of the procedures.(10)

Public procurement in the EU is subject to the principles of the Treaty, and the detailed provisions of the EU Directives on public procurement(11), which coordinate all the national procurement rules. The modernization of the Public

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(7) For related discussion on public private partnerships, C. BOVIS, *Public private partnerships in the EU*, London, Routledge Taylor & Francis, 2014, pp. 86-110.

(8) EC Comm., “Framework for State aid for research and development and innovation”, Section 4.3.1.

(9) Definition from the OECD.

(10) A. SANCHEZ GRAELLS, *Public Procurement and the EU competition rules*, 2nd ed., Oxford, Hart Publ., 2015, p. 102. In this particular case, the author stressed the diversity of Public Procurement goals, underlining the idea that its economic objectives are the “most noteworthy.”

(11) Dir. 2014/24/EU on public procurement (known as the ‘classic directive’); Dir. 2014/25/EU on procurement by entities operating in the water, energy, transport and postal services sectors (the ‘sector specific directive’); and Dir. 2014/23/EU on the award of concession contracts.

Procurement Directives in 2014 included new provisions relating to innovation as a goal of public procurement. Innovation is included among the strategic goals of procurement, alongside green procurement and social procurement.

Procurement for innovation relates to purchasing products or services that do not yet exist, or that need major improvements so they must use research and development to fulfill those features requested by the contracting authorities in the tender procedure.<sup>(12)</sup> Before public procurement was just based on lowest price or value for money. This paradigm has shifted: “public procurement has recently started to move towards strategic innovation, as an instrument that can lead to satisfying unsatisfied human needs and solving societal problems”.<sup>(13)</sup>

The interest in public procurement as a driver for innovation can be traced back to the first programmatic documents relating to a Europe of innovation. In 2004 the Kok report meant to revitalize the Lisbon strategy by promoting recommendations for procurement practices favorable to R&D and innovation, sustaining eco-innovations and national road maps for the implementation of the EU’s Environmental Technology Action Plan (ETAP) and even promoting national action plans for ‘greening’ public procurement.<sup>(14)</sup>

### 3.2. The legal provisions

The legal provisions that are relevant for procurement for innovation can be found in different places in the Procurement Directives 2014, although the main instrument is considered to be the innovation partnership.

First, in the context of public procurement *innovation* is defined in the Directive as “the implementation of a new or significantly improved product, service or process, including but not limited to production, building or construction processes, a new marketing method, or a new organizational method in business practices, workplace organization or external relations inter alia with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth”.<sup>(15)</sup>

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(12) Art. 31(1) and Art. 2(I)22 of the Dir. 2014/24/EU, “provides indication for public procurement procedures in its reference to the need for such innovative product or works”; see P. TELLES and L.R.A. BUTLER, “Public procurement award procedures in Directive 2014/24/UE”, in *Modernising Public Procurement: The New Directive* (F. LICHÈRE, R. CARANTA and S. TREUMER eds), Copenhagen, Djørf, 2014, p. 133.

(13) C. EDQUIST, J.M. ZABALA-ITURRIAGAGOITIA and J. MIKEL, “Public Procurement for Innovation as mission-oriented innovation policy”, *Research Pol.*, Vol. 41, Iss. 10, December 2012, pp. 1757-1769. The same authors have made a classification of procurement for innovation according to three dimensions: “(i) the user of the purchased good; (ii) the character of the procurement process; and (iii) the cooperative or non-cooperative nature of the process”.

(14) Report from the High Level Group chaired by W. KOK, *Facing the challenge The Lisbon strategy for growth and employment*, November 2004.

(15) Art. 2, par. 1 and 22, Dir. 2014/24/EU.

Second, there are several legal provisions that can be referred to when buying innovation:

- Article 14 from the Directive relates to R&D services covered by the Directive;
- Article 26 on the choice of procedures makes reference to the competitive procedure with negotiation and to competitive dialogue, which may also include requirements related to design or innovative solutions;
- Article 32 (3) – a negotiated procedure without prior publication of a tender notice can be conducted in order to buy products manufactured purely for research, experimentation, study or development, but does not include quantity production to establish commercial viability or to recover research and development costs; it also excludes the purchase of ‘first products’ developed as a result of research.
- Article 32 (2) b – the negotiated procedure without prior publication may be used where the works, supplies or services can be supplied only by a particular economic operator for any of the following reasons: (...) the protection of exclusive rights, including intellectual property rights.

Third, a new dedicated procedure was inserted in the Directives. Apart from the above general procedures that may include requirements for innovative products, services or works, the most referred to legal text remains the one on *innovative partnerships*, which will be discussed below.

### 3.3. The Innovation partnership

Regulated in Article 31 of the 2014 Directive, innovation partnership is a complex procedure. It is a combination of competitive procedure with negotiation and competitive dialogue procedure, which allows public and private actors to establish partnerships with an ultimate purpose of developing an innovative solution.

Using this procedure, the contract may be awarded to one or more private operators in successive phases with intermediate targets. The selection criteria will be “the candidates’ capacity in the field of research and development and of developing and implementing innovative solutions”.<sup>(16)</sup>

It is a single procedure, in one stage, and it involves both R&D activities and the product/service/work thus developed, by concluding a single contract with reference to maximum costs envisaged at the end of the award procedure.

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(16) Art 31 (6), Dir. 2014/24/EU.

As a method for award, it is a negotiated procedure with a prior call for competition with one or more private partners, which may include successive phases with intermediate targets. After each phase, there is the possibility of continuing with a reduced number of partners or even terminating the procedure when no satisfying outcome is in sight.

In selecting an awardee, the contracting authorities may assess the vendors previous accumulated capacity in R&D and in innovative solutions as part of the selection criteria.

### 3.4. The concepts of PCP and PPI

In literature, two categories of innovative procurement are often discussed, although they are not regulated in the Directives: Pre-Commercial Procurement and Public Procurement for Innovation.<sup>(17)</sup>

#### 3.4.1. Pre-Commercial Procurement (PCP)

According to the European Commission Framework for State aid for research and development and innovation, pre-commercial procurement means the public procurement of research and development services where the contracting authority or contracting entity does not reserve all the results and benefits of the contract exclusively for itself for use in the conduct of its own affairs, but shares them with the providers under market conditions. The contract, the object of which falls within one or several categories of research and development defined in this framework, must be of limited duration and may include the development of prototypes or limited volumes of first products or services in the form of a test series. The purchase of commercial volumes of products or services must not be an object of the same contract.<sup>(18)</sup>

In other words, PCP covers the purchase by a contracting authority of R&D services (Research and Development) and concerns the phase before commercialization, whether a company wants to create a new product or service or just update an existing one. It thus refers to the procurement of a long-awaited research result, being a matter of direct public R&D investments, without great involvement in the actual product development phase. It does not involve the purchase of many units of a (non-existing) product, and no buyer of such a product is therefore involved in the procurement.<sup>(19)</sup> The purchase of R&D

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(17) See for details P. TELLES and L.R.A. BUTLER, "Public procurement award procedures in Directive 2014/24/UE", *op. cit.*, p. 133.

(18) EC Comm., "Framework for State aid for research and development and innovation article 1.3.", 2014/C 198/01.

(19) C. EDQUIST, N.S. VONORTAS, J.M. ZABALA-ITURRIAGAGOITIA and J. EDLER, *Public procurement for innovation*, Cheltenham, Edward Elgar, 2015, p. 9.

can cover fields such as: solution exploration, energy, health, design, prototyping, up to the original development of a limited volume of first products or services in the form of a test series.(20)

One of the biggest challenges of PCP is the allocation of intellectual property rights (IPR) and the way procurers will share with suppliers at market price the benefits and risks related to the IPRs resulting from the R&D.(21) If the result of R&D is a positive one, and a new product or service is being launched on the market, it becomes important that the rules for allocation of IPR have been set up prior to the start of the project. The European Commission has stressed the importance of having clear provisions in the tender documentation and in the call for tenders to deal with property rights: the distribution of rights and obligations between public procurers and R&D providers, including the allocation of IPRs, shall be published in the PCP call for tender documents and the PCP call for tender shall be carried out in a competitive and transparent way in line with the Treaty principles which leads to a price according to market conditions. The public procurers should ensure that the PCP contracts with R&D providers afford financial compensation according to market conditions compared to what would be an exclusive development price for assigning IPR ownership rights to participating R&D providers, in order for the PCP call for tender not to involve State aid.(22)

It was stated that in pre-commercial procurement, the public purchaser does not reserve the R&D results exclusively for its own use: public authorities and industry share risks and benefits of the R&D needed to develop new innovative solutions that outperform those available on the market.(23)

PCP works in conjunction with PPI (Public Procurement of Innovative Solutions), but PCP should not be confused with PPI. PCP focuses on 'development' while PPI focuses on 'deployment'. PPI is used in cases closer to the market or in cases where there is no R&D that is required to address the procurement need or when R&D has already concluded. "Distinguishing between PCP and PPI also allows companies that have developed products through means other than a PCP (e.g. through SME instruments, other grants, own company R&D resources) to still compete for PPI deployment contracts,

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(20) EC Comm. to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, "Pre-commercial Procurement: driving innovation to ensure sustainable high quality public services in Europe", SEC(2007) 1668, COM/2007/0799 final.

(21) *Horizon 2020 Work Programme 2014 – 2015*, p. 20, par. 19.

(22) *Ibid.*

(23) EC Comm. to the European Parliament, the Council, the European Economic and Social Committee and The Committee of the Regions Pre-commercial Procurement, "Driving innovation to ensure sustainable high quality public services in Europe", SEC(2007) 1668, p. 3.

avoiding issues of foreclosing of competition and crowding out of other R&D financing sources”.(24)

### 3.4.2. Public Procurement for Innovation

PPI is a procedure that refers to situations where a contracting authority acts as a lead customer (also called first buyer) by obtaining ‘innovative’ solutions that are new arrivals in the market, but not yet available on a large-scale commercial basis. Public procurement for innovation does not primarily aim to develop new products but to promote a policy instrument which will target functions that satisfy human needs.(25)

Public procurement for innovation can be identified on the demand side where participants act as technologically demanding customers that buy the development and testing of new solutions. “This enables European public authorities to modernize public services faster and to create opportunities for companies in Europe to take international leadership in new markets”.(26)

For example, the public procurement for innovations solution uses procurement as a catalyst, in the sense that authorities are putting money into the “development and prototyping of innovations that have a strong societal value and for which there is a clear identified market failure”.(27)

## 4. State Aid for R&D&I

State aid is another important tool for fostering R&D&I. State aid is subjected to tight control, as an important part of the EU’s competition policy, because free and undistorted competition requires that not only private actors adopt a pro-competitive behavior but also that State intervention on the market shall be subject to different means of control. According to European Union law, it is illegal for Member States to give financial help to some undertakings and not to others in a way which would distort fair competition. This help is deemed to be State aid, and the rules barring it are enforced by the European Commission and national courts. Article 107 of TFEU states that “any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favoring certain undertakings or the production of certain goods shall, in so far as it

(24) EC, “Smart Specialization Platform Pre-commercial procurement & public procurement of innovative solutions”.

(25) C. EDQUIST, N.S. VONORTAS, J.M. ZABALA-ITURRIAGAGOITIA and J. EDLER, *Public procurement for innovation*, *op. cit.*, p. 7.

(26) EC, “Digital Single Market, Pre-Commercial Procurement”.

(27) *Final Report Feasibility study on future EU support to public procurement of innovative solutions: Obtaining Evidence for a Full Scheme [Contract Notice 2010/S 103-155769]*.

affects trade between the Member States, be incompatible with the internal market”.

Depending on the Community applicable legal basis, State aid is classified as either: (a) aid for which notification is required; (b) aid exempted from notification; (c) *de minimis* aid.

The need to notify an aid measure is determined by reporting the maximum amount of aid that Member States intend to grant under the thresholds established under Regulation (EU) No. 651/2014 (GBER) which declares certain categories of aid compatible with the common market in application of Articles 107 and 108 TFEU.

In the case of notified aid, the Commission shall examine the notification as soon as it has been received. If the information provided is incomplete, the Commission requests additional information. Within two months of receipt of the notification, the Commission shall take one of the following decisions: there is no aid within the meaning of the EU rules, and the measure may be implemented; the aid is compatible with EU rules, because its positive effects outweigh distortions of competition, and may be implemented; serious doubts remain as to the compatibility of the notified measure with EU State aid rules, prompting the Commission to open an in-depth investigation. In this instance, the measure may not be implemented until the investigation is concluded.(28)

Under the *formal investigation procedure*, the European Commission will assess the compatibility of the aid measure with Community State aid rules. The formal investigation procedure shall be closed by means of a decision as follows:(29) positive decision: where the measure is no aid or the aid is compatible with the Internal Market; conditional decision: the measure is found compatible, but its implementation is subject to the conditions stated in the decision; negative decision: the measure is incompatible and cannot be implemented. The Commission in principle orders the Member State to recover aid that has already been paid out from the beneficiaries.(30)

In the case of unlawful aid, the Commission may initiate its own investigation or commence an investigation following a complaint from the concerned persons.

Aid that complies with the conditions set out in GBER is compatible with the Internal Market and there is no need for notification or any authorization

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(28) Art. 4 of the Council Regul. (EU) No. 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union (Text with EEA relevance).

(29) Art. 9 of the Council Regul. (EU) No. 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union (Text with EEA relevance).

(30) EC, “State Aid Procedures”.

from the European Commission. In this case a simple information notice is sufficient.(31)

In the case of *de minimis* aid – whose total amount granted per Member State to a single undertaking shall not exceed € 200.000 over a period of three fiscal years – there is no obligation to notify the European Commission or the obligation to inform the Community forum after the implementation of such a measure. The procedural rules on *de minimis* aid are exclusively set at the level of the Member State.(32)

Given the considerable amount of finance needed for research and development projects, the Commission has adopted a favorable view of State Aid for R&D since 1986 when the first *Framework* on the matter was adopted.(33) Ever since, the State Aid package entered a modernization process.(34) The current *Framework for State Aid for R&D&I*(35) has as an objective of promoting the faster modernization of public services by supporting the potential buyers of innovative solutions. The State Aid Framework for R&D&I sets out the grounds for granting State aid to companies that will carry out R&D&I activities.

State aid for R&D&I shall ensure that innovative ideas can be turned into products and services that create growth and jobs. Aid for R&D&I will be justified on the basis of Articles 107(3)(b)(36) and 107(3)(c)(37) of the Treaty, according to which State aid for R&D&I may be considered by the Commission compatible with the Internal Market, when it promotes the execution of an important project of common European interest or when it supports the development of certain economic activities, with the condition that the competition is not distorted contrary to the common interest.

(31) See GBER, Annex II.

(32) EC, Commission Regul. (EU) No. 1407/2013 of 18 December 2013 on the application of Art. 107 and 108 of the TFEU to *de minimis* aid, recital 1.

(33) EC, “Community framework for State aid for Research and Development”, *OJEC*, C 83:2 of 11 April 1986.

(34) The role of research and development in improving growth, competitiveness and employment was then debated in the Community framework for State aid for research and development, *OJEC*, C 045 of 17 February 1996, pp. 5-16, followed by the framework from 2006 (*OJEC*, C 323 of 30 December 2006) and they were both used for the assessment of aid for research and development and innovation which is notified to the Commission.

(35) Regul. (EU) No. 651/2017 of 17 June 2014 (General Block exemption Regulation – GBER) and the Framework for State aid for research, development and innovation, Com. Comm., C (2014)3282, 21 May 2014.

(36) Art. 107(3)(b) from the Treaty, “The following may be considered to be compatible with the internal market aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State”.

(37) Art. 107(3)(c) from the Treaty, “The following may be considered to be compatible with the internal market aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest”.

R&D that can be financed by State aid with no notification to the Commission is included in the new General Block Exemption Regulation (GBER).<sup>(38)</sup> GBER exempts some categories of State aid from notification and plays an essential role given the fact that it expands the scope of measures that no longer need to be notified to the Commission for prior approval. R&D is among the exempted areas under certain conditions, so granting State aid for R&D&I does not fall under the remit of article 107 from the Treaty when State aid targets non-economic activities.<sup>(39)</sup> The current rules involve a greater flexibility because it expands the categories of aid allowed in this field.

GBER lays down in section 4 the rules for granting State aid for R&D&I by emphasizing the condition that must be fulfilled in order to exempt the aid given for research and development from the notification requirement imposed by the Article 108(3) of the Treaty. So, if the aid is intended for research and development projects (Art. 25) or if it is an investment aid for research infrastructures (Article 26), aid for innovation clusters (Art. 27), innovation aid for SMEs (Art. 28), start-up aid for small and innovative enterprises (Art 22-5), aid for process and organizational innovation (Art. 29), or if it is an aid for research and development in the fishery and aquaculture sector (Art. 30), then it shall be considered compatible with the Internal Market within the meaning of Article 107(3) of the Treaty.<sup>(40)</sup>

RDI financing can fall outside State aid rules in its entirety if the economic use of a research infrastructure is purely ancillary, meaning that where an infrastructure is used for both economic and non-economic activities, the funding through State resources of the costs linked to the non-economic activities of the infrastructure does not constitute State aid. The same will be the conclusion where the infrastructure is used almost exclusively for a non-economic activity, or for an economic activity which is directly related to and necessary for the operation of the infrastructure or intrinsically linked to its main non-economic use, and is limited in scope.<sup>(41)</sup>

(38) Regul. (EU) No. 651/2014 of 17 June 2014, declaring certain categories of aid compatible with the internal market in application of Art. 107 and 108 of the Treaty.

(39) Par. 18 of Comm. Com., “Framework for State aid for research and development and innovation”, states that: “Where the same entity carries out activities of both economic and non-economic nature, the public funding of the non-economic activities will not fall under Article 107(1) of the Treaty if the two kinds of activities and their costs, funding and revenues can be clearly separated so that cross-subsidisation of the economic activity is effectively avoided. Evidence of due allocation of costs, funding and revenues can consist of annual financial statements of the relevant entity”. Further on, par. 19 of the Framework includes “independent R&D for more knowledge and better understanding, including collaborative R&D where the research organisation or research infrastructure engages in effective collaboration” in those activities which Commission considers activities with a non-economic character.

(40) B. VON WENDLAND, “New Rules for State Aid for Research, Development and Innovation: ‘Not a Revolution but a Silent Reform’”, *EStAL*, 1/2015, p. 25.

(41) Recital, 49 GBER 2014, par. 20, RDI Framework 2014.

The regulation has adopted these special detailed provisions in new areas such as investment aid for research infrastructures, aid for innovation clusters, innovation aid for SMEs, aid for process and organizational innovation and aid for research and development in the fishery and aquaculture sector to ease the assessment by the Commission when analyzing the compatibility of such measures with the Internal Market. Finally, given the importance of granting State aid for R&D&I, the current GBER has doubled the notification thresholds for research and development projects from the previous one.(42)

### ***5. Public Procurement for Innovation vs State Aid for Innovation***

The link between State aid and procurement is clearly stated in the Commission's Communication – Framework for State aid for research and development and innovation,(43) which lays down the principles applicable to State aid granted to undertakings carrying out R&D&I, defines pre-commercial procurement and R&D projects, and points out the conditions to fulfill for the ongoing PCPs and PPI not to involve granting of illegal State aid.

In this section, we will compare the use of public procurement and State aid for fostering innovation, advantages and challenges for each legal tool. The comparison will look at the procedure of awarding/granting financing and at data regarding the use of the two mechanisms.

As to the procedure, the following conclusions may be drawn:

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(42) Art. 4(1) from Regul. (EU) No. 651/2014: this Regulation shall not apply to aid which exceeds the following thresholds:(i) for aid for research and development: (i) if the project is predominantly fundamental research: EUR 40 millions per undertaking, per project; that is the case where more than half of the eligible costs of the project are incurred through activities which fall within the category of fundamental research; (ii) if the project is predominantly industrial research: €20 millions per undertaking, per project; that is the case where more than half of the eligible costs of the project are incurred through activities which fall within the category of industrial research or within the categories of industrial research and fundamental research taken together; (iii) if the project is predominantly experimental development: €15 millions per undertaking, per project; that is the case where more than half of the eligible costs of the project are incurred through activities which fall within the category of experimental development; (iv) if the project is a Eureka project or is implemented by a Joint Undertaking established on the basis of Article 185 or of Article 187 of the Treaty, the amounts referred to in points (i) to (iii) are doubled; (v) if the aid for research and development projects is granted in the form of repayable advances which, in the absence of an accepted methodology to calculate their gross grant equivalent, are expressed as a percentage of the eligible costs and the measure provides that in case of a successful outcome of the project, as defined on the basis of a reasonable and prudent hypothesis, the advances will be repaid with an interest rate at least equal to the discount rate applicable at the time of grant, the amounts referred to in points (i) to (iv) are increased by 50%; (vi) aid for feasibility studies in preparation for research activities: €7,5 millions per study.

(43) 2014/C 198/01.

- Public procurement for innovation is harder to compare to State aid because it regards the purchase of final products/services and not only the process of developing such products and services. Pre-commercial procurement, on the other hand, is easier to compare because it can finance just the R&D activities without the purchase of the final product. However, the specificity of State aid when requiring results is less astute than in the case of a public procurements procedure, which identifies with more precision the end results of the R&D activities.
- The procedure for awarding public contracts takes as long as 108 days (average) based on an estimate of the European Commission from 2011,(44) while the time for granting State aid that is notified to the Commission is 6 months on average and can reach 20 months if a formal investigation is opened.(45)
- PCP and (less so) PPI can be assessed against their interaction with State aid. More precisely, the problem that has arisen in practice about PCP, for example, was that these procedures had to focus on showing the best solution for special needs of contracting authorities, but without getting to unilateral State aid. Because in PCP the contracting authorities do not keep the R&D results exclusively for their use, pre-commercial procurement must be understood as an approach to procuring R&D services/products, by sharing the risks and benefits with the supplier in a manner that will not constitute State aid.

Nevertheless, PCP and PPI have their advantages: if undertakings received from a contracting authority include the right to spend money on research, innovation and development of new technologies, the risk of investing in R&D is reduced, from the point of view of the contracting authority. The resort to PCP and PPI practically improves the quality of the public service offered to the citizens of Europe through the deployment of innovative goods and services.

When there is a constant disparity between risk – benefit sharing, and especially when the price paid for the R&D&I product is higher than market price, there is the risk of confronting State aid that will normally have to be notified to the Commission, as required by the Treaty.

- When looking at the rate of R&D financing through the use of the two mechanisms, we realize that the share of public procurement for innovation and that of State aid for innovation is difficult to compare.

(44) Study prepared for the EC, “Public procurement in Europe. Cost and effectiveness”.

(45) EU Comm., “State aid: Commission adopts Best Practices Code and Simplified Procedure to accelerate State aid decisions – frequently asked questions”, MEMO /09/208, Brussels, 29 April 2009.

Public expenditure on research and development and innovation is a key factor for the EU's efforts in reaching its Europe 2020 strategy. Accordingly, the EU hopes to spend 3% of gross domestic product (GDP) on R&D activities, by 2020, which would create 3.7 million jobs and increase annual GDP by close to €800 billion by 2025. The percentage of R&D expenditure by source of funding shows for instance that more than half (55.3 %) of the total expenditure in R&D field in 2014 around EU came from business enterprises, with only one third (32.3%) funded by government, and a further 10.0 % from abroad (foreign funds).(46) R&D expenditure in the EU reached 2.04% of GDP in 2014, up from 1.77% in 2007.(47)

Public procurement stands for an estimated 16% of the European Union's GDP,(48) and according to a Commission report, around one in twenty companies have been involved in the Public Procurement of Innovative Solutions (data for 2011),(49) and about four in ten companies (38%) that have won a public procurement contract included innovations as part of the winning bid (data for 2012-2015).(50) In 2012 according to European Commission a quarter (24%) of public procurement interactions included the possibility of selling an innovation to the government, whilst in 2015 more than one third (38%) say they included innovations as part of a public procurement that they won.(51) As to the 'innovation' content of the European procurement actions, 2006-2010, in percentage of actions, the following table is to be mentioned:

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(46) Eurostat, R&D expenditure.

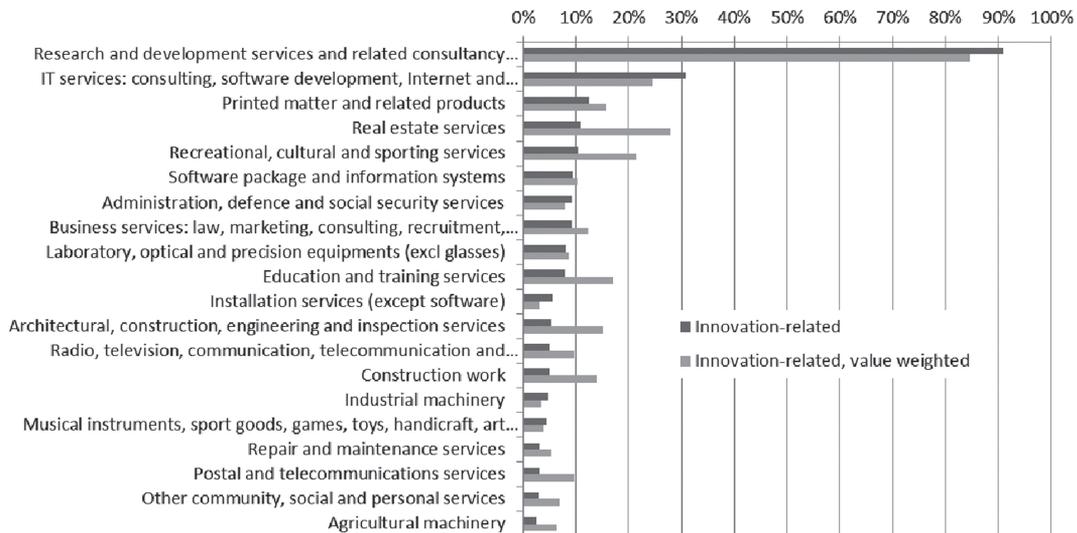
(47) Eurostat Statistics, Europe 2020 indicators – R&D and innovation.

(48) EU Comm. policy, "Accessing markets, Public procurement".

(49) EU Comm., "State of the Innovation Union 2011", COM/2011/0849 final.

(50) EU Comm., Flash Eurobarometer 415 Innobarometer 2015 – The Innovation Trends At EU Enterprises.

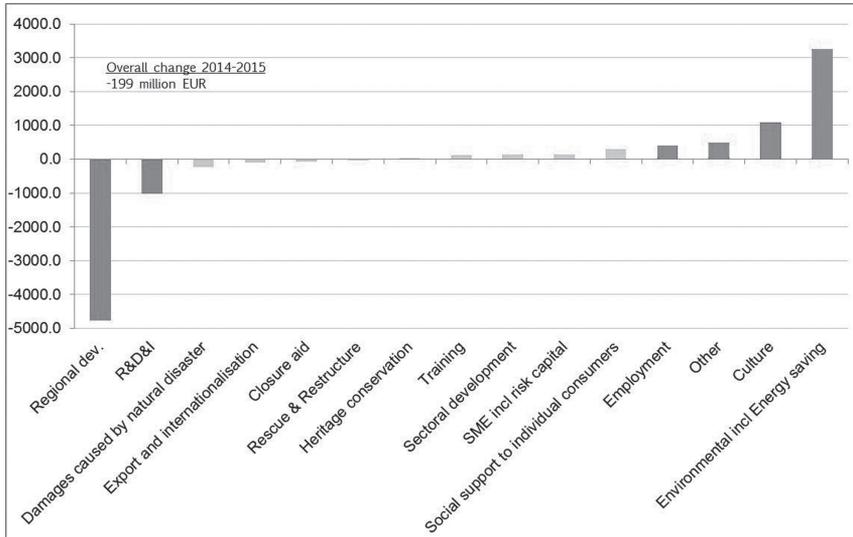
(51) Flash Eurobarometer 343, Innovation in the Public Sector: its Perception in and Impact on Business, 2015 – The Innovation Trends at EU Enterprises.



\*Source: OECD analysis of TED data.

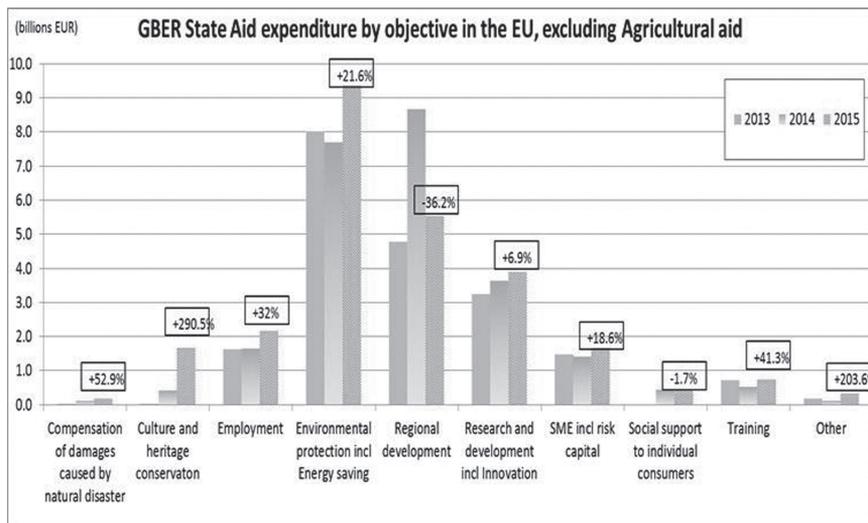
Regarding State aid, the 2016 State Aid Scoreboard from the Commission<sup>(52)</sup> reveals that aid expenditure made by Member States before 2016 which falls under the scope of Article 107(1) TFEU was around €98 billion, standing for 0.67% of EU GDP.

(52) State Aid Scoreboard 2016.



\*Source: State Aid Scoreboard 2016

The new General Block Exemption Regulation (GBER) which tried to simplify the procedure of granting State aid had a certain impact in State aid for R&D&I, by increasing the not-notified State aid (GBER exempted) spending for this kind of activities.



\*Source: State Aid Scoreboard 2016

It is very complicated to actually compare the share of the two instruments in promoting innovation, as they both involve a certain degree of approximation. The almost 4 billion euros (excluding agriculture!) from GBER adds up to the 98 million that falls under the notification procedure requirements. In public procurement, only by approximating the share of innovative procurement starting from the 16% from the GDP (which was in 2016 16.5 trillion euros) we can conclude roughly that public procurement is worth 2.64 trillion euros and procurement for innovation is a portion of that. How big of a portion is hard to estimate, as all the studies are looking at the percentage of companies that included innovation in their bids, and not the actual worth of such procurements.

- Transparency: procurement for R&D&I must observe the principles from the Treaty and from the 2014 Directives: transparency, value for money, non-discrimination, equal treatment, mutual recognition, proportionality.<sup>(53)</sup> State aid granted for R&D&I should in theory comply with these principles but for example the transparency requirement is specific to the State aid *control*, not to the procedure of granting the State aid, which is conducted between initiator and deciding authorities and away from the public eye.<sup>(54)</sup> Even considering that since July 2016, the transparency requirement has entered into force for State aid as well, and became a principle of State aid procedure on the basis of Article 9 and annex III of GBER,<sup>(55)</sup> the transparency is not similar to the one imposed to procurement procedures. In public procurement procedures transparency is present in all phases of the awarding procedure, beginning with the preliminary market consultations and finalized with the conclusion of the contract.<sup>(56)</sup> The goal of the transparency requirement in granting State aid is to promote a higher responsibility of granting authorities and to minimize uncertainties on the market, whilst the purpose of the transparency in public procurement is linked to undermining corruption, and to promoting the efficient spending of public money.<sup>(57)</sup>
- The goals of public procurement for R&D&I and of State aid for the same activities reveal a long-term different perspective. Public procurement for R&D&I aims to bring beneficial effects on the demand side and focuses on the best allocation of public funds. In public procurement for

<sup>(53)</sup> Recital 1, Dir. 2014/24/EU.

<sup>(54)</sup> Complementary information on all authorized State aid in the EU, including information in relation to the transparency requirement, can be found online on the State aid Transparency public search page, which gives access to State aid individual award data provided by Member States.

<sup>(55)</sup> EU Comm., State aid control.

<sup>(56)</sup> Art. 40, Dir. 2014/24/EU.

<sup>(57)</sup> Transparency and public procurement, *Supplement to the 2011 Annual Statistical Report on United Nations Procurement*.

innovation the behavior of the supply side is primarily in the background rather than the foreground. Public procurement for innovation focuses on the way authorities spend public money when buying innovative goods or services. On the other hand, State aid may be compatible with the Internal Market only where there has been a market failure, so that the Commission is entitled to refuse to authorize the aid, when it considers the State intervention is not necessary in the public market.(58)

- The hypotheses that justify State aid and public procurement for R&D&I are very different. The most common justification for granting State aid for R&D&I is the need of the State to correct market failures, by enhancing competitiveness. However, granting State aid does not exclusively presuppose the existence of market failures: it is also applicable in situations when although the outcome is efficient, the delays make an intervention of State aid far more satisfactory.(59) State Aid for R&D&I has a highest goal of encouraging companies to undertake more research than they would otherwise take on under other market conditions. In reverse, State aid for R&D&I may distort competition (for example by reducing the rival companies' possibilities to invest or by enabling the beneficiary to engage in exclusionary practices whilst other competitors that did not receive aid are excluded from the market). Potentially negative side effects must then be avoided when granting State aid for R&D&I. Theoretically, Article 33 from the Framework for State aid for research and development and innovation,(60) explains how to avoid State aid in public R&D procurement.

Public procurement as an instrument for innovation can also be justified by market failure, but usually on the supply side, while its main justification

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(58) For further discussions on the structure and the goals of State Aid, see C. QUIGLEY, *European State Aid Law and Policy*, 3rd ed., Oxford, Hart Publ., 2015.

(59) Regul. (EU) No. 651/2014, aforesaid.

(60) Art. 33, "In all other cases, including pre-commercial procurement, the Commission will consider that no State aid is awarded to undertakings where the price paid for the relevant services fully reflects the market value of the benefits received by the public purchaser and the risks taken by the participating providers, in particular where all of the following conditions are fulfilled: (a) the selection procedure is open, transparent and non-discriminatory, and is based on objective selection and award criteria specified in advance of the bidding procedure, (b) the envisaged contractual arrangements describing all rights and obligations of the parties, including with regard to IPR, are made available to all interested bidders in advance of the bidding procedure, (c) the procurement does not give any of the participant providers any preferential treatment in the supply of commercial volumes of the final products or services to a public purchaser in the Member State concerned 29, and (d) one of the following conditions is fulfilled: – all results which do not give rise to IPR may be widely disseminated, for example through publication, teaching or contribution to standardisation bodies in a way that allows other undertakings to reproduce them, and any IPR are fully allocated to the public purchaser, or – any service provider to which results giving rise to IPR are allocated is required to grant the public purchaser unlimited access to those results free of charge, and to grant access to third parties, for example by way of nonexclusive licenses, under market conditions".

remains helping public authorities to achieve more efficiency, effectiveness and performance of the public sector.

The impact of procurement of R&D is not that big when it's done individually and not by a central purchasing body or through collaborative procurement. While State aid can reach many companies at the same time and foster innovation by financing research and development, the power of contracting authorities to influence the market by individual or even bundled procurement is reduced. However, procurement for innovation can be pursued at the initiative of any contracting authority and thus the volumes that it triggers are larger. The initiative of contracting authorities to propose State aid to the central government are rare. Here the initiative comes from the central government or comes attached to EU structural funds financing.

Administrative capacity plays an important role when it comes to procurement for innovation, as many public officials lack the expertise to engage in such procedures confidently. In transposing new directives into national law, Member States should ensure that procurement personnel receive training in the application of the new legislation and that regional contracting authorities do not lack the appropriately prepared staff. On the State aid side, the fact that it is decided at the central level means the need for expertise is concentrated in ministries and thus easier to assemble. State aid measures are designed and approved at the central level, which in theory at least benefits from better expertise when it comes to market assessment, so from this point of view State aid tools seem to be preferable when the State intends to advance its innovative agenda.

The procurement Directives aim to ensure that local authorities can make use of both PPI and PCP. Public procurement for innovation could be financed by local authorities, and less by the State or regional authorities. However, the administrative capacity to conduct such procedures is the other way around. On the other hand, State aid is not that used by local authorities even though it is important to mention that the expression 'through State resources' from the definition on State aid (taken from Art. 107 TFEU) may include (rarely) the use of local authority funds. When speaking of State aid an overwhelming proportion is represented by the regional aid which is allowed especially for ensuring the regional development.(61)

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(61) The *Guidelines on regional State aid for 2014-2020* states that: "Regional aid can further be effective in promoting the economic development of disadvantaged areas only if it is awarded to induce additional investment or economic activity in those areas. In certain very limited, well-identified cases, the obstacles that these particular areas may encounter in attracting or maintaining economic activity may be so severe or permanent that investment aid alone may not be sufficient to allow the development of that area. Only in such cases may regional investment aid be supplemented by regional operating aid not linked to an investment". Information from European Union Institutions, Bodies, Offices and Agencies European Commission.

The thresholds for applying the EU Public procurement rules are set out at Article 4 of the Directive 2014/24/EU at around 5 million euros for works and 134,000 euros for services and products. This means that above these thresholds the innovative partnership can be used as a procedure for awarding contracts. However, this does not prevent contracting authorities from including innovation requirements in below threshold procurements. Regarding State aid for R&D&I, we can notice a tendency towards flexibility<sup>(62)</sup> under the GBER, which increased the threshold amounts below which aid is exempted from notification, meaning that it does not have to be notified to the Commission for approval. For example, Member States can now grant aid for experimental development of up to €15 million per project and per beneficiary without prior Commission approval, as compared to €7.5 million under the previous rules. Moreover, the scope of aid measures for R&D&I projects that can be exempted from notification under the GBER has also been widened. It now extends to pilot projects and prototypes, innovation clusters and aid for process and organizational innovation.<sup>(63)</sup>

When procuring R&D&I products or services contracting authorities may encounter a number of specific and inherent obstacles. For instance, technological risks may arise in all stages of the procurement process, when the suppliers are not able to find in practice the innovative solution as presented in the bid package. This might happen when choosing the improper technology or when the chosen technology even is suitable in theory, it does not match standards in practice.

On the other hand, authorities considering granting State aid measures for R&D&I must define their purpose and the aim they pursue, provided that they identify, from the very beginning of the procedure, the outcome of the measures adopted in R&D&I field.

In both public procurement for innovation and the procedure of granting State aid for R&D&I an important role is given to control. State aid control aims at pursuing the EU's joint interest and its rationale relates to distortions of competition through State subsidies to private or public companies that are in active or potential competition with other companies.<sup>(64)</sup>

The relationship between public procurement and State aid control rules has been controversial for some time. The underlying idea is that compliance with

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(62) Another example of flexibility is the new rule of ancillary economic activities Framework, Cf. B. von WENDLAND, "New Rules for State Aid for Research, Development and Innovation: 'Not a Revolution but a Silent Reform'", cit., p. 20.

(63) European Commission Press Release Brussels, "State aid: Commission adopts new rules facilitating public support for research, development and innovation", 21 May 2014.

(64) J. HAUCAP and U. SCHWALBE, *Economic Principles of State Aid Control*, Düsseldorf, Heinrich-Heine-Universität, Department of Economics, Düsseldorf Institute for Competition Economics (DICE), 2011.

procurement rules of the awarding procedure excludes the element of ‘undue economic advantage’ (or, even further, the prerequisite of ‘selectivity’) – consequently eliminating all risks of disguised granting of State aid by means of public contracts.(65)

In any innovative procurement procedure, we should mention the fact that small firms and not-for-profit organizations are particularly disadvantaged. That is why it would be better if contracting authorities establish better communication channels with the economic operators. It is also important that SMEs, with their less extensive networks, should be included into procurement procedures aiming to reach R&D&I. In addition, compared to State aid, procurement of innovation may be beneficial for SMEs to have an access to business opportunities and resources, which they might have difficulty in accessing through State aid. State aid for innovation for SMEs remains underused even though the *Framework for State Aid for R&D&I* provides, with regard to small and medium-sized enterprises, that innovation aid may be awarded for obtaining, validating and defending patents and other intangible assets, for the secondment of highly qualified personnel, and for acquiring innovation advisory and support services. Moreover, in order to encourage large enterprises to collaborate with SMEs in process and organizational innovation activities, the costs incurred by both SMEs and large enterprises for such activities may also be supported.(66)

## 6. Final Considerations

This paper can be useful in offering a perspective on the legal and practical issues involved in the use of procurement and State aid in the area of research, development and innovation, although it just touches lightly on the issues that may be raised in relation to the two legal approaches. There is no clear-cut conclusion on which of the two models of State intervention in the economy is more prone to bring about innovation. In terms of quantities, the quotas of public procurement and State aid for innovation in the EU GDP are difficult to compare without further economic estimates.

The big expectations from public procurement for R&D&I as established in 2020 Agenda seem attainable through the use of the two instruments analysed here: public procurement and State aid. However, public procurement, as part of the EU demand-oriented innovation policy, needs new forms of coordination and governance, reconciling at least three different logics: the efficiency

(65) A. SANCHEZ-GRAELLS, “Public Procurement and State Aid: Reopening the Debate?”, *PPLR*, forthcoming.

(66) EU Comm., “Framework for State aid for research and development and innovation”, 2014/C 198/01, Art. 12, d.

logic (for the buyer, value for money), the broader economic logic (direct effect on producers, value chains, spillovers to private demand) and the sectoral policy logic (to deliver goods/better public service/societal effects).(67) State aid needs to be more transparent and administrative capacity at the local level needs to be strengthened in order for State aid rules to be accommodated effectively.

Establishing better communication channels with the economic operators should be a priority for both approaches. It is important that SMEs, with their less extensive networks, should be included in communications by public agencies so that the SMEs' innovative capabilities can be utilized. Market consultations before launching a procurement procedure for innovation as well as innovation fairs where public procurers meet possible tenderers and discuss a possible way of innovating existing products and services should be organized more often. State aid is sometimes designed at the initiative of companies in the market, so the link with the needs of the market is already present.

The contractual regime in awarding procedures should also be optimized to encourage innovation. The parties should agree from the very beginning on the rights to intellectual property by deciding which party has the right to further use the innovative product in other markets. The innovative products or services that are developed as a result of State aid remain with their developers, while as in procurement for innovation there is the option to buy them at the end. As stated in the 2011 updated Report from The Commission *State Aid Scoreboard Report on State aid contribution to Europe 2020 Strategy*, State aid can contribute to generate more R&D&I only if it addresses well-identified market failures, which prevent markets from reaching optimal R&D&I levels, and if it is well designed by ensuring that distortions of competition and trade are minimized and public spending efficiency is maximized.(68)

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(67) EU, Directorate-General for Research European Research Area, Expert Group Report on *Risk management in the procurement of innovation Concepts and empirical evidence in the European Union*, Brussels, 2010, p. 19.

(68) EU Comm., "A European Agenda For The Collaborative Economy", COM/2011/0356 final, available at [eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2016:356:FIN](http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2016:356:FIN).



**CHAPTER 11**  
**The U.S. Small Business Innovation Research (SBIR)**  
**Program: A Comparative Assessment**

BY

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Like many other nations around the world, the United States aggressively pursues technological innovations that contribute to its continuing economic and strategic success. The U.S. government's procurement system enables the government to use multiple methods to develop and procure technology. One method is the Small Business Innovation Research (SBIR) program, which funds small businesses to develop these innovative solutions. The SBIR program was in important ways an inspiration for the European Union's 'innovation partnerships', which similarly fund research and development through European procurements in a three-phase process.<sup>(1)</sup>

The U.S. Congress established the SBIR program 35 years ago specifically to foster small business participation in technological research and development (R&D), and Congress funds the SBIR program by 'taxing' the major R&D budgets at other agencies. SBIR participants proceed through three phases, during which the participants foster an idea from a small-scale prototype, to stable product, and eventually to a tailored technology solution suiting the government's (and the commercial market's) needs. To support small businesses participating in the program, the SBIR program takes a uniquely liberal approach to competition requirements and data rights in procurements involving technology developed under the program, compared to typical procurement methods. Currently, eleven federal agencies participate in the

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(1) See, e.g., European Commission, "Innovation Partnerships Keep Public Services Up to Date", 3 March 2016, [ec.europa.eu/growth/content/8699-innovation-partnerships-keep-public-services-date\\_en](http://ec.europa.eu/growth/content/8699-innovation-partnerships-keep-public-services-date_en); M. ANDHOV, "Innovation Partnership in the New Public Procurement Regime – A Shift of Focus from Procedural to Contractual Issues?", 24 *Pub. Proc. L. Rev.*, 2015, p. 18, available at [ssrn.com/abstract=2910911](http://ssrn.com/abstract=2910911).

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SBIR program, among them the Department of Defense (DoD), which spends over \$1 billion per year funding technology projects in the first two phases.

To offer a case study for other countries' 'innovation partnerships', this paper focuses specifically on the DoD's use of the SBIR program and the challenges the Defense Department faces in demonstrating success in the third phase, during which SBIR technologies transition into military systems for use in the defense mission. This paper seeks to identify measures of the SBIR program's success, and to offer preliminary conclusions as to whether the SBIR program presents useful contracting methods to increase small business participation in research and development, and whether the SBIR program provides meaningful transition of new technologies to DoD projects.

## 1. Introduction

The United States Small Business Innovation Research (SBIR) program dedicates a portion of its website, [www.sbir.gov](http://www.sbir.gov), to its success stories. Procurement programs worldwide have copied tenets of the program, advocates for small business declare its economic importance, and federal agencies assert that the program has afforded important cost savings and value to U.S. innovation. But are these claims alone sufficient to conclude that the program is successfully delivering innovative technology into the hands of government users?

Over the past 35 years, the SBIR program, established through statute and executive order, has emerged as a leading method to foster small business participation in research and development (R&D) in the U.S. federal government. The U.S. Small Business Administration (SBA) administers the program and is responsible for ensuring its success. (The SBA's *Policy Guidance* for the SBIR program sets forth the program's central legal requirements). The SBIR program includes three phases, during which program participants advance an innovation from a small-scale prototype in Phase I, to a stable product in Phase II, and eventually to a tailored technology solution suitable for government (and often commercial) use in Phase III.

Currently a large number of federal agencies – those with R&D budgets over \$100 million per year – participate in the SBIR program: the Department of Agriculture, the Department of Commerce (including the National Institute of Standards and Technology (NIST)), and the National Oceanic and Atmospheric Administration (NOAA), the Department of Defense (DoD), the Department of Education, the Department of Energy, the Department of Health and Human Services (HHS), the Department of Homeland Security (DHS), the Department of Transportation (DOT), the Environmental Protection Agency (EPA), the National Aeronautics and Space Administration (NASA), and the

National Science Foundation (NSF). Each agency with an R&D budget over \$100 million must contribute, by law, at least 3.2% of its R&D budget to the SBIR program.<sup>(2)</sup> Because of the DoD's large R&D budget, DoD agencies are leading users of the SBIR program.

The SBIR program has always been a source of controversy, in part because of the enforced 'taxation' which funds the program (and draws resources from more traditional R&D projects), and in part because of the special preferences (discussed below) for technologies that emerge from the program.<sup>(3)</sup> As recently as January 2018, two agencies of the U.S. government published sometimes conflicting perspectives on the SBIR program's effectiveness. The first report was from the Section 809 Panel, a blue-ribbon panel commissioned by Congress in Section 809 of the National Defense Authorization Act of 2016<sup>(4)</sup> to study opportunities to improve DoD acquisitions by updating the DoD's procurement rules. Volume I of the Section 809 Panel's report recommended that the Defense Department leverage the SBIR program's successes to "advance warfighting capabilities and capacities", and further suggested permanent policy changes to incentivize use of the SBIR program. The Section 809 Panel referenced reports of 'positive outcomes', noting that the government has received "high quality and innovative proposals" and that small business participants are receiving venture capital to further subsidize their innovations.<sup>(5)</sup> The Section 809 Panel report was not entirely positive, however. The panel also concluded that the SBIR program "lacks speed, agility, and flexibility", and that the "program's processes are increasingly onerous".<sup>(6)</sup>

The second mixed report was from the U.S. Government Accountability Office (GAO), an agency within the legislative branch which audits and investigates government agencies on behalf of Congress. This report summarized the SBIR program and determined that due to "challenges in collecting and verifying the accuracy of data", it was unclear if the program was meeting its own benchmarks. The report sharply concluded that although "federal agencies have awarded billions of dollars to small businesses to help these businesses

(2) U.S. Small Business Administration, "About SBIR", [www.sbir.gov/about/about-sbir](http://www.sbir.gov/about/about-sbir).

(3) See, e.g., I.M. SILVERMAN, J.M. DAWICKI-MCKENNA, D.W. FREDERICK, C. BIALAS, J.R. REMSBERG, N.L. YOHN, N. SEKULIC, A.B. REITZ and D.M. GROSS, "Evaluating the Success of the Small Business Innovation Research (SBIR) Program: Impact on Biotechnology Companies in Pennsylvania", *Tech. Transfer & Entrepreneurship*, 4, 2015, p. 5: "It remains controversial whether this form of private enterprise stimulation is a productive use of federal funding that might be better spent supporting university-based research. Additionally, there is growing concern that changes to the law allowing for majority venture-backed companies to compete for SBIR awards could crowd out companies that lack other sources of funding", [pdfs.semanticscholar.org/7957/1a1e078b85930bf3bc8f80e466ef004cc566.pdf](https://pdfs.semanticscholar.org/7957/1a1e078b85930bf3bc8f80e466ef004cc566.pdf).

(4) Public Law No. 114-92, 114<sup>th</sup> Cong., 1<sup>st</sup> Sess., 129 Stat. 726, 2015.

(5) Section 809 Panel, *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations*, Vol. 1, January 2018, pp. 182-184, [section809panel.org/wp-content/uploads/2018/04/Sec809Panel\\_Vol1-Report\\_Jan18\\_REVISIED\\_2018-03-14.pdf](http://section809panel.org/wp-content/uploads/2018/04/Sec809Panel_Vol1-Report_Jan18_REVISIED_2018-03-14.pdf).

(6) *Ibid.*, p. 4.

develop and commercialize innovative technologies [...] assessments have been based on inaccurate or incomplete data”.(7)

There is no doubt that technological innovation is key to achieving the Defense Department’s mission, and supporting that innovation through procurement is an essential process. To those ends, this paper will describe the foundational aspects of the SBIR program, review and identify by what measures the SBIR program has been successful, compare the program with the ‘innovative partnership’ initiative in the European Union (EU), and assess whether the SBIR program is merely a useful means of leveraging procurement to increase small business participation in R&D, or a more meaningful means of transitioning new technology to Defense Department projects.(8)

## ***2. The SBIR Program: Description***

To gain admission to the SBIR program, small businesses develop proposals to conduct experimentation, analyses, and early-stage development of technology ideas that may be useful to U.S. government agencies and/or commercial industry. Rather than relying merely on internal funds or investor venture capital to pursue these technically risky endeavors, small businesses receive federal funding to cover these ‘Phase I’ costs. Technology projects typically experience funding shortfalls, colloquially called the ‘Valley of Death’, during the period between initial development and commercialization of a technology.(9) One goal of the SBIR program is to bridge this gap for small businesses by providing more stable federal funding, compared to private investor funding. Nevertheless, as is discussed below, foundering in this ‘valley’ is still a frequent occurrence in the SBIR program for firms between award phases.

The SBIR program also allows participating businesses to retain intellectual property (IP) rights to the ideas and products they generate during the program; these IP rights are critical to selling the final products. The first two phases are funded via federally-provided SBIR contracts as the products take shape. The final phase is reserved for tailored development of nearly-production-ready products to suit the specific and verified needs of DoD customers, paid for by the receiving organization.

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(7) U.S. Government Accountability Office, “Small Business Research Programs: Agencies Need to Take Steps to Assess Progress Toward Commercializing Technologies”, *GAO 18-207*, 2018, [www.gao.gov/products/GAO-18-207](http://www.gao.gov/products/GAO-18-207).

(8) Because of the size and strategic importance of the U.S. Department of Defense’s SBIR program, this paper will focus on that agency.

(9) See, e.g., Y. OSAWA and K. MIYAZAKI, “An Empirical Analysis of the Valley of Death: Large-Scale R&D Project Performance in a Japanese Diversified Company”, 14 *Asian J. Tech. Innovation*, 2006, p. 93.

To understand the SBIR program's value, it is important to understand its purpose and structure. This section describes the program's codification, its phased approach to maturing innovations, and measurements of its success transitioning those innovations to DoD projects.

## 2.1. Governing Statutes and Policies

The SBIR Program is codified at Section 9 of the Small Business Act, 15 U.S.C. § 638.(10) The statute requires that all federal agencies with R&D budgets exceeding \$100 million must not only participate in, but also allocate at least 3.2% of their R&D budgets to the program.(11) The DoD, which receives substantial R&D funding from Congress, is a major participant in the SBIR program.(12)

Congress' goals in establishing the program were grounded in the assumption that small businesses are the 'engine' for U.S. economic development, and that therefore nurturing technologies developed by small businesses is a sound national policy. The SBIR program is intended to increase small business participation in R&D, which traditionally was mostly in the hands of large institutions. Through the SBIR program – which is part of a broader framework of preferences and programs under the Small Business Act – Congress seeks to spur small businesses' development of new technologies, to encourage disadvantaged and minority-owned small businesses to participate, and to increase the number of government R&D projects that become commercially viable products.(13) To be successful in this program, small businesses generate innovative solutions to some of the government's biggest challenges. The ultimate goal of any SBIR initiative is commercialization, which is defined as “the process of developing products, processes, technologies, or services and the production and delivery (whether by the originating party or others) of the products, processes, technologies, or services for sale to or use by the Federal government or commercial markets”.(14) The 2014 SBIR/STTR Interagency

(10) For historical background on the Small Business Act, *see, e.g.*, M.V. KIDALOV, “Small Business Contracting in the United States and Europe: A Comparative Assessment”, 40 *Pub. Cont. L.J.*, 2011, pp. 443, 450; *see also*, C.W. WESSNER, (ed.), *An Assessment of the Small Business Innovation Research Program*, National Research Council, 2007, available at [www.ncbi.nlm.nih.gov/books/NBK9609/pdf/Bookshelf\\_NBK9609.pdf](http://www.ncbi.nlm.nih.gov/books/NBK9609/pdf/Bookshelf_NBK9609.pdf).

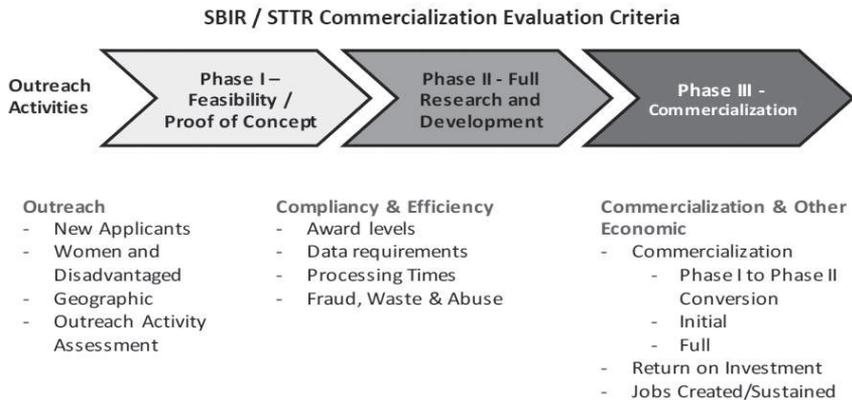
(11) 15 U.S.C. § 638; *see* Small Business Administration, “Small Business Innovation Research (SBIR) Program – Policy Directive”, 24 February 2014, p. 3, [www.sbir.gov/sites/default/files/sbir\\_pd\\_with\\_1-8-14\\_amendments\\_2-24-14.pdf](http://www.sbir.gov/sites/default/files/sbir_pd_with_1-8-14_amendments_2-24-14.pdf).

(12) SBIR/STTR, “Dashboard”, [www.sbir.gov/awards/annual-reports](http://www.sbir.gov/awards/annual-reports) (reports may be generated by agency).

(13) Small Business Innovation Development Act of 1982, Pub. L. No. 97-219, § 2, 1982.

(14) 15 U.S.C., § 638(e)(10); *see also* Program Interagency Policy Committee, *Report to Congress on Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR) Commercialization*, 15 September 2014, available at [www.sbir.gov/sites/default/files/2\\_commercialization-ipc\\_report\\_to\\_congress.pdf](http://www.sbir.gov/sites/default/files/2_commercialization-ipc_report_to_congress.pdf).

Policy Committee Report to Congress regarding commercialization outlined the following goals for successful SBIR commercialization, which confirmed that the program's goals reach well beyond merely developing innovative technology:(15)



*Figure 1. Best Practice Recommendations for SBIR Commercialization (16)*

In a market dominated by capital-heavy large businesses, it is clear that the SBIR program provides an important avenue for small businesses, including disadvantaged businesses, to participate in technology development and create high-tech jobs. Is establishing that avenue enough, though, to deem the SBIR program a success? Summarizing the defense acquisition marketplace, the Section 809 Panel emphasized the need for outcomes to ensure the nation's security: "To stay ahead in a dynamic, ever-changing environment, DoD needs a new approach to acquisition. Rather than focusing on price and process to measure success, DoD's acquisition system should focus on outcomes".(17) In keeping with this suggestion, the following section describes the SBIR program's structured process and suggests ways to analyze its success in providing innovative solutions to the Defense Department's needs.

(15) Program Interagency Policy Committee, *Report to Congress on Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR) Commercialization*, op. cit., 12, 4.

(16) *Ibid.*

(17) Section 809 Panel, *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations*, op. cit., pp. 4, 6.

## 2.2. Description of SBIR Phases I, II, and III

The SBIR program uses a uniform, three-phased process to foster technological advancements at various stages of development.(18) The [www.SBIR.gov](http://www.SBIR.gov) Web site summarizes the three phases.

Phase I. The objective of Phase I is to establish the technical merit, feasibility, and commercial potential of the proposed R/R&D (research/research and development) efforts and to determine the quality of performance of the small business awardee organization prior to providing further Federal support in Phase II. SBIR Phase I awards normally do not exceed \$150,000 total costs for six months.

Phase II. The objective of Phase II is to continue the R/R&D efforts initiated in Phase I. Funding is based on the results achieved in Phase I and the scientific and technical merit and commercial potential of the project proposed in Phase II. Only Phase I awardees are eligible for a Phase II award. SBIR Phase II awards normally do not exceed \$1,000,000 total costs for two years.

Phase III. The objective of Phase III, where appropriate, is for the small business to pursue commercialization objectives resulting from the Phase I/II R/R&D activities. The SBIR program does not fund this phase. Phase III may involve follow-on non-SBIR funded R&D or production contracts for products, processes or services intended for use by the U.S. Government.(19)

In addition to the anecdotal ‘Success Stories’ provided on the [sbir.gov](http://sbir.gov) website, the SBA has included a database of Phase I and Phase II SBIR awards dating back to 1983, which is presented as an Awards Dashboard.(20) Most recently in 2018, the database included records for 433 DoD SBIR awards, comprised of 252 Phase I and 181 Phase II awards.(21) This public database provides opportunities to conduct quantitative analyses of SBIR awards through the years. The following section will provide several measurements that assess the extent to which SBIR technologies have been successful in fostering innovation in DoD projects.

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(18) Small Business Administration, “Small Business Innovation Research (SBIR) Program – Policy Directive”, *op. cit.*, p. 9.

(19) About SBIR, Three-Phase Program, available at [www.sbir.gov/about/about-sbir](http://www.sbir.gov/about/about-sbir).

(20) SBIR/STTR, “Dashboard”, *op. cit.*, p. 10.

(21) *Ibid.*

### 3. Measuring SBIR Program Success

As a contracting vehicle, the SBIR program is successful at executing awards. Alongside its sister Small Business Technology Transfer (STTR) program, the SBIR program has made over 162,000 contract awards exceeding \$46 billion since 1982.<sup>(22)</sup> By these measures, it is clear that the program is supporting small businesses and fostering technological development. Nonetheless, the data in the sbir.gov Web site on the number of SBIR contract awards and funding shows a steadily downward trend beginning 2010.<sup>(23)</sup>

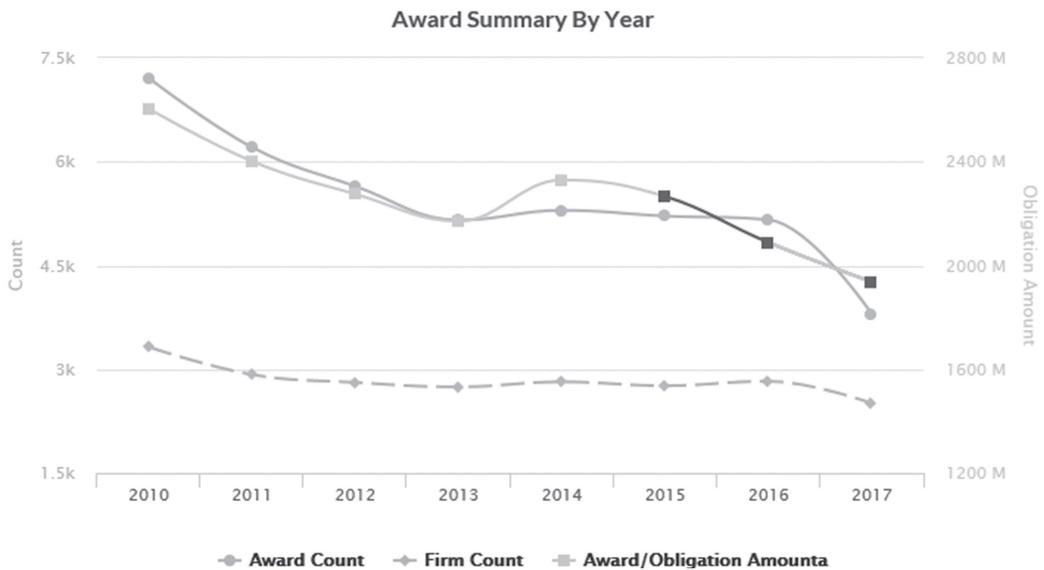


Figure 2. SBIR Award Trends 2010-2017<sup>(24)</sup>

Perhaps this trend reflects uncertainty that SBIR investments are producing meaningful, transition-ready innovations for DoD projects. Since the first statute launched the SBIR program, Congress has updated the law to require tracking, measuring, and reporting against benchmarks at each Phase. Effective with the 2011 reauthorization act, the SBIR programs must track and report on two benchmarks meant to increase the probability that development efforts will result in commercial-ready products. The first benchmark, Transition Rate Benchmark, requires that over the past five years (not including

<sup>(22)</sup> U.S. Government Accountability Office, “Small Business Research Programs: Agencies Need to Take Steps to Assess Progress Toward Commercializing Technologies”, *op. cit.*, p. 6.

<sup>(23)</sup> SBIR/STTR, “Dashboard”, *op. cit.*, p. 10.

<sup>(24)</sup> *Ibid.*

the last year), a company must transition one quarter of its Phase I efforts into Phase II. The second, Commercialization Benchmark, requires that over the past ten years (not including the last two years), companies with over 15 Phase II awards must receive at least an average of \$100,000 in sales/investments per Phase II award. Companies that do not meet these benchmarks are ineligible for future SBIR awards.(25)

Due to the diverse and decentralized funding sources for Phase III, there is no consolidated data source listing Phase III SBIR awards. In response to this information gap and to foster improvements in Phase III transitions, the SBIR and STTR Reauthorization Act of 2012 established the Commercialization Readiness Program (CRP). This program requires U.S. defense and military organizations to identify SBIR projects “that have the potential for rapid transitioning to Phase III and into the acquisition process”.(26) In response, when the DoD released the FY14 Annual Report on CRP in November 2017, it summarized transition successes from the Air Force, Army, and Navy. Table 1 includes a summary of these successes.

*Table 1. FY14 CRP Transition Success Summary(27)*

Service	FY14 SBIR CRP Projects	Total Projects since CRP Inception	Overall Benefit
Air Force	20	63	Each project meets the technology needs of at least one Air Force system with total cost savings estimated at over \$1 Billion
Army	30	101	While too early to provide specifics of success, Army SBIR expects at least a 5:1 return on investment (~\$250M) within the next five years.
Navy	29	273	Cumulatively, the DON has invested over \$504 million in SBIR funding to CRP projects, which includes funding for the acceleration of transition efforts.

According to this annual report, the Air Force’s anticipated cost savings from SBIR successes roughly exceeded all of the Defense Department’s SBIR

(25) Small Business Administration, “Small Business Innovation Research (SBIR) Program – Policy Directive”, *op. cit.*, p. 9.

(26) 15 U.S.C., § 638, Research and development.

(27) Department of Defense, *Fiscal Year 2014 Report Submission on Commercialization Readiness Program (CRP)*, March 2015, 5, pp. 23-26, available at [www.sbir.gov/sites/default/files/FY14%20CRP%20Report.pdf](http://www.sbir.gov/sites/default/files/FY14%20CRP%20Report.pdf).

costs for a year.(28) The Army was projecting significant returns from its investments, as well.(29) Finally, the Navy was leading the way in using the program to identify, develop and inject modern capabilities through the acquisition lifecycle.(30)

Combining this commercialization data with the Defense Department's SBIR award data available in the online sbir.gov award dashboard, in Table 2 we can draw some meaningful insights regarding 'transition successes' in the program.

Table 2. SBIR Awards(31) and CRP Projects(32)

Year	Total DoD SBIR Phase I and II Awards	DoD Phase I Awards	DoD Phase II Awards	DoD Commercialization Projects (from FY14 report)
FY13	2,157	1318 (61%)	838 (39%)	
FY14	2,014	1299 (65%)	715 (35%)	79
FY15	1,996	1262 (63%)	734 (37%)	

Based upon this table, the trend shows that a little more than a third of DoD SBIR performers successfully transition to Phase II R&D contracts. However, the evidence also shows that Phase II awardees reach a steep cliff at the end of their SBIR-funded contracts. If we assume that the 79 reported FY14 commercialization transitions were FY13 Phase II projects, it would seem that over 90% had died in the 'Valley of Death' – the chasm between development and commercialization – over that year. Even compared to the commercial industry high-technology space, these DoD transition statistics are low.

In response to lackluster Phase III successes, the 2014 SBIR/STTR Inter-agency Policy Committee Report to Congress offered some best practices related to commercialization success – though those suggested best practices are only partially actionable. The first best practice merely observed that depending on the market or sector, capabilities will mature on different timelines, impacted by 'financially intensive readiness' and other technology factors. The second best practice recommended Commercial Assistance Programs (CAPs), which provide mentoring and training opportunities to small businesses specifically

(28) *Ibid.*, p. 23.

(29) *Ibid.*, p. 26.

(30) *Ibid.*, pp. 23, 17.

(31) SBIR/STTR, "Dashboard", *op. cit.*, p. 10.

(32) Department of Defense, *Fiscal Year 2014 Report Submission on Commercialization Readiness Program (CRP)*, *op. cit.*, p. 23.

for navigating the SBIR phased process. The final recommendation for commercialization suggested using “Post Phase II Bridge funding (e.g. Phase II-B/II-E/II-X)” to secure funding and avoid the ‘Valley of Death’ capital drought at any phase.(33)

Policy makers in the U.S. government hope that benchmarks and commercialization support initiatives will prevent chronically ineffective technology developers from continuing to receive SBIR funding. More reliable award data would shed light on the small business performers’ health and effectiveness. Meeting Congress’ required benchmarks will not guarantee an improvement in transition success statistics. Still, without the benchmark data, after spending \$1 billion per year, it is impossible to quantify whether the SBIR program is indeed successful deploying innovative technologies to DoD projects, or merely successfully at using defense funding to bolster small businesses economically. And yet even with this significant metric for success still an open question – with relative success in bringing SBIR projects to the commercial marketplace still not definitively proven – procurement systems worldwide, such as the European initiative discussed in the following section, have begun to mimic the SBIR program.

#### ***4. European Union (EU) Innovation Program***

As in the United States, European economies depend upon continuous technology sector growth. In response, the EU has crafted an overarching ‘Single Market’ strategy that focuses on identifying the breadth of societal needs, creating policies and standards that enhance collaboration and inclusiveness, expanding fair competition throughout the EU procurement system, and recognizing the importance of Small and Medium-sized Enterprises (SMEs).(34) This holistic approach focuses on the problem first, and then ensures the right tools are applied to solve it. Through the Innovation Union, the EU focuses on becoming a ‘world class science performer’, preventing market obstacles to delivering ideas quickly, and fostering partnerships between EU government organizations and businesses.(35)

To achieve these innovative ends, the EU established a seven-year, €75 billion program called Horizon 2020 in 2014. It focuses on areas to enhance EU innovation, with a special focus on addressing societal issues. This program is not exclusive to small- and medium-sized enterprises

(33) Program Interagency Policy Committee, *Report to Congress on Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR) Commercialization*, op. cit., 12, 10.

(34) EU, *State of the Innovation Union: Taking Stock 2010-2014*, Luxembourg, POEU, 2014.

(35) EU, *Innovation Union, A Pocket Guide on a Europe 2020 Initiative*, Luxembourg, POEU, 2013.

(SME's). To support innovation by SME's, however, the EU established a concept called the SME Instrument to foster participation by these small- and medium-sized companies.<sup>(36)</sup> According to the Horizon 2020 Information Guide published in 2014, the SME Instrument was 'inspired' by the U.S. SBIR program.<sup>(37)</sup> The SME Instrument is a competitively awarded program which includes three phases, similar to the U.S. SBIR program. Phase 1 contracts support 'Concept & Feasibility Assessment', span fewer than six months, and are awarded on the basis of a brief business plan conveying the small business' business concept. Phase 2 contracts support Research and Development (R&D) Innovation, which takes place over 12-24 months, and is awarded on the basis of a more mature, detailed business plan describing the innovation. Finally, Phase 3 promotes 'Commercialisation' through training, networking, and facilitating the small business' access to private financing. The EU does not fund Phase 3 activities. Unlike the U.S. SBIR program, SME's may participate in only one project (in Phase 1 or 2) per year.<sup>(38)</sup>

While very similar in structure to the U.S. SBIR program, the Horizon 2020 SME Instrument seems to take less responsibility for the sponsoring government's use of the innovations in the program, and instead focuses on fostering small business' commercial success after the program. The Horizon 2020 Information Guide includes the following graphic, which draws on the SBIR program to depict the funding evolution for ideas in the innovation cycle, from public to private, as they mature through the R&D process and eventually enter the commercial market. The 'V' shape demonstrates the funding 'Valley of Death' commonly experienced by technology companies, but also reiterates that the SBIR funding is meant only to sustain a company during development, and that funding is to be surpassed by private investments in the future.

(36) European Commission, "What is Horizon 2020? Horizon 2020 – Work Programme 2018-2020 General Introduction", 27 October 2017, available at [ec.europa.eu/research/participants/data/ref/h2020/wp/2018-2020/main/h2020-wp1820-intro\\_en.pdf](http://ec.europa.eu/research/participants/data/ref/h2020/wp/2018-2020/main/h2020-wp1820-intro_en.pdf).

(37) Art. 31 of the EU's primary public procurement Dir., 2014/24/EU, permits a uniquely flexible and phased procurement process for 'innovation partnerships'. For a discussion of how Art. 31 and innovative partnerships had been transposed into the United Kingdom's procurement law, see J. BENNETT, "Innovation partnership – does it offer a genuine breakthrough?", 22 April 2015, available at [publicsectorblog.practicallaw.com/innovation-partnership-does-it-offer-a-genuine-breakthrough/](http://publicsectorblog.practicallaw.com/innovation-partnership-does-it-offer-a-genuine-breakthrough/). Other European initiatives which reflect strong parallels with the U.S. SBIR program are the United Kingdom's Small Business Research Initiative (SBRI) initiative, see <https://sbri.innovateuk.org/>, and the European Defense Fund, which would fund European research and development in defense materiel, to support long-term production in the European defense industry, see, e.g., C.R. YUKINS, "European Commission Proposes Expanding the European Defence Fund – A Major Potential Barrier to Transatlantic Defense Procurement", 60 *Government Contractor*, 27 June 2018, par. 196, available at [ssrn.com/abstract=3204844](http://ssrn.com/abstract=3204844).

(38) EU, *State of the Innovation Union: Taking Stock 2010-2014*, op. cit., p. 38.

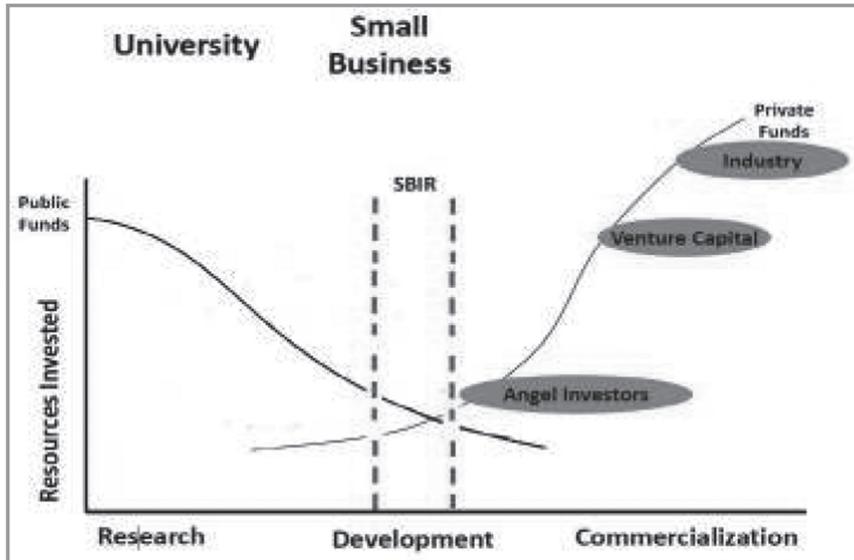


Figure 3. EU Horizon 2020 SME Instrument (39)

Having borrowed the three-phased U.S. SBIR structure, but adapted to reflect EU societal priorities, the Horizon 2020 program is reportedly meeting its goals, with a few exceptions. In its 2014-2016 Horizon 2020 results brochure, the European Commission noted that the SME Instrument funded 2,319 grants, 78% for Phase 1 and 22% for Phase 2 activities. The Commission provided statistical results which spanned all of the Horizon 2020 initiatives and reflected proposal success metrics, country participation, and societal impact areas. The Commission did not, however, provide any data regarding the SME Instrument's Phase 3 commercialization.<sup>(40)</sup> It appears, therefore, that the U.S. SBIR program may not be alone in having difficulty measuring success in this final stage.

As the foregoing discussion showed, governments have had uneven success in nurturing emerging technologies into the commercial marketplace. The following section describes several of the U.S. SBIR program's unique features which contribute to both its successes and its challenges.

(39) European Commission, *Horizon 2020 Information guide: SME opportunities for EU-US collaboration in Horizon 2020*, Luxembourg, POEU, February 2014, available at [ec.europa.eu/research/isep/pdf/policy/sme\\_opportunities\\_h2020\\_feb2014.pdf](http://ec.europa.eu/research/isep/pdf/policy/sme_opportunities_h2020_feb2014.pdf).

(40) European Commission, *Horizon 2020 in Full Swing – Three Years On – Key facts and figures 2014-2016*, Luxembourg, POEU, 2018, available at [ec.europa.eu/programmes/horizon2020/sites/horizon2020/files/h2020\\_threeyearson\\_a4\\_horizontal\\_2018\\_web.pdf](http://ec.europa.eu/programmes/horizon2020/sites/horizon2020/files/h2020_threeyearson_a4_horizontal_2018_web.pdf).

## 5. Defining Features of SBIR Contracts

### 5.1. Award Preferences

To be eligible for an SBIR Phase I or II contract award, a business must be for-profit, geographically located in the United States, legally organized, more than 50% owned by individuals or small businesses that are U.S. citizens/permanent resident aliens, and employ fewer than 500 persons.(41) While it is tempting to rely on Congress' assertion that small businesses are better at innovating than large businesses, all companies' innovations depend upon their incentives to pursue them. Incentivizing small business as a means to distribute wealth, Congress established the SBIR program in 1982 specifically to support these enterprises, and to "foster and encourage participation by minority and disadvantaged persons" in the technology development process.(42) For DoD SBIR Phase I and II awards, this program serves as a \$1 billion opportunity for small businesses in the United States. However, the SBIR program is struggling to achieve some of its major objectives related to preferences.

While the program overall is successful in funding small businesses, it is lagging in its support for minority-owned and disadvantaged companies. The 2014 report to Congress found that despite industry outreach efforts, during 2013 minority-owned companies had earned only 4.57% of the SBIR awards and women-owned companies had earned only 9.22%.(43) One factor that could explain this shortfall is that the program strongly favors more established companies with diverse and consistent revenue streams. Phase II awards may lag months or years behind Phase I awards, and similarly Phase III awards may come only after a significant delay. Retaining a workforce ready to execute highly technical, innovative SBIR projects during these funding gaps is nearly impossible for most small business owners. Across the Defense Department, George Washington University doctoral candidate Ronnie Schilling noted, small businesses are not consistently staying in the DoD marketplace. His research spanned 11 years, 1997-2008, and demonstrated that by the end of

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(41) Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR), "U.S. Department of Defense SBIR STTR: Getting Started", 31 March 2018, available at [www.acq.osd.mil/osbp/sbir/sb/getting-started-phase-1.shtml](http://www.acq.osd.mil/osbp/sbir/sb/getting-started-phase-1.shtml).

(42) United States Congress, Pub. L. 97-219, *Small Business Innovation Development Act of 1982*, United States Code, U.S. Government Publishing Office, 22 July 1982. There has been criticism, though, from the Section 809 Panel, *see supra*, notes 5-6 and accompanying text, that the "Small Business Act, as it stands today, does not state a goal for government agencies to leverage small businesses as a means to enhance or support mission execution. The statute includes a reference that the American economic system of private enterprise and competition is essential to the 'security of this Nation,' but contains no direct references to agency missions or national defense".

(43) Program Interagency Policy Committee, *Report to Congress on Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR) Outreach*, 15 September 2014, p. 7.

the study period fully 44% of the small companies were no longer conducting DoD business at all, and only 1.9% of all the companies had worked consistently with the DoD throughout the period.<sup>(44)</sup> These statistics suggest that small business' incentives to use the SBIR program are more often focused on near-term, rather than long-term, goals. Nevertheless, since the 1980's many entrepreneurs have used Phase I and II SBIR awards as a foundation to build successful technology companies, demonstrating that the preference incentive may be worthwhile.

In contrast, Phase III awards are not limited to small businesses. As the SBIR guidance published by the U.S. SBA explains, former SBIR Phase I and II awardees that have graduated from the small business size standard are eligible to receive Phase III funding. Further, as is discussed below, the policy authorizes *sole source* Phase III contract awards to those that have won prior Phase I and II awards.<sup>(45)</sup> This policy can tie government purchasers to Phase III technology that was developed years earlier, when the likely future trajectory of the technology was only hazily understood by the officials approving Phase I and Phase II awards. In practice, Phase III awards may be made to small or large businesses via subcontracts, which make them all the more difficult to track or measure. Altogether, these competition policies provide support to small businesses primarily during Phases I and II, though the more enabling incentives in Phase III (discussed below) may be a driving force for transitioning mature technologies to government and commercial uses. But without additional quantifiable data to assess these transitions, measuring success is elusive.

## 5.2. Data Rights

Another defining feature of SBIR contracts is that although the government pays for technology development in all phases, the government does not acquire unlimited rights (normally the rights the government demands for work it funds) in the SBIR work product, whether technical data or computer software.<sup>(46)</sup>

The U.S. SBA defines SBIR Technical Data Rights as “the rights an SBIR awardee obtains in data generated during the performance of any SBIR Phase I, Phase II, or Phase III award that an awardee delivers to the Government during or upon completion of a Federally-funded project, and to which

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(44) R. SCHILLING, “Survey of Small Business Barriers to Department of Defense Contracts”, *Defense ARJ*, Vol. 24, No. 1, 2017, pp. 2-29.

(45) Small Business Administration, “Small Business Innovation Research (SBIR) Program – Policy Directive”, *op. cit.*, pp. 9, 13.

(46) See Defense Federal Acquisition Regulation Supplement (DFARS) Subparts 227.71 - 227.72, 48 Code of Federal Regulations Subparts 227.71 - 227.72.

the Government receives a [royalty-free] license”.(47) Under the terms of the SBA’s SBIR guidance, the government must protect the small business’ data from non-government entities, including competitors; must continue to protect the data for at least four years after receipt of the final product; must provide these protections through all three Phases, unless the business agrees to other terms; and, must not coerce the business into releasing data rights for SBIR products. The SBA directive also warns that “SBA will report to the Congress any attempt or action by an agency to condition an SBIR award on data rights, to exclude the appropriate data rights clause from the award, or to diminish such rights”. Small businesses are incentivized to participate in the SBIR program because the federal government carries the cost burden and risk during technology development, while the business also establishes potential long-term opportunities to sell the product in the commercial marketplace. Theoretically, as a result of this incentive, the government has greater access to more innovative products from the small business industry base. In practice, the DoD has difficulty realizing this benefit.

The realization challenge arises in part because DoD agencies must follow acquisition guidance, *DoD Instruction (DODI) 5000.02, Operation of the Defense Acquisition System*, which prescribes a process to design, develop, field, and maintain systems and subsystems for military use.(48) Successful implementation of this process depends upon defense managers’ long-term acquisition strategies, and upon the system architecture being sequenced efficiently. For a non-commercial product developed exclusively with government funds, the DoD generally expects to retain rights to use and modify the product in perpetuity. When a product is developed using mixed funding, the Defense Department normally gains rights to use the technology for government purposes.(49) Specifically, the Defense Federal Acquisition Regulation Supplement states: “[Contractors] may not restrict the Government’s rights in items, components, or processes developed exclusively at Government expense (unlimited rights) without the Government’s approval. When an item, component, or process is developed with mixed funding, the Government may use, modify, release, reproduce, perform, display or disclose the data pertaining to such items, components”.(50) The SBIR program stands as a major exception

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(47) Small Business Administration, “Small Business Innovation Research (SBIR) Program – Policy Directive”, *op. cit.*, pp. 9, 7.

(48) Office of the Undersecretary of Defense for Acquisition, Technology, and Logistics, “Operation of the Defense Acquisition System”, DoD Instruction 5000.02, Washington, DC: USD(AT&L), January 2015.

(49) See, e.g., Defense Information Systems Agency (DISA), “Data Rights”, [disa.mil/about/legal-and-regulatory/datarights-ip/datarights](http://disa.mil/about/legal-and-regulatory/datarights-ip/datarights).

(50) Defense Federal Acquisition Regulation Supplement (DFARS), 48 C.F.R. ch 227.713-4 License Rights, 2012.

to these policies, and runs contrary to most defense managers' training and assumptions about data rights.

To support continued maintenance of any system, subsystem, or component, a defense manager is interested not only in the specific hardware items or software executables, but also in the tangential know-how and documentation. As the systems age, they require updates. As a cost control measure, defense managers often plan and execute competitive contracts for these updates, which becomes difficult when the government holds a license to use, but no data rights to modify or share, a product. DoD Instruction 5000.02 provides specific guidance for what are known as 'IP Strategies', which are a statutory requirement for defense managers in planning and executing major weapons systems development. DoD Instruction 5000.2 notes that Intellectual Property Strategies must describe "how program management will [...] acquire competitively whenever possible, the intellectual property deliverables and associated license rights necessary for competitive and affordable acquisition and sustainment over the entire product life cycle".<sup>(51)</sup> SBIR data rights protections, which heavily favor the private developers, may disrupt the government's rights during defense systems' maintenance and update phases if a defense manager has not adequately accommodated the SBIR limitations in the project's intellectual property strategy.

Recognizing the challenge of integrating intellectual property that bears distinct private rights (such as SBIR data rights) into major acquisition programs, DoD published guidance in 2014 to facilitate intellectual property strategies. The DoD guidance noted that proprietary technology may impact a defense manager's ability to conduct full and open competition, but suggests two significant factors for a successful integration of technical components without full data rights. The first factor is time. The guidance suggests that the sooner a manager identifies and documents a system, subsystem, or component to which the government has limited data rights, the better the manager can plan for competition issues. The second factor is related to system design. The guidance suggests the use of an 'Open Architecture' with a highly segregated components structure, so that limited data rights for one portion of the system do not hamper competition for development or maintenance of the entire system.<sup>(52)</sup> To use restricted data in a DoD system successfully while using best-practice competition for procurements, a defense manager must assimilate these limitations into both the project's acquisition plans and the system design itself.

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(51) Office of the Undersecretary of Defense for Acquisition, Technology, and Logistics, "Operation of the Defense Acquisition System", *op. cit.*, p. 49.

(52) Department of Defense Open Systems Architecture Data Rights Team, "Intellectual Property Strategy Brochure", Defense Acquisition University (DAU), August 2014.

A final data rights challenge exists with regards to Phase III awards made to large prime contractors performing on behalf of the DoD, for example Lead Systems Integrators (LSI). Under the Small Business Administration's guidance for the SBIR program, subcontracts awarded under these large prime contracts are to be treated as Phase III awards, and thus afford the private parties greater data rights than normal subcontracts. The prime contractors incorporating these technologies have, however, a strong incentive to integrate the SBIR technology into their own base of technical know-how, which may have the effect of increased use of the emerging technology on the government's behalf. On the other hand, incorporating this SBIR-funded intellectual property into projects run by large prime contractors may dilute the salutary effect that the SBIR program normally has in nurturing the small business industrial base. These are further examples of how the SBIR initiative in practice may pose a challenge to Defense Department acquisition programs – and to its own goals – because of the conflicting incentives and guidance related to intellectual property and data rights.

### 5.3 Competition

One of the most prominent values held by the U.S. procurement community is its faith in competition. When he offered the U.S. acquisition workforce common-sense approaches to procurement policy, Mr. Frank Kendall, then the Under Secretary of Defense for Acquisition, Technology and Logistics (AT&L), noted: “Competition and the threat of competition provide the most effective incentive”.<sup>(53)</sup>

On its face, the SBIR program seems to embrace competition. Phase I and II performers must demonstrate the merits of their solutions before moving forward in the SBIR process, and many fail. On the assumption that these two initial, competitive phases are sufficient, the SBA's policy supports sole-source awards to Phase III performers. It states: “The competition for SBIR Phase I and Phase II awards satisfies any competition requirement of the Armed Services Procurement Act, the Federal Property and Administrative Services Act, and the Competition in Contracting Act”. Further, the SBA policy states that an SBIR Phase III project may be cited in a Justification and Approval (J&A)<sup>(54)</sup> for a sole-source (technically, an other than full-and-open competition) award under Federal Acquisition Regulation (FAR) 6.302-5, so long as the project “is derived from, extends, or completes efforts made under prior SBIR funding agreements and is authorized under 10 U.S.C. 2304(b)(2) or 41

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(53) F. KENDALL, “Better Buying Power Principles: What Are They?”, *Defense Acquisition, Technology, and Logistics (AT&L) J.*, January 2016, pp. 2-4.

(54) 48 Code of Federal Regulations 6.302-5.

U.S.C. 3303(b)".(55) Under the policy, this sole-source option is available years into the future, which in practice can create a long-term sheltered marketplace for SBIR-funded research and development.

It is not clear that the limited competition imposed by the SBIR program leads to optimal results. While the SBIR program uses competition, there is evidence that its methods do not necessarily identify the best innovations in the marketplace to support the DoD mission.

A first weakness related to the competition policy is that small businesses must have a strong understanding of the DoD marketplace and specific customer needs to win SBIR work. In his survey of small businesses seeking DoD contracts, Ronnie Schilling noted: "We did find statistical evidence to support the idea that businesses with less defense business experience perceive defense business to be more challenging than those with extensive defense experience. We also found support for smaller small businesses perceiving defense business to be more challenging than those larger businesses that still qualify for small business contracts". Breaking into the DoD market is very difficult. Schilling noted that though this perceived experience/knowledge gap was not the most significant barrier, it was among the reasons that small businesses avoid pursuing DoD business, which strongly influences the competitive environment in favor of the most experienced, mature small businesses.(56)

To facilitate their entry into the government market, the SBIR Web site provides guidance to small businesses pursuing SBIR opportunities, which includes step-by-step instructions and training materials related to the application process.(57) However, these instructions do not provide information to assist these innovators in understanding specialized military operations and functionality gaps, let alone the acronym-heavy technical language used to describe them.

Unless they hire consultants, small businesses in the high-tech, commercial market may not have insight into the DoD's current goals, and so may struggle to identify relevant innovations. Apparently this problem has disproportionately impacted socio-economically disadvantaged businesses, as well as those companies geographically distant from DoD acquisition commands. The 2011 SBIR/STTR Reauthorization Act called for a focus on industry outreach to address this issue, but as recently as 2014, the Policy Committee report demonstrated that women-owned and disadvantaged companies were

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(55) Small Business Administration, "Small Business Innovation Research (SBIR) Program – Policy Directive", *op. cit.*, pp. 9, 13.

(56) R. SCHILLING, "Survey of Small Business Barriers to Department of Defense Contracts", *op. cit.*, p. 46.

(57) Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR), "U.S. Department of Defense SBIR STTR: Getting Started", *op. cit.*, p. 43.

still lagging in awards. Additionally, during the period 2010-2013, companies located in Virginia, Maryland, the District of Columbia, California, New York, and Massachusetts – geographic centers of the Defense Department’s work in research and development – had won over 50% of the SBIR awards.(58) The evidence suggests that the competitive pool favors businesses with existing experience and proximity to DoD projects, which may leave out important innovators in the commercial small business marketplace.

A second weakness in the SBIR competitive process is momentum. Award data in the online sbir.gov dashboard shows that winning companies statistically continue winning, buoyed by the new benchmarks, while those less successful at technology transitions are trimmed from the competitive pool. In 2017, among the total 614 Phase I and II DoD SBIR awards, 86 companies (20%) won two or more awards, while 326 companies (80%) won only one award. That metric does not appear problematic, until one observes the proportion of contracts that these repeat awardees are winning. In this regard, the dashboard shows that repeat awardees received a total of 288 (47%) awards that year, demonstrating that although they comprise only a fifth of the provider group, these companies are winning nearly half of the work.(59) In the online dashboard’s 2017 awards list, two firms stood out as the most successful. Physical Optics Corporation (POC) received 17 SBIR awards totaling \$7.9 million, and Charles River Analytics received 11 SBIR awards totaling \$6.8 million.(60)

Small businesses employ numerous tactics to remain competitive in the SBIR program. Spinning off companies is a common practice in federal contracting which allows small, successful portions of businesses to continue pursuing opportunities in the small business market rather than growing as a cohesive large business. Physical Optics Corporation’s website noted that over the prior decade the firm had “created six spinoff companies and ha[d] provided a technology base for two additional joint venture companies. These companies were all based on POC technology, and were once divisions within POC”.(61) One of those spin-offs won a small Phase I award in 2017. Between the benchmarks and disproportionately strong companies in the program,

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(58) Program Interagency Policy Committee, *Report to Congress on Small Business Innovation Research (SBIR) Small Business Technology Transfer (STTR) Outreach*, *op. cit.*, p. 44. The Section 809 Panel, *see supra*, note 5, observed in its January 2018 report that many “companies that are not small, but far from large, struggle to compete for government contracts against large, well-established companies without set-aside programs and other support... This structure incentivizes small companies to adopt strategies that may be inconsistent with DoD’s interests and small business programs’ goals”.

(59) SBIR/STTR, “Dashboard”, *op. cit.*, p. 10.

(60) *Ibid.*

(61) Physical Optics Corporation, “POC Corporate Overview: Spinoffs”, 31 March 2018, available at [www.poc.com/corporate-overview/spinoffs/](http://www.poc.com/corporate-overview/spinoffs/).

these practices effectively skew competition in favor of those companies that can best respond to the SBIR program's unique regulatory requirements.

The third weakness in the SBIR program's claim that it enhances competition relates to the assumption that the SBIR process nurtures the most capable innovative solutions on the market, over the many years from a Phase I award to a Phase III contract. Well-known theories in high technology, such as Moore's Law, posit that technology advances exponentially fast, perhaps doubling every two years.<sup>(62)</sup> Even without significant funding gaps, due to the proposal, contracting, and execution periods associated with Phases I and II in the SBIR program, a small business may not be ready to launch into Phase III until more than three years after writing the initial proposal. Comparing the SBIR timeline with the much sharper upward trajectory of normal technological progress, it is entirely conceivable that over these three years companies outside the SBIR program may have developed innovative solutions that far surpass the original concept funded in SBIR Phase I. For this reason, tying government customer agencies to sole-source Phase III awards may be a dangerous presumption, in effect limiting DoD's access to emerging technologies. And worse, without a way to collect and measure the Defense Department's use of technology which has advanced to Phase III, policy makers will lack the data necessary to assess this issue.

## ***6. Conclusion and Recommendations***

By all accounts, the Department of Defense's SBIR program is noble in its aim to support small businesses and to encourage innovation in the DoD marketplace. Anecdotal evidence suggests that the program has been successful in several ways, including the following:

- Providing funding to small businesses to conduct innovative Phase I and II research, which affords vital investment to sustain otherwise risky R&D projects.
- Producing transition-ready hardware and software to support emerging DoD acquisition needs.

On the other hand, the data also indicates that the DoD's use of the SBIR program has become less effective over the last decade. Reduced participation in Phase I and II initiatives suggests that new performance benchmarks, lackluster outreach campaigns, and tepid Phase III technology transitions have eroded DoD managers' confidence in the program.

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(62) Intel, "Moore's Law and Intel Innovation", 1 May 2018, available at [www.intel.com/content/www/us/en/history/museum-gordon-moore-law.html](http://www.intel.com/content/www/us/en/history/museum-gordon-moore-law.html).

This paper posits that the program's unique features, including the following, may explain the SBIR program's limitations in fostering innovation in Defense Department procurement:

- Small businesses face barriers to entry and challenges sustaining DoD business, which hamper the SBIR program's ability to meet rapidly evolving defense requirements.
- Small businesses that do remain in the DoD R&D market can skew the competitive field by becoming highly proficient at leveraging the SBIR process.
- Although the SBIR program is at its heart a small business preference, SBIR Phase III contracts may be awarded to large businesses.
- The SBIR data rights policy is out of synch with DoD acquisition guidance, which introduces design constraints, forces additional planning in maintenance and operations, and requires additional training for defense acquisition managers.
- The SBIR program's three-phased process can be so lengthy that innovations occurring outside the SBIR program may provide more timely and more advanced solutions to DoD requirements.

SBIR program officials and proponents offer vivid success stories as evidence of the program's soundness, but those stories are often dispersed across the initiative, are mostly anecdotal, and can be difficult to quantify in light of the DoD's annual \$1 billion SBIR investment. As a whole, the DoD is unable to track its progress transitioning innovations born from the SBIR program. Without these metrics, the program is vulnerable to criticism that it is largely a 'tax' to DoD projects to fund small businesses.

There remains a serious and unresolved risk that the SBIR program's first focus on a small business preference does too little to incentivize transition-ready technology development. To address these issues, the DoD may benefit from a more holistic model that includes a culture of innovation based upon updated acquisition guidance; draws on input from innovators across the agencies, laboratories, and industry; and establishes an enterprise-level process to identify the best strategies to pursue innovation. As part of this process of holistic reform, capturing quantitative data for DoD Phase III projects will allow the Defense Department to assess the program's impact as an innovation tool. When the DoD prioritizes Phase III transition success as highly as meeting small business goals, it will be better able to capture the full value of innovation in the SBIR program.

**CHAPTER 12**  
**Innovation Partnerships: Purpose, Scope**  
**of Application and Key Elements**  
**of a New Instrument of Strategic Procurement**

BY

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***1. Innovation Partnership as a Specific  
Instrument of Strategic Procurement***

The European legislators consider innovation partnership as an instrument of strategic procurement. In recital 47 of the Public Procurement Directive (PPD), they describe “research and innovation, including eco-innovation and social innovation” as the ‘main drivers’ for future growth, (*i.e.* sustainable (ecological) and inclusive (social) growth).<sup>(1)</sup> The PPD aims at encouraging contracting authorities to procure innovative products (*i.e.* products that are guaranteed with high quality and efficiency for the fulfilment of public service tasks combined with major macroeconomic, ecological and social benefits). Against this background and as a reaction to the global financial crisis, the innovation partnership has formed part of the strategy ‘Europe 2020’ for smart, sustainable and inclusive growth by the European Commission.<sup>(2)</sup>

As an instrument of strategic ‘innovation procurement’, the innovation partnership complements a range of existing instruments for the procurement of innovative products. As paragraph 97(3) of the German Act against Restraints of Competition (“*Gesetz gegen Wettbewerbsbeschränkungen*” – GWB) clarifies, aspects of innovation can be considered at all stages of the award procedure<sup>(3)</sup> – (*i.e.* by

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(1) Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC (referred to as ‘PPD’), 72. Art. 26-31 of the Directive describe the procurement methods under EU law; a prior version of this piece was published through the Ius Publicum Network Review ([www.ius-publicum.com](http://www.ius-publicum.com)), issue 2, 2018.

(2) EC Com., “Europe 2020. A strategy for smart, sustainable and inclusive growth”, COM (2010) 2020 final.

(3) Cf. C. KRÖNKE, “Das neue Vergaberecht aus verwaltungsrechtlicher Perspektive”, in *NVwZ* 2016, 568 - 573.

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using functional requirements in the technical specifications [Art. 42(3)(a) PPD], by authorizing tenderers to submit variants [Art. 45 PPD] or by implementing innovative characteristics in the award criteria [Art. 67(2)(a) PPD]). Furthermore, Art. 26(4)(a)(ii) of the PPD shows that innovation partnership is not the only procedural instrument that can be used in order to purchase ‘innovative solutions’. The competitive dialogue procedure, a procedure specifically for carrying out exceptionally complex procurements,<sup>(4)</sup> and the competitive procedure with negotiation are also instruments of innovation procurement.<sup>(5)</sup> In addition, the Commission has laid out several models of ‘pre-commercial procurement’ as drivers of innovation – even though these models are not (necessarily) covered by the PPD and the GWB (*see* Art. 14[2] PPD and § 116[1][2] GWB).<sup>(6)</sup>

So why introduce another instrument for procuring innovation? A closer look at the scope of application and the key elements of the rules on innovation partnership reveals that such instrument is intended to provide the contracting authorities with an additional, *specific* procurement procedure for innovative products which addresses a different situation and a different subject-matter – ones not covered by the other instruments. The rules on innovation partnership state that the method is to be used only when solutions that are already available on the market cannot meet the needs of the contracting authority,<sup>(7)</sup> which means that the method should be used only when there is a considerable need for innovation under the given circumstances. European legislators’ goal in creating the innovation partnership procedure was to make it possible (or at least easier) for contracting authorities to acquire the ‘innovative result’ of a development process from an innovator, without a need for a separate procurement procedure. The procedure thus<sup>(8)</sup> provides incentives for market participants to invest in the necessary – but possibly expensive – development of innovation. The subject-matter of the innovation partnership agreement, the term of which is usually fixed for a relatively long period, includes the development as well as the subsequent purchase of the innovative product (‘development-plus-purchase’).<sup>(9)</sup>

(4) Dir. 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts (referred to as ‘CPD’), recital 31, 118; even more clearly in recital 42 of the PPD (“with innovative projects”), *op. cit.*, pp. 71-72.

(5) Please refer to part B. III of this paper for the distinction between these procedural instruments of innovation procurement.

(6) EU Comm., “Pre-commercial Procurement: Driving innovation to ensure sustainable high quality public services in Europe”, COM(2007) 799 final; as well as recital 47 of the PPD, *op. cit.*, p. 4.

(7) Please refer to part B. I and II of this paper for a detailed analysis of the scope of application of the rules on innovation partnerships.

(8) Recital 49 of the PPD, *op. cit.*, p. 73; *see also* S. ARROWSMITH, *The Law of Public and Utilities Procurement*, 3<sup>rd</sup> ed., 2014, par. 9-126.

(9) S. ARROWSMITH, *The Law of Public and Utilities Procurement*, *op. cit.*, p. 8, paras. 9-128-9-129.

## 1.1. Scope of application

The GWB provides two requirements for the application of the rules on innovation partnership (§ 119[2][2] of GWB), to wit: (1) The contracting authority must specify the need for an innovative product that “cannot be met by purchasing products, services or works already available on the market” (*see* Section I, below), and (2) the innovation partnership needs to aim at (both) the development of an innovative product and the subsequent purchase of its result (*see* Section II, below). These two requirements are also set in Article 31 (1). The innovation partnership differs from the other procedures that also promote innovation because it can be used by a contracting authority only after complying with the requirements described above (*see* Section III, below).

### 1.1.1. Solutions available on the market do not meet the procurement need

The first requirement under Article 31(1)(2) of PPD is that products available on the market cannot meet the contracting authority’s need for an innovative product. This requirement should be interpreted in conjunction with the definition of the term ‘innovation’ in Article 2(2) No. 22, PPD (which has not been transposed into German law). Accordingly, innovation means the “implementation of a new or significantly improved product, service or process, including but not limited to production, building or construction processes, a new marketing method, or a new organizational method in business practices, workplace organization or external relations *inter alia* with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth”. An innovative product, therefore, requires (1) an indication of the “innovative” nature of the product, and (2) a degree of innovation from the existing solutions.

### 1.1.2. Connection of the innovation to the subject-matter of the contract

The innovative aspect, which makes the requested solution stand out from the solutions that are already available in the market, can be related either directly to the subject-matter of the contract (e.g. asking for a building concept with a demand for energy reduction at a certain minimum) or to the procurement process in a wider sense (e.g. using building materials and energy from ecologically sustainable and socially inclusive sources for the construction of a building).

The innovations that are directly connected to the subject-matter of the contract do not raise any specific legal questions. They are called ‘product

innovations’, and may be included as part of the functional requirements in the technical specifications.(10)

The scope of innovations related to the procurement process in a wider sense, however, requires an accurate definition. Certainly, Article 22(1), No. 22, of PPD lays down the several types of ‘process innovations’ (*i.e.* innovations that are related to the “production, building or construction processes, a new marketing method, or a new organisational method in business practices, workplace organisation or external relations”). Despite this broad definition, process innovations still require a specific link between the innovation and the subject-matter of the contract; this makes the contracting authority responsible for implementing the innovative aspect of the procurement by way of (functional) technical specifications, award criteria or an additional contract performance conditions. Although the innovative elements need not form part of the ‘material substance’ of the subject-matter of the contract, it is still required that they be specifically “linked to the subject-matter of the contract” within the meaning of Article 42(1)(2), Article 67(3) and Article 70(1) of PPD.

## 1.2. Degree of Innovation

Article 2(1), No. 22, of PPD also provides the indicators for determining how much innovation (compared to already existing solutions) is required for the procurement of an innovative solution through an innovation partnership. According to the definition in Article 2(1), No. 22, of PPD, an innovation is not limited to entirely new products, services or processes, but it may also refer to any significant improvement in the existing products, services or processes.(11) The innovation partnership may therefore be considered by a contracting authority as an option in either of these two scenarios: (1) An eligible product is not available on the market at all (e.g., one-litre cars to be used as police cars).(12) (2) Although there is an appropriate product that is available on the market, either its quality is not satisfying (e.g., electronic cars are available but they lack a sufficient operating distance for use as police cars) or it is not available at a reasonable price (e.g., high performance electronic cars for use as police cars).(13)

(10) Cf. M. BURGL, “Die Förderung sozialer und technischer Innovationen durch das Vergaberecht”, in *NZBau* 2011, pp. 577, 580-581, on the significance of functional technical specifications for promoting innovation.

(11) Cf. E. BADENHAUSEN-FÄHNLE, “Die neue Vergabeart der Innovationspartnerschaft – Fünftes Rad am Wagen?” in *VergabeR* 2015, pp. 743, 746.

(12) See for this example also M. BURGL, “Die Förderung sozialer und technischer Innovationen durch das Vergaberecht”, *op. cit.*, pp. 577, 581.

(13) Cf. S. ARROWSMITH, *The Law of Public and Utilities Procurement*, *op. cit.*, par. 9-131.

Some authors seem to argue<sup>(14)</sup> that the use of the innovation partnership procedure should be restricted only to scenario (1) ('new' products, services or processes), and the procedure should not be extended to merely introducing 'significant improvements' according to our scenario (2). These authors do so to distinguish innovation partnerships from competitive dialogues and the competitive procedure with negotiation. However, this interpretation may lead to at least two possible issues, specifically: 1) whether the European legislator had a different understanding of 'innovation' in Article 31(2) PPD on the one hand ('development of an innovative product, service') and in Art. 22(1) No. 22 PPD on the other hand; and 2) whether the procurement needs must necessarily aim at developing a completely new product (e.g., a 'breakthrough innovation' so to speak) or if the legal requirements can be met merely by an 'incremental innovation'. Consequently, the contracting authorities must bear the risk resulting from an uncertain definition of the term 'innovation', that is, if a contracting authority wrongfully considers the innovation partnership to be applicable, and, hence, chooses an incorrect procedure, this will be a violation of the procurement rules, which can be contested through a review procedure.

To minimize the inherent risk for a contracting authority considering an innovative partnership, the authority must monitor the market to avoid choosing the innovation partnership wrongfully. That market review also reduces the tenderer's risks in developing an innovative solution, for a thorough market survey which confirms the novelty of the item makes it less likely that the contracting authority will terminate the contract prematurely.

### 1.2.1. Development and purchase of innovations

In choosing an innovation partnership among the available procurement methods, the contracting authority must aim at both developing and purchasing the innovative product. This requirement reflects the purpose of the innovation partnership: innovation partnership is intended to encourage tenderers to create innovations by holding out the prospect that the contracting authorities will purchase the product resulting from the innovation.

In purchasing the product, the contracting authority must define the arrangements on intellectual property rights in the procurement documents according to the competition regulations<sup>(15)</sup> (*see* Art. 31[6][3][1] PPD). Nevertheless, the innovation partnership does not necessarily have to aim at purchasing an exclusive right of use for the innovation. Such an exclusive obli-

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(14) *Cf.* E. BADENHAUSEN-FÄHNLE, "Die neue Vergabeart der Innovationspartnerschaft", *op. cit.*, pp. 743, 745.

(15) *Cf.* the R&D Framework, 12, section 33(b); P.C. GOMES, "The innovative Innovation Partnerships under the new EU directive for the public sector", in PPLR, volume 4, 2014, p. 211, esp. pp. 217 f.

gation could run counter to the purpose of innovation partnership to provide incentives for tenderers (because further economic uses of the innovation will become very limited).(16)

Against this background, the material scope of the innovation partnership can be put in context through Article 14(2) of PPD and paragraph 116(1), No. 2, of GWB. In principle, the PPD and the GWB rules cover only certain research and development ('R&D') services, on the condition that the contracting authority (1) holds the exclusive property rights of the outcomes, and (2) solely finances all the services therein. In contrast, as we have seen, the innovation partnership does not necessarily have to result in purchasing the exclusive rights. It is therefore reasonable to assume that Article 14(2) of PPD and paragraph 116(1), No. 2, of GWB do not restrict the application of the rules on innovation partnership. As a result, all activities that contribute to developing the innovative solutions that are not available on the market fall within the material scope of the innovation partnership – even if they are not awarded, per se, by tender pursuant to Article 14(2) of PPD and paragraph 116(1), No. 2, of GWB.(17)

## ***2. Distinguishing Innovation Partnerships From Other Procedures Which Also Promote Innovation***

The requirements as described in the preceding section clearly separate the material scope of the innovation partnership from those of other procedures that also promote innovation.(18) In contrast to the negotiated procedures and the competitive dialogue, under an innovation partnership the solutions sought cannot be already available on the market.(19) Consequently, an innovation partnership's scope of application is considerably limited because of the specific focus on innovations.

The unique feature of the innovation partnership is the specific and formalized regulation of 'development-plus-purchase agreements', that is, it merges development and purchase in one single procurement procedure. In fact, it is a valuable enrichment to the available procurement procedures prior to 2016. The provisions on innovation partnerships include several concrete precautions to ensure the principles of equal treatment and transparency (e.g., Art. 31[2] of PPD requires a preliminary agreement on intermediate targets, remuneration

(16) P.C. GOMES, "The innovative Innovation Partnership", *op. cit.*, p. 215.

(17) *See*, for the opposite view, E. BADENHAUSEN-FÄHNLE, "Die neue Vergabeart der Innovationspartnerschaft", *op. cit.*, p. 14.

(18) Please refer to Part A of this article for these procedures above in A.

(19) *Cf.* E. BADENHAUSEN-FÄHNLE, "Die neue Vergabeart der Innovationspartnerschaft", *op. cit.*, p. 14.

instalments on performance levels, and a maximum cost for the innovative product).(20)

## 2.1. Key elements of the award procedure

The innovation partnership award procedure has three phases:(21) (1) submission of requests to participate, (2) negotiation, and (3) execution of the innovation partnership. As recital 49 of the PPD states, the innovation partnership is based on the rules of the competitive procedure with negotiation. Thus, the rules for the competitive procedure with negotiation apply to the innovation partnership in the same way, if and insofar as there are no specific rules on innovation partnership and the application of rules on competitive procedure with negotiation does not run counter to the rationale of the innovation partnership.(22) In German procurement law, the procedural details of the innovation partnership are not provided in the GWB; instead, they are set out in the “*Vergabeverordnung*” (‘VgV’) and other subordinate regulations.

### 2.1.1. Submission of requests to participate

The award procedure starts with the publication of a contract notice, including a call for submission of requests to participate (§ 19[2][1] VgV). The contracting authority may, however, describe the need for an innovative product by (functional) technical specifications (§ 19[1][3] VgV) either in the publication notice (e.g. a more practical option) or in the procurement documents. The authority indicates which elements of this description define the minimum requirements to be met by all tenders (§ 19[1][4] VgV). It also defines the selection criteria concerning, in particular, the candidates’ capacity in the field of research and development, and in developing and implementing innovative solutions (§ 19[1][4] VgV). According to § 127(5) GWB (and § 52[2][1], No. 5, VgV), the procurement documents must include the award criteria as well as their relative weighting (or the descending order of importance for such criteria). The *minimum* time limit for receipt of requests to participate is 30 days from the date on which the contract notice is sent (§ 19[3] VgV).

Based on the submitted information, the contracting authority selects those enterprises that will further participate in the procedure. In this context, paragraph 42[2][1] VgV explicitly prescribes that only those competitors that have established proof of meeting the selection criteria (*i.e.* according to § 122[2]

(20) S. ARROWSMITH, *The Law of Public and Utilities Procurement*, *op. cit.*, p. 13, par. 9-128.

(21) *Cf.* also E. BADENHAUSEN-FÄHNLE, *VergabeR 2015*, *op. cit.*, p. 14.

(22) *Cf.* M. FEHLING, “Forschungs- und Innovationsförderung durch wettbewerbliche Verfahren”, in NZBau, 2012, pp. 673-676.

GWB the suitability to pursue the professional activity [No. 1], the economic and financial standing [No. 2], technical and professional ability [No. 3]) and have not been excluded may be selected. In particular, the candidates' experience in developing and implementing innovative solutions<sup>(23)</sup> as well as – depending on the complexity of the demanded solution – their economic and financial resources are of particular relevance for the innovation partnership. The contracting authority has discretion in selecting the candidates for the negotiation phase with utmost consideration to the principles of equal treatment and transparency. Furthermore, it can decide to limit the number of tenderers to three from the outset (§ 19[1][4] VgV and § 51 VgV).

### 3. Negotiation

The negotiating phase commences upon the invitation to the selected participants to submit tenders in the form of research and innovation projects (§ 19[1][4] VgV). The initial and all subsequent tenders are subject to negotiations that allow some flexibility with regard to organizing them; however, the final tenders must not be negotiated (§ 119[7][2] GWB and § 19[5][1] VgV). This negotiation phase aims at improving research and innovation projects in terms of content and adapting them to the contracting authority's needs. Therefore, the entire content of the procurement, except for the minimum requirements and award criteria, are subject to negotiations (§ 19[5][2] VgV). The contracting authority is permitted to carry out the negotiations in successive stages in order to reduce the number of tenders to be negotiated by applying the previously specified award criteria (§ 119[7][2] GWB and § 19[5][3] VgV). However, the contracting authority should carefully preserve the confidentiality of the information they obtain during the negotiations, while ensuring equal treatment to all competitors (§ 19[6] VgV).

The negotiation phase ends by awarding an innovation partnership to one or more tenders (§ 19[7][1] VgV). The sole criterion is the best price-quality ratio, taking into account the innovation as an important factor.<sup>(24)</sup> Therefore, the awarding of an innovation partnership that is based on the lowest price or the lowest cost is – in contrast to other procurement procedures – inadmissible (§ 19[7][2] VgV). The contracting authority can enter into an innovation partnership with only one or with several partners (§ 19[7][3] VgV).

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(23) *Ibid.*, p. 22.

(24) *Ibidem*, p. 22.

#### **4. Performance of the Innovation Partnership**

According to the general purpose of the innovation partnership procedure, the executive phase can be sub-divided into (1) an R&D-phase, which includes the development of the innovative solution, and (2) a purchase phase, when the innovative product is purchased (§ 19[8][1] VgV). The R&D-phase must be structured by intermediate targets, which have been agreed individually, and are adapted to the innovation degree of the proposed solution. Furthermore, there must be an agreement on an appropriate partial remuneration for achieving these targets (§ 19[8][2-3] VgV).

In principle, there are three possibilities to terminate an innovation partnership:

- (1) The innovative solution is purchased after completing both phases of the innovation partnership.
- (2) Only the R&D phase has been completed and the solution is not purchased because the performance levels or the maximum costs have not been met (§ 19[10] VgV, § 18[10] SektVO, § 3b[5], No. 9, VOB/A EU). If the contracting authority still aims at purchasing the innovative product despite non-compliance with the agreements, there must be a separate contract award after another tendering.<sup>(25)</sup>
- (3) The R&D phase is not completed, and the innovation partnership is terminated early (also in case it affects only a single innovation partner) at the end of a development stage. For this eventuality, the contracting authority must point out in the contract notice or in the procurement documents, whether and under which conditions it is going to exercise its right of termination (§ 19[9] VgV).

#### **5. Outlook: Made for ‘Big Innovation’**

It will be exciting to see whether and how the new instrument of innovation partnership will be used in practice. Due to its very specific scope of application (*see above in B. I. and II.*) and complex procedural structure (*see above in C.*), and in view of the (typically) high technical and legal demands for establishing a partnership, the innovation partnership procedure will probably be reserved for large, centralized and experienced contracting authorities, dealing with challenging procurement issues. It is therefore even more important to emphasize that the innovation partnership is – by far – not the only instrument of public procurement law that can be used as a tool of fostering (smaller) innovation (*see above in A.*). The innovation partnership is clearly made for ‘big innovation’.

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(25) S. ARROWSMITH, *The Law of Public and Utilities Procurement*, *op. cit.*, p. 13, par. 9-142.



**PART IV**

**Innovation  
in the Procurement Process**

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# CHAPTER 13

## Innovation in the Evaluation of Public Procurement Systems

BY

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### *1. Introduction*

Evaluating and measuring public administration and, by consequence, public policies have been some of the ultimate challenges in public governance. Striking the right balance or finding the right approach for evaluation in any domain requires a perfect understanding of the subject matter and the capacity to make choices, to decide on the methodologies and to apply certain techniques that might impact the outcome of the process. This practice is further amplified in the field of public governance, due to the subjectivity of the analysed topics, the usual lack of hard data and the difficulty of agreeing on common metrics.

Public procurement is a crucial component of good governance, poverty reduction, and sustainable development. Governments around the world spend approximately USD 9.5 trillion in public contracts every year. This fact means that on average, public procurement constitutes around 12%-20% of a country's GDP (12% of GDP in OECD Countries,(1) 16% in the European Union). In recent years, public procurement has become one of the most studied public policies. Therefore, strengthening public procurement systems is central to achieving concrete and sustainable results and to building effective institutions. Its economic impact helps explain the shift towards strategic procurement together with the recognition from many governments and stakeholders

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\* The views expressed in this article reflect those of the authors, who contributed personally and not on behalf of the OECD.

(1) OECD, "Government at a Glance", 2017.

of procurement's capacity to boost broader policy objectives, in the field of sustainability, innovation, small and medium enterprises or social considerations, and has increased the long deserved attention and interest in procurement. In fact, strengthening public procurement systems is central to achieving concrete and sustainable results and to building effective institutions.

In spite of this hype around public procurement, there is still a shortfall of evaluation and measurement techniques that could increase the understanding about the relevance and impact of public procurement systems, and hence contribute to better evidence-based decisions.

This chapter will highlight innovations in the evaluation of public procurement systems, namely by presenting the role of the *Methodology for Assessing Procurement Systems – MAPS*,<sup>(2)</sup> a tool that was revamped and revised over the past three years (2015-2018), and reviewing the arguments around its revision, a debate which has allowed the MAPS tool to stand as the only global standard to assess public procurement in a harmonised, universal and mutually accepted way.

The chapter will go through the origins of the MAPS, its revision process, analytical framework and indicators, the proposed governance and monitoring structures for its future use, including the establishment of a MAPS Secretariat, and how this process is expected to increase its potential and applicability as a solid and reliable tool to assess and evaluate public procurement systems of all kinds.

The chapter will also explain why the MAPS is the most relevant tool to evaluate public procurement systems, helping identifying areas for improvement and reform. Created more than a decade ago, the tool has recently been renovated to re-emerge as a universal assessment for countries in all contexts, regardless of their income level or development status.

MAPS is intended to provide a harmonized tool for use in the assessment of public procurement systems. MAPS is a common assessment tool to be used by countries and the international community irrespective of geographical application or income level. Efforts to ensure a wider dissemination and integration of public procurement activities with public finance management are also part of the modernization of the tool. The methodology has been designed to enable a country, with or without external partners, to conduct an assessment of its procurement system to determine the system's strengths and weaknesses. The assessment provides the country (and interested stakeholders) with information they can use to monitor the performance of the system and the success of the reform initiatives in improving it. In identifying weaknesses

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(2) See the Web site on MAPS initiative: [www.mapsinitiative.org](http://www.mapsinitiative.org).

in a given system, external financial partners are also provided with information that helps them determine risks to the funds they provide to countries.

### 1.1. Background, the creation and evolution of the MAPS

This section provides the background of the Methodology for Assessing Procurement Systems (MAPS), going back to its beginning. The origins are intricately linked with the aid effectiveness agenda adopted by the donor community in the late 1990s and early 2000s.

The MAPS was initially developed in 2003/2004 as a contribution to the collective efforts of many stakeholders to assess and improve public procurement systems, by providing a common tool to analyse information on their key aspects. This methodology was targeted initially to be used in the development context as its concept and design came from the development community.

Since its inception, the MAPS advanced in parallel to the international aid effectiveness agenda which has been marked by a series of high-level forums and agreements on development assistance since the Paris Declaration in 2005. Public procurement has been indirectly a topic from the beginning, given that procurement is central to delivering development projects.

Over the years, the MAPS evolved to be considered one of the main international tools, commonly accepted, to assess public procurement systems. This evolution is linked to a general trend: developing countries were increasingly taking charge of their own development strategies. The result was an increased demand for using the countries' own systems to implement projects. This demand had to be balanced against donors' worries about safeguarding taxpayers' money. With regard to public procurement, MAPS was included into the efforts towards increased aid effectiveness as a tool for enhancing public procurement systems and for monitoring progress in doing so<sup>(3)</sup>.

The OECD Development Assistance Committee (DAC) recognised the need for a benchmarking tool for partner countries' procurement systems during the implementation of the 2001 DAC Recommendation on Untying Official Development Assistance (ODA) to the Least Developed Countries. In an effort to increase the effectiveness and efficiency of ODA, DAC members agreed to untie their development assistance. 'Untying aid' means that goods, services and works purchased with ODA should increasingly be open to international competition; fewer and fewer ODA-financed projects should be tied to a requirement to purchase in the donor country. A DAC note on the implementation of

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(3) 4th High Level Forum on Aid Effectiveness, 2011.

the recommendation to untie ODA states that “DAC members will work with partner countries to identify needs and to support efforts” to promote “local and regional procurement in partner countries” (OECD/DAC, 2001). In order to support the practical untying of aid, aside from the commitments on paper, countries saw the need to improve country procurement systems. A diagnostic tool was identified as potential assistance to doing so.

There were two types of policy communities involved, and broadly, two streams of events were intertwined: A working group was founded that focussed primarily on public procurement and the development of the MAPS (the “World Bank / OECD Development Assistance Committee [DAC] Procurement Round Table” initiative). In addition, a broader, more overarching community devised principles for development assistance in general, which culminated for example in the Paris principles for aid effectiveness and the related High Level Forums and Declarations. While early discussions took place simultaneously, the evolution of MAPS as a procurement tool became increasingly a part of the discussions around more general principles of Public Financial Management, and of the more general principles set out in the Paris Declaration (2005.) The succession of these international high level forums on development relate to MAPS in three ways: first, the commitments coming out of these meetings triggered the development of the MAPS indicators/methodology. Second, MAPS – already in place – offered indicators to monitor the commitments. Third, broader goals of the development declarations, such as use of country systems, offered a justification for undertaking more MAPS assessments. These levers both influenced the use of MAPS and were influenced in turn by the outcome of the MAPS assessments. Table 1 summarises the main events that helped in consolidating the MAPS.

*Table 1: Timeline: MAPS development in the context of the aid effectiveness agenda*

Date	Event	Policy Community
March 2002	Monterrey Financing for Development Conference and “Monterrey Consensus”	Aid Effectiveness
January 2003	Launch of the World Bank / OECD Development Assistance Committee (DAC) Procurement Round Table	Public Procurement
February 2003	1st High-Level Forum on Aid Effectiveness, Rome and “Rome Declaration”	Aid Effectiveness

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Date	Event	Policy Community
December 2004	First publication of a public procurement benchmarking methodology (aka MAPS) as part of the Johannesburg Declaration, conclusion of Roundtable	Public Procurement
March 2005	2nd High-Level Forum on Aid Effectiveness, Paris and “Paris Declaration”	Aid Effectiveness
May 2008	Arusha Statement of the OECD DAC Joint Venture on Procurement	Public Procurement
September 2008	3rd High Level Forum on Aid Effectiveness, Accra and “Accra Agenda for Action” (AAA)	Aid Effectiveness
November 2011	4th High-Level Forum on Aid Effectiveness, Busan and the “Global Partnership for Effective Development Cooperation” (GPEDC) Cusco Declaration of the OECD DAC Taskforce on Procurement	Aid Effectiveness Public Procurement
October 2013	Meeting on the Task Force on Procurement, Rabat	Public Procurement
April 2015	Global Public Procurement conference, Manila	Public Procurement
June 2015	First meeting of the Stakeholder Group on the Revision of the MAPS	Public Procurement
July 2015	3rd International Conference on Financing for Development and the “Addis Ababa Action Agenda” (AAAA)	Aid Effectiveness
September 2015	Sustainable Development Goals (SDGs)	General

Source: Author's compilation.

As a consequence of what was previously explained, the Methodology for Assessing Procurement Systems was then developed by the joint World Bank / OECD Development Assistance Committee (DAC) Procurement Round Table initiative, which was a multi-stakeholder approach led jointly by those organisations, bringing together developing countries, as well as bilateral and multilateral donors. Their aim was to develop a set of tools and standards to guide improvements of public procurement systems, and to monitor progress on related commitments, focusing on four areas:

- 1) Develop research about the benefits of good public procurement practices (establishing the rationale for focusing on public procurement reform);
- 2) Agree on standards to benchmark progress on public procurement reform (set targets for countries' reforms and follow up achievements);

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- 3) Build capacity in public procurement systems (develop a strategy for capacity building, based on the World Bank's Country Procurement Assessment Reviews, CPAR);
- 4) Develop monitoring and evaluation mechanisms for reform progress (closely related to no. 1, benchmarks).

The diagnostic framework mentioned as the second goal of the Johannesburg Declaration essentially corresponded to the indicator framework that became the MAPS.

The MAPS was used for different purposes, with some goals receiving more attention than others, depending on the partners and countries applying the methodology.

Concretely, these were the main goals behind the development and application of MAPS:

- 1) Start and follow reform processes;
- 2) Provide a benchmark in support of use of country systems;
- 3) Harmonise and allow mutual accountability.

Since then, MAPS has been used, mainly by developing countries and institutional partners alike, to assess the quality and effectiveness of public procurement systems, but also having in view a strong fiduciary and credit component. When possible, based on the identified strengths and weaknesses, the countries and the interested partners would move on to develop reform strategies and implementation plans. These reforms typically focused on creating the foundation for a well-functioning public procurement system by establishing legal, regulatory, and institutional frameworks. At this stage, MAPS was mainly considered a 'donor tool', used primarily and principally by multilateral development banks to assess the compliance of countries' public procurement systems to support decisions about credit and investment and whether or not to use partner countries' procurement systems when implementing projects.

In recent years renewed commitments to strengthening public procurement systems were made in the global development-related agreements, notably the Sustainable Development Goals (SDGs), which elevated the debate, creating a common understanding among countries of all levels, international organisations and institutional partners about the need to work together to improve global public procurement tools and standards. While these international agreements stood in the tradition of the efforts of improving how development assistance is delivered, public procurement was increasingly perceived as a lever to achieve sustainability.

In fact, the SDGs emphasize the role of public procurement in achieving sustainable development outcomes in a clear manner: Goal 12, which looks at

sustainable consumption, features a specific target (12.7) on sustainable procurement: “Promote public procurement practices that are sustainable, in accordance with national policies and priorities”.(4) In addition, target 16.6 called for the development of “effective, accountable and transparent institutions”, which includes public procurement systems.(5) Taking advantage of this situation, MAPS re-gained importance in parallel. As described in the next section of this chapter (on the revision of the MAPS), the process to revise the tool and adapt it to today’s challenges gained momentum around the same time, and a strong congregation of interests made possible a truly state-of-the-art outcome.

## 2. *The revision process of the MAPS*

Despite repeated assessments and progress on the MAPS-scale, the amount of ODA channelled through country systems remained behind targets. In addition, the application of the MAPS repeatedly presented the same challenges, regardless of context. In early 2015, taking into account the difficulties in applying the MAPS as it was originally designed, *i.e.* to support reforms and enhance national procurement systems, the increasing recognition of public procurement as a strategic tool from a mere administrative process, and the challenges placed by new global objectives such as the SDGs, different stakeholders called for a profound revision of the MAPS. As it will be explained, the revision confirmed the consolidation of the MAPS as a reform tool, emphasising the universality and robustness of the methodology.

The revision of the MAPS was largely driven by an informal stakeholder group. This stakeholder group built on a history of similar groupings that had been formed and abandoned in parallel with the high-level development forums of the 2000s, as mentioned above. The MAPS revision process was structured as an informal exchange, driven by stakeholders who have used or will use MAPS in the future. The Stakeholder Group on the Revision of the MAPS guided the revision process. First discussions about a MAPS revision took place in 2013, emerging out of the World Bank and the OECD. First ‘stock-takes’ of how MAPS had been used were conducted; options for revising the MAPS were explored in several meetings, for example in Rabat in 2013. During this meeting, stakeholders referred back to the unfinished aspects of the Task Force on Procurement from 2011. The MAPS revision started

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(4) See the Web site of the United Nations Sustainable Development Knowledge Platform, Sustainable Development Goal, 12. Ensure sustainable consumption and production patterns.

(5) *Ibid.*, 16. Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels.

concretely in the spring of 2015, at a global public procurement conference in Manila, Philippines (20-21 April 2015). Subsequently, interested stakeholders met periodically to discuss the process of the MAPS revision and first drafts of the updated tool. Meetings were coordinated by the OECD, acting as the MAPS Secretariat, and supported in different ways by the members of the stakeholder group, which came to include representatives from countries, bilateral and multilateral development assistance providers, international organisations and other interested experts and parties, proving to be a unique gathering of international and regional players to develop a common good, under the same understanding.<sup>(6)</sup>

The stakeholder group shared the objectives of the MAPS revision. To summarize, the reasons for the revision were the following:

1. Evolution of public procurement within public policy and development policy;
2. Increasing importance of performance over compliance;
3. Improving coordination;
4. Emphasising the universality of the MAPS approach.

1. Evolution of public procurement within public policy and development policy.

Public procurement as a policy and research area progressed substantially in recent years. The most immediate reason why a MAPS revision was called lies in this progress. It goes beyond the scope of this paper to describe this development in detail; to grossly simplify, public procurement as a government function developed from an administrative function to a strategic function, and this change was driven by many prominent international organisations, led by the OECD. In the past, public procurement was considered as the simple purchasing of goods, services and works for the government. Now, in the majority of the cases, the strategic aspects of this activity are being highly

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(6) Representatives from the following countries and organisations participated in the exchanges of the stakeholder group: Afghanistan, African Development Bank (AfDB), Agency for Public Management and eGovernment (Difi) in Norway, Asian Development Bank (ADB), Australia's Department of Foreign Affairs and Trade, Global Affairs Canada, Caribbean Development Bank (CDB), Chile, Council of Europe Development Bank (CEB), Colombia, European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB), European Commission, Expertise France, Georgia, GIZ – commissioned by the German Federal Ministry for Economic Cooperation and Development, Inter-American Development Bank (IADB), Islamic Development Bank (IsDB), Organisation for Economic Cooperation and Development (OECD), Philippines, Senegal, SIGMA (Support for Improvement in Governance and Management), United States Agency for International Development (USAID), World Bank, Zambia, as well as independent public procurement consultants.

appreciated and accounted for, when developing and assessing the functioning of public procurement systems. Countries actively use the governmental purchasing power within a more general understanding, pursuing strategic goals beyond the narrow ones of the past. This, however, made the public procurement function much more complex than before, requiring more sophisticated legal and institutional frameworks and in turn requiring an assessment of the quality of the public procurement system that takes account of that.

International frameworks have been reflecting this shift: most notably, in 2015, the OECD developed a new standard for public procurement systems. This standard was adopted by the OECD member countries through the OECD Recommendation of the Council on Public Procurement.<sup>(7)</sup> This recommendation is based on twelve integrated principles, which function together without any prioritisation:

- Access;
- Accountability;
- Balance;
- Capacity;
- Efficiency;
- E-procurement;
- Evaluation;
- Integration;
- Integrity;
- Participation;
- Risk management;
- Transparency.

These principles describe in an aspirational way how a state-of-the-art public procurement system should look and operate. They cover the entirety of the procurement system and the entirety of the public procurement cycle. Together with many other international standards<sup>(8)</sup> and the procurement frameworks of the MDBs, it provides a background and an inspiration for the new MAPS, moving it away from the benchmark model only (defining minimum requirements) towards a principles-based and fully aspirational approach.

## 2. Increasing importance of performance over compliance.

A second development is related to this expansion in approaches to public procurement. Generally, the quality of a system was increasingly based on

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(7) See the OECD Web site on Recommendation on Public Procurement.

(8) EU Public Procurement Directives, 2014, UNCITRAL Model Law, 2011, WTO/GPA, 2014 etc.

performance considerations which cannot be assessed by applying a checkbox-style assessment. Instead of assessing mere de-jure compliance, assessors and policy makers are increasingly interested in qualitative evaluations, taking into account de-facto performance. In turn, because of this greater interest, more data has been (and has to be) gathered. This facilitates performance-based assessments in a way that was not possible before. The revised methodology now includes indicators that support this aim, while the previous version of the MAPS was not designed to conduct this type of assessment.

### 3. Improving coordination.

A third development that sparked the revision of the MAPS was the insight that coordination around assessments and reform was necessary. In fact, countries were faced with an increasing burden to undergo repeated, cumbersome assessments. A revision of the MAPS could introduce changes that facilitated self-assessments, and reduce the burden of repeated assessments by having coordination and mutually reliability/recognition. Stakeholders to the MAPS revision hope to improve coordination around MAPS assessments to exploit synergies, thereby reducing individual costs for assessments and alleviating assessment fatigue on the part of the countries. One ambition has been to revise MAPS in order to create a stronger basis for mutual recognition of assessments, by making the assessments more comparable and by possibly creating an independent party that would supervise the assessment processes. Previously, two assessment teams might not arrive at the same conclusions in the same country when applying the same methodology in the same period of time. This concept of “mutual reliance” was a strong component of the discussions and a large motivation to devote resources to the revision.

### 4. Universality of the MAPS approach.

The fourth reason for revising the MAPS was to stress the universality of the underlying aim of MAPS: to assist and support countries in improving their public procurement systems, regardless of their current status. Giving priority to this universal goal also contributed to ensuring the relevance of MAPS in the future when countries evolve. Many countries that benefitted from previous MAPS assessments indeed graduated from their status as developing country into mid-income range (such as Chile or Colombia). Constantly striving to improve their public procurement systems, their systems outgrew the previous MAPS. At the same time, the new MAPS indicator framework, targeting the entire procurement system, harbours great potential for more advanced reform. This aspect is also framed by the launch of the SDGs in September 2015, defining a universal set of aims, valid for all countries. The

revised MAPS is therefore aligned with this standard: instead of providing a low common denominator or benchmark, the revised MAPS provides aspirational goals of what constitutes a good public procurement system, applicable to all countries no matter from what development level or economic strength they are coming.

One tangible way to allow for this universal applicability in any given country context was realised by introducing optional modules in addition to a 'core' MAPS tool that focus on assessing the main (common and basic) features of a procurement system. In fact, MAPS was expanded to a "suite" model, with indicator frameworks for specific and particular topics of a public procurement system that can be added to the assessment as needed, therefore providing a more comprehensive vision of the system. At the time of writing, six optional modules are being developed, on the following topics:

- Agency-level assessments;
- E-procurement;
- Professionalization;
- Public-private partnerships and concessions;
- Sector market analysis;
- Sustainable public procurement.

This list is not exhaustive. These topics were developed taking into consideration the priorities and current trends in the implementation of optimal procurement systems as understood by the MAPS Stakeholders Group. Additional optional modules may be added in the future, as per proven demand from countries or institutions.

Following the substantive review of the MAPS indicator system, the first draft of the revised MAPS was vetted. In the summer of 2016 (from August to October), the draft was publicly available for comment on an OECD Web site;<sup>(9)</sup> the draft was also widely circulated in the public procurement and policy communities. Overall, 25 comments were received from 35 countries, agencies, civil society organisations and procurement experts from five continents. Some contributions were submitted jointly. In addition to the solicitation of comments remotely, the MAPS draft was first presented and discussed with a larger audience in a November 2016 meeting in Dakar, Senegal, co-organised by the Senegalese public procurement authority *Autorité de Régulation des Marchés Publics* (ARMP) and the OECD. Overall, the intention has been to create an inclusive revision process, as evidenced

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(9) See the OECD Web site on the consultation on the revised Methodology for Assessing Procurement Systems (MAPS).

by this broad public consultation in addition to the already very representative stakeholder group on the revision of the MAPS. The feedback has been overall positive. Comments generally positively acknowledge some innovations in the MAPS which responded to the criticisms and goals described earlier. Further improvements were called for with respect to addressing some questions of policy making, as well as technical aspects related to the concrete formulation of indicators. A summary of the feedback can be accessed at the consultation website.<sup>(10)</sup> In the first half of 2017, the MAPS was tested in a limited number of countries, both developed and developing ones (Norway, Chile and Senegal). These assessments follow the goal of testing whether the revised MAPS methodology works in practice and in what areas it has to be improved, but were nevertheless very comprehensive assessments of a country's public procurement systems, which allowed the national authorities to build on the assessments. The lessons learned from these testing exercises were taken up together with the feedback of the public consultation in the second draft of the revised MAPS, which was presented in October 2017.

### ***3. The New Methodology for Assessing Procurement Systems (MAPS 2018)***

As previously mentioned, the new version of MAPS comes timely in the wake of the launch of the SDGs. Like the SDGs, MAPS will be relevant for all countries, irrespective of income level or development status. In addition, MAPS is anchored in the 2015 OECD Recommendation of the Council on Public Procurement and reflective of leading international procurement frameworks such as the UNCITRAL Model Law on Public Procurement (2011), the EU Directives on Public Procurement (2014), the procurement frameworks of most of the multilateral development banks, the procurement-related indicators of international standards (such as PEFA), and new trends towards open contracting initiatives. It provides a holistic assessment framework by establishing the criteria of an effective and efficient procurement system that countries should strive to achieve.

The new MAPS has in its core assessment tool three main sections:

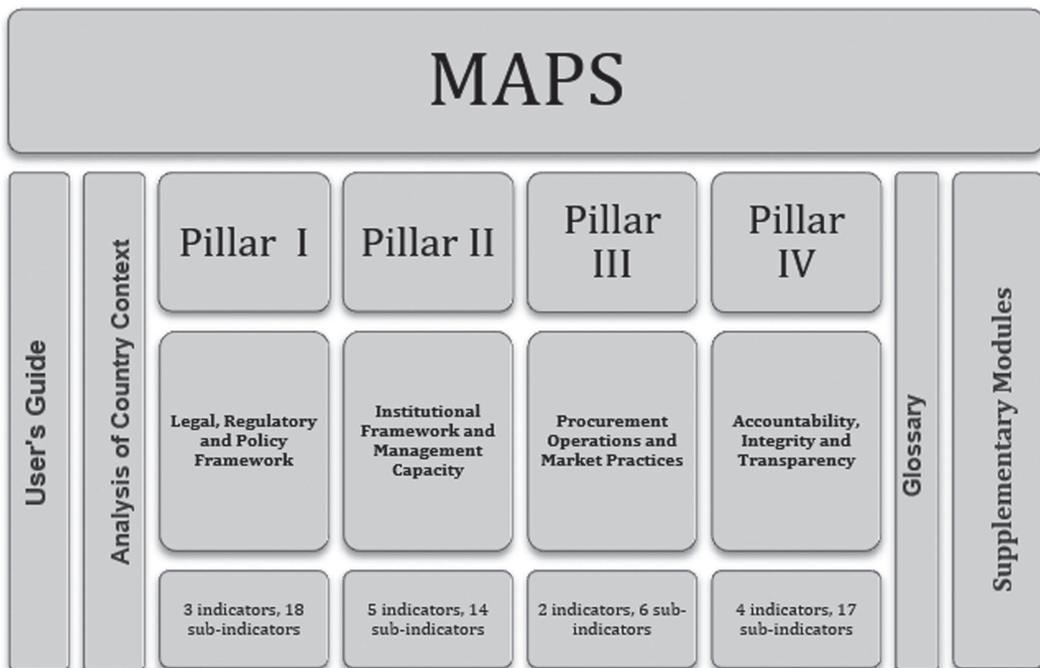
- Section I – User's Guide;
- Section II – Analysis of Country Context;

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(10) *Ibid.*

- Section III – Assessment of Public Procurement Systems: 4 Pillars, 14 indicators, 55 sub-indicators; indicators are expressed in qualitative and/or quantitative terms (assessment criteria).

The MAPS analytical framework is presented in Fig. 1 below.



*Fig. 1 – The MAPS Analytical Framework*  
 Source: MAPS Stakeholder Group

In terms of the analytical framework the new MAPS includes not only core indicators, but also supplementary modules, and require an analysis of the country context. The indicator system was enhanced and expanded and the scoring system was abandoned. The former scoring system had merits but turned out to be counterproductive, as countries tended to focus more on the result in itself than on the reasons that led to that result or on the areas for improvement deriving from it. Instead the new MAPS focuses on determining substantive or material gaps and will assign red flags (if necessary), based on a 3-step approach:

- Step 1: Review of the system applying assessment criteria expressed in qualitative terms;
- Step 2: Review of the system applying assessment criteria expressed in quantitative terms;
- Step 3: Analysis and determination of substantive or material gaps (gap analysis) to illustrate the need for developing adequate actions to improve the quality and performance of the system.

The new MAPS is designed to work with a colour mechanism (green, yellow and red), to allow an immediate recognition of the current situation for each of the indicators in each pillar. Should the assessor identify reasons that are likely to prevent adequate actions ‘red flags’ should also be assigned (e.g. disagreement on assessment results; national laws /international agreements impose contrary obligations; other reasons preventing appropriate improvements) etc.

A huge emphasis was also put on improving the assessment process by developing a set of supporting tools, such as concept notes, terms of reference, new data collection methodologies and engagement of stakeholders, from the initial planning to the validation of the assessment results, including a strong stance on quality assurance and peer review mechanisms.

On a pillar by pillar analysis we can highlight the improvements described below. In general terms, we can say that the MAPS Stakeholders Group introduced plenty of innovations in the new methodology (innovations since 2003 when MAPS was initially developed). These changes reflect the modern understanding of public procurement in the international scene, the alignment towards the SDGs and the linkages between the pillars and the optional modules, allowing a complete coverage of the procurement cycle in a comprehensive and strategic manner. Most of the indicators were streamlined and the assessment criteria refined to give a global vision for public procurement, moving away from the development angle only.

### 3.1. Pillar I – Legal, Regulatory and Policy Framework

Pillar I deals with the legal aspects of the system. The main novelty is indicator 3, which is new and looks at some basic aspects of Sustainable Public Procurement – SPP (e.g. whether the country has adopted a policy to implement SPP in support of broader national policy objectives, and whether the legal framework permits the consideration of sustainability criteria (economic, environmental, social criteria) in public procurement. It also analyses international obligations, looking at legal obligations relating to public procurement that originate from membership in international and/or regional associations

or other binding agreements, e.g. consistent reflection in corresponding laws and regulations. Table I below provides an overview of the 3 indicators of Pillar I.

*Table 1 – MAPS Pillar I – Legal, Regulatory and Policy Framework*

Indicators	Content
<b>1 Legal framework achieves principles; complies with obligations</b>	<i>Are laws and regulations covering all aspects of public procurement?</i> <ul style="list-style-type: none"> <li>• Regulations for the entire procurement cycle</li> <li>• E-procurement, data management</li> <li>• Public procurement principles</li> </ul>
<b>2 Supporting regulations and tools</b>	<i>How are the laws translated into practice?</i> <ul style="list-style-type: none"> <li>• Implementing regulations</li> <li>• Model documents, templates</li> <li>• Guidance</li> </ul>
<b>3 Secondary policy objectives, international obligations</b>	<i>What is the overarching framework?</i> <ul style="list-style-type: none"> <li>• Sustainable Public Procurement (SPP)</li> <li>• Obligations deriving from international agreements</li> </ul>

### 3.2. Pillar II – Institutional Framework and Management Capacity

Pillar II assesses the institutional setting and the management capacity providing new approaches. Indicator 5 contains criteria about the assignment of functions without gaps or overlaps, the way authorities are in line with responsibilities assigned or are free from possible conflicts of interest. Indicator 7 is new and addresses electronic procurement, to understand to which extent e-Procurement is currently used and what is the existing capacity to deal with it or the corresponding strategic plans. Another novelty relates to the treatment given to open data and disclosure of information in support of the concept of open contracting. Indicator 8 is also new and bundles several components relevant for managing and improving the public procurement system as a whole, such as training, advice and assistance, professionalisation, performance measurement systems that focus on outcomes vs. set targets, development impact, and strategic plans to improve the system. Table 2 highlights the relevant topics in each indicator of Pillar II.

*Table 2 – MAPS Pillar II – Institutional Framework and Management Capacity*

Indicators	Content
4 Mainstreaming and integration with the PFM system	<i>Is the procurement system well-coordinated?</i> <ul style="list-style-type: none"> <li>• Planning, budgets</li> <li>• Financial procedures</li> </ul>
5 Institution in charge of the normative / regulatory function	<i>How is the procurement regulator structured?</i> <ul style="list-style-type: none"> <li>• Status, responsibilities</li> <li>• Organisation, funding, staffing, level of independence</li> </ul>
6 Procuring entities and their mandates	<i>How are procuring entities structured?</i> <ul style="list-style-type: none"> <li>• Responsibilities, mandates</li> <li>• Centralized procurement body</li> </ul>
7 Information systems	<i>How is procurement information managed?</i> <ul style="list-style-type: none"> <li>• Publication, information technology, e-Procurement</li> <li>• Strategies</li> </ul>
8 System's capacity to develop and improve	<i>How does the system learn?</i> <ul style="list-style-type: none"> <li>• Training, assistance for procurers</li> <li>• Procurement as a profession</li> <li>• Performance monitoring</li> </ul>

### 3.3. Pillar III – Procurement Operations and Market Practices

Pillar III goes beyond the original MAPS traditional approach by addressing the procurement operations and the functioning of the system in practice. It is a breakthrough pillar, closing the gap between qualitative and quantitative assessments, between compliance-based analysis and performance measurement indicators. In spite of having just two indicators this pillar is quite comprehensive in its analysis. Indicator 9 was designed with the objective of collecting empirical evidence on how the procurement system works in practice, by looking at the practical implementation of procurement principles, rules and procedures formulated in the legal and policy framework. The focus is on the results of the procurement procedures, specifically those that have a higher impact in terms of value for money, improved service delivery, trust in government and secondary policy objectives. It is a demanding exercise as it requires the selection and review of a (representative) sample of actual procurement cases. To substantiate the assessment, the use of additional quantitative indicators is recommended.

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Indicator 10 contains aspects related to the market and key procurement sectors and also the interaction with the private side, such as the participation of civil society in consultative processes when formulating changes to the system, or measures that can improve access to the government marketplace by the private sector. Table 3 below reflects how these indicators are framed.

*Table 3 – MAPS Pillar III – Procurement Operations and Market Practices*

	Indicators	Content
9	Public procurement practices	<i>How does the system perform in practice?</i> <ul style="list-style-type: none"> <li>• Planning</li> <li>• Selection</li> <li>• Contract management</li> </ul>
10	Public procurement market	<i>How is the private sector involved in public procurement?</i> <ul style="list-style-type: none"> <li>• Dialogue, partnerships</li> <li>• Organisation, access to public procurement</li> <li>• Key sectors and sector strategies</li> </ul>

### 3.4. Pillar IV – Accountability, Integrity and Transparency of the Public Procurement System

The last pillar of the MAPS provides a decisive contribution to a complete assessment of a public procurement system by looking at indicators designed to assess key dimensions, such as integrity or transparency. It is also innovative as it includes open contracting principles and it is aligned with the upgraded PEFA framework in some of its sub-indicators. It also recognizes the role civil society can play as a safeguard against inefficient and ineffective use of public resources. That includes among others a focus on making public procurement more competitive and fair or improving contract performance. The pillar also provides clear guidance and visionary directions towards the establishment, independence and capacity of the appeals bodies. Finally, the last indicator covers a wide array of measures to prevent, detect and penalize corruption in public procurement. Reflecting the innovative and evidence base approach of the new MAPS, several quantitative indicators are recommended to substantiate the assessment of indicator 14. Table 4 provides an overview of the content for each of the indicators of Pillar IV.

*Table 4 – MAPS Pillar IV – Accountability, Integrity and Transparency of the system*

	Indicators	Content
11	Transparency and civil society engagement	<p><i>How is the public involved in procurement?</i></p> <ul style="list-style-type: none"> <li>• Consulting the public and civil society, access to information by the public</li> </ul>
12	Effective control and audit systems	<p><i>How is the control system in charge of procurement working?</i></p> <ul style="list-style-type: none"> <li>• Laws, organisation, procedures, coordination, enforcement in the control system on procurement</li> <li>• Qualification and training</li> </ul>
13	Appeals mechanisms	<p><i>How is the appeals system working?</i></p> <ul style="list-style-type: none"> <li>• Process for challenges and appeals</li> <li>• Independence, capacity, decisions of the appeals body</li> </ul>
14	Ethics and anticorruption measures	<p><i>How is integrity in procurement safeguarded?</i></p> <ul style="list-style-type: none"> <li>• Laws on prohibited practices</li> <li>• Implementation of integrity measures (training, code of conduct, reporting, enforcement, procurement documents)</li> <li>• Stakeholder support</li> </ul>

#### **4. The governance structure of the New MAPS**

As explained in the previous sections, following a general consensus and understanding towards creating a global and more effective instrument to assess public procurement systems worldwide, the MAPS was revised between 2015-2018 by a wide group of stakeholders, organised successfully in an informal manner, that formed the so-called informal MAPS Stakeholder Group, coordinated by the OECD as the informal secretariat. The updated core methodology was presented in October 2017 and endorsed by the OECD Working Party of the Leading Practitioners in Public Procurement, the formal OECD body in charge of public procurement matters. While the previous MAPS development and the revision were informal, the MAPS Stakeholder Group is now working towards institutionalising the new MAPS and its supporting structures to ensure sustainable implementation of the MAPS initiative and the subsequent follow up, including any remaining aspects of the revision process (such as the completion of the optional modules.)

In fact, one of the most important points of consensus generated when the revision of the MAPS started was the agreement by all partners that a new, modern and effective approach towards managing the new tool was needed, if it was to

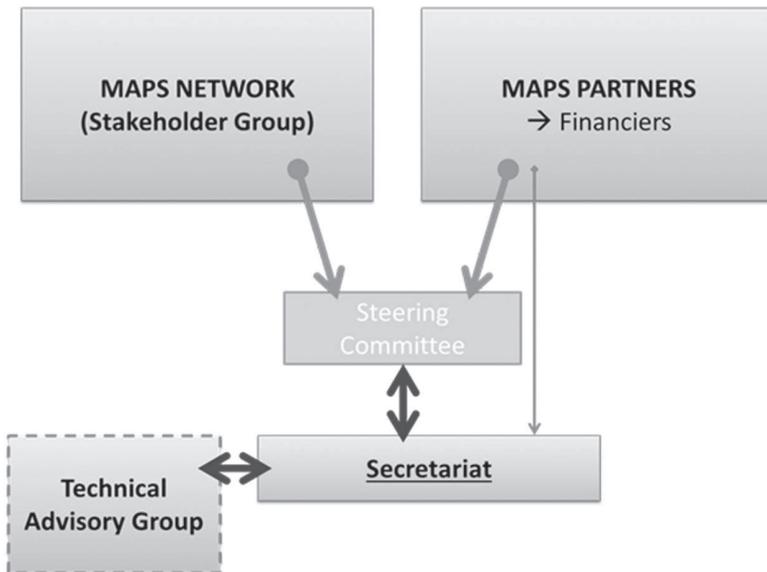
achieve the expected objectives. To achieve that in a sustainable way, the stakeholders supporting the MAPS have been working over the last three years to attain a governance structure reflective of the aspirational features of the tool; *i.e.* harmonised, universal and a basis for reforms. To reach these ambitious goals it was necessary to conceive not just a central entity that could act as the guardian of the methodology, be the repository of the information, provide guidance and training or monitor the performance of the MAPS – the formal MAPS Secretariat – but also to embed it in the other pieces of the surrounding environment.

In fact, to ensure the attainment of the objectives of the MAPS initiative, it was considered necessary to create a comprehensive and inclusive governance structure, capturing the different experiences, sensitivities, backgrounds and expectations of the stakeholders. The following paragraphs detail the vision for the MAPS Secretariat and the governance structure, as it had been agreed by the MAPS Stakeholder Group at the time of writing. Aside from the Secretariat, the core-governing bodies are suggested to be:

- The MAPS Partners (*i.e.* financial);
- The MAPS Network;
- The Steering Committee;
- The Technical Advisory Group.

Their envisioned corresponding tasks are outlined below as agreed previously, irrespective of a possible implementation at a later stage; figure 2 provides an overview of the governance structure.

Fig. 2: MAPS Governance Structure



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*Source: MAPS Stakeholder Group*

#### 4.1. MAPS Partners

The MAPS Partners would represent the financiers of the secretariat providing a certain minimum amount. The amount of funding provided by each member is contingent upon their capabilities, taking into account the different demand for MAPS-related services from each of the development banks.

#### 4.2. MAPS Network

The MAPS Network is a formal continuation of the informal Stakeholder Group on the Revision of the MAPS. This grouping includes the founders of the MAPS and other interested parties, including non-paying members with an interest in the tool. The MAPS Network would ensure representation and inclusion of parties that might be implicated by MAPS assessments (such as countries) or that have a voice on topics featured in the MAPS, such as countries or non-paying international organisations like the OECD and World Bank as the original sponsors of the MAPS. The group would remain open.

To ensure a meaningful inclusion of the MAPS Network in the governance of the MAPS, a limited number of MAPS members would participate in the Steering Committee. As an initial number, five members of the MAPS Network would take seat in the Steering Committee:

- One representative of the developing countries;
- One representative of bilateral assistance providers;
- One representative of the development banks;
- Two representatives for the original sponsors of the MAPS and major contributors to the revision process, the World Bank and the Chair of the Working Party of the Leading Practitioners in representation of the OECD.

Participation in the Steering Committee would rotate.

#### 4.3. Steering Committee

The Steering Committee would be the oversight body over the Secretariat. It would consist of all financiers of the initiative, plus five members of the MAPS Network. The participants from the MAPS Network would rotate, and would be included to maintain a link to the constituency that is unable to contribute financially but should be heard in the oversight over the secretariat (such as developing countries).

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#### 4.4. Technical Advisory Group

The primary task of the Technical Advisory Group is to ensure intrinsic and even quality of individual MAPS assessments, also providing a forum to raise concerns related to individual MAPS assessments.

While the concrete Technical Advisory Group supervising different MAPS assessments will differ, each member of the MAPS Network and member of the Steering Committee would designate a contact point that serves as the first contact for the MAPS Secretariat with regards to MAPS assessments. In general, the Technical Advisory Group for each country assessment would review assessment reports and other documents as needed, and could provide comments to the assessment.

#### 4.5. The MAPS Secretariat

The MAPS Secretariat would be established to ensure sustainable support of the MAPS Initiative and all activities related to the MAPS, including fulfilling a range of functions to support scale-up and utilisation of the new MAPS. It was designed building on previous experiences and already established structures that provide examples of good practices. The MAPS Secretariat would be the 'guardian' of the revised MAPS. The MAPS Stakeholder Group agreed to work together towards having the OECD as the host institution to the MAPS Secretariat. The informal MAPS Stakeholder Group agreed on the following objectives for the Secretariat:

1. Promotion of the MAPS;
2. Quality control/assurance of assessments and assessors;
3. Impact studies around the use of MAPS, including collection of statistics/data;
4. Maintenance of the MAPS (future improvements);
5. Training for officials and assessors.

The Secretariat would be in charge of the day-to-day management and coordination in furtherance of roll-out and global utilisation of the MAPS. The Secretariat would also facilitate quality assurance of MAPS assessments, and assist countries in planning and conducting MAPS assessments.

It is estimated that the multilateral development banks alone would conduct approximately 20 to 25 MAPS assessments per year on average. This estimate is based on the number of assessments conducted by the multilateral development banks from the creation of MAPS in 2004/5 until 2016, and takes into consideration that some of these assessments overlapped in the past with regards to the evaluated country. A MAPS Secretariat would be able to coordinate the different assessments and ensure that a country is

not assessed several times within a short period of time by different actors. An independent quality check of the assessments is necessary to achieve this consolidation of the MAPS assessments. To ensure that all parties trust and use the same MAPS assessment, each assessment should be vetted by an independent, neutral institution – the MAPS Secretariat. The MAPS Secretariat could also link parties who wish to conduct an assessment of the same country, to potentially create synergies. In addition, a secretariat could support countries wishing to conduct self-assessments.

The below paragraphs explain in brief the rationale behind each suggested objective and the outcomes that are envisioned.

#### 4.6. Objective 1: Promotion of the tool/MAPS

- Establish access to past MAPS assessments: the Secretariat would maintain a publicly accessible, electronic database with those MAPS assessments that have been conducted under the guidance of the Secretariat, *i.e.* that have passed the quality check and that have been cleared by the respective governments.
- Provide help desk-type support to assessors using the MAPS methodology: The Secretariat would provide technical support to those who wish to apply MAPS and would facilitate the use of the MAPS. It would be possible to establish a basic help-desk function immediately.
- Conduct outreach and communication related to the MAPS: MAPS as a tool is an established brand. In addition to the tasks related to the MAPS assessments as described above, the Secretariat would conduct limited MAPS-related outreach and communication to maintain the “MAPS brand” to ensure visibility and to gather feedback.

#### 4.7. Objective 2: Quality control/assurance of assessments and of assessors

- Conduct quality monitoring and provide ‘certification’ of assessments that meet the quality standard specified in the MAPS. The quality assurance mechanism is at the core of the functions of the Secretariat to ensure credibility of MAPS assessments and support mutual reliability. The Secretariat would be in charge of ensuring the quality of the assessments conducted with the approval of the MAPS Secretariat.
- The Secretariat would be able to provide basic quality assurance functions by reviewing and approving the terms of reference and concept notes of MAPS assessments. The MAPS Secretariat would conduct formality checks of the MAPS assessments. This means that the MAPS

Secretariat would review the process and documents associated with a given MAPS assessment, such as TORs, concept notes, and other planning documents. The Technical Advisory Group would provide an additional level of quality assurance for the MAPS assessments. The vetting process for MAPS assessors is envisioned as an incremental process, step-by-step building up to a structured process (in line with the Secretariat's capacity.)

#### 4.8. Objective 3: Impact studies around the use of MAPS, including collection of statistics/data

- Monitor the impact of the MAPS: This task would include a) the collection of data / statistics about the use of MAPS beyond the mere collection of conducted assessments (e.g., by conducting evaluations and surveys around the assessments); b) the analysis of the data, and c) the publication of studies of the collected statistics. Given the complexities of impact evaluation, and to allocate sufficient attention and expertise to this important aspect, the Secretariat would develop a coherent strategy and a framework for impact assessment related to the MAPS.

#### 4.9. Objective 4: Maintenance of the tool (future improvements)

- Monitor over time to what extent MAPS as a tool remains adequate for fulfilling its stated purpose and trigger future revisions where necessary to improve the tool: The MAPS Secretariat would fulfil tasks to ensure that the MAPS remains up-to-date. This would include organising periodic reviews and meetings of the stakeholders and bodies in the governance structure, keeping abreast with regards to other, international instruments and methodologies, as well as related tools and initiatives, and to trigger future revisions to the MAPS.

#### 4.10. Objective 5: Training for officials and assessors

- Provide training for public procurement officials, assessors and any other interested stakeholders in relation to the aspirational standards set in the MAPS: This task would include designing training modules and delivering or providing support to delivering training on how to conduct an assessment with the methodology, how to address findings from an assessment and how to implement changes for a better public procurement

system. This task of the Secretariat would focus on conveying knowledge about the MAPS, without aiming at a certification.

### ***5. Conclusion***

As mentioned in the introduction, evaluating public procurement, its strategies and systems, its complexities, its interactions and linkages to broader policy objectives or to public finance management in general is far from being an exact science or a finished task. However, there is a clear understanding amongst the international community about the need to improve methodologies and tools and provide global standards to help countries assessing the functioning of their procurement systems in a clear, sound and impactful way. A convergence of wills and needs originated the first Methodology for Assessing Procurement Systems, MAPS, back in 2003/2004, allowing it to be used by donors and development banks around the world over the past 15 years, and making it one of the most recognized tools for assessing public procurement. An even stronger convergence, interest and commitment from relevant partners started the revision process of this methodology back in 2015.

As explained in the previous sections, the new MAPS was prepared and developed to emerge as the global international standard to assess public procurement in all countries, irrespective of their income level or development status. All steps that were taken in the recent years will allow creating a robust foundation for a sustainable application of the revised MAPS in the years to come. The new MAPS is a great improvement from the previous methodology. It generated a global consensus among all parties. It has a clear governance model and quality assurance mechanisms. Its goals are clear and the structures that were designed will help achieving them. All partners to the MAPS initiative need to play their role properly to ensure that the MAPS will be universal, harmonized and a true global standard. In that regard, the independent MAPS Secretariat will play a very important role in guaranteeing that the objectives of the new MAPS are achieved. The innovation that was put in the collaborative approach that built the new MAPS is reflected in the quality of the tool but also in the sustainable approach that is envisaged for its future. With this in mind it is possible to say, starting from now, that the paradigm of evaluating public procurement systems has changed. And that it has a new standard, the Methodology for Assessing Procurement Systems, the MAPS, our contribution to better policies for better lives.

## CHAPTER 14

### The Pursuit of Streamlined Purchasing: Commercial Items, E-Portals, and Amazon

BY

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#### *1. Introduction*

Throughout its history, the U.S. federal government has considered a range of innovations in its procurement policies and practices. A number of these efforts have involved the acquisition of commercial items. In U.S. federal procurement, the term ‘commercial items’ generally refers to those products and services that are of a type offered, sold, or leased in the commercial marketplace.(1) The U.S. federal government has long promoted the acquisition of commercial items, and while policies promoting commercial item acquisition have existed since the 1970s, the major acquisition reforms of the 1990s, the Federal Acquisition Streamlining Act of 1994 (FASA), and the Clinger-Cohen Act of 1996 (CCA, also known as the Federal Acquisition Reform Act of 1996 [FARA])(2) placed a renewed emphasis on the federal government’s purchase of commercial items. These reforms to accommodate the commercial market are gaining new momentum, as the U.S. government explores the use of commercial online platforms, such as Amazon, for direct purchases by government officials that would bypass traditional procurement channels.

#### *2. Procurement Reform and Commercial Items*

The commercial item provisions of FASA were based on recommendations from an advisory panel established under the National Defense Authorization Act (NDAA) of 1991.(3) The 1991 NDAA directed the Department of Defense (DoD) to establish an advisory panel, known as the Section 800 Panel,

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(1) Federal Acquisition Regulation (FAR) 2.101 includes a formal definition for commercial item.

(2) Federal Acquisition Streamlining Act of 1994, Public Law No. 103-355, 13 October 1994; Federal Acquisition Reform Act of 1996, Public Law No. 104-106, Division E, Section 4001, 10 February 1996.

(3) “National Defense Authorization Act for Fiscal Year 1991”, Pub. L. No. 101-510.

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to (1) review the acquisition law applicable to the DoD with a view toward streamlining the defense acquisition process; (2) make any recommendations for the repeal or amendment of such laws as the Panel considered necessary; and (3) prepare a proposed code of relevant acquisition laws.(4) Prior to the 1990s procurement reforms, DoD agencies frequently met their needs through government-unique requirements, with products frequently designed under government-specific specifications. Along with the move to introduce reform and greater efficiency to the procurement process, the findings of the Section 800 Panel identified the benefits of purchasing commercial items, including: that they are less expensive; are more technically advanced than their government unique counterparts; purchasing commercial increases competition, which generally leads to lower prices; they offer greater economies of scale, increase surge capacity and increased access to cutting-edge technologies.(5)

Thus, the Section 800 Panel recommended changes to the procurement laws, including: a preference for commercial items; a definition of commercial item; a more streamlined process for commercial items acquisitions; and relief from numerous statutes and contracts clauses for acquisitions for commercial items.(6) The Section 800 Panel recommendations were adopted in FASA. In addition to the commercial item benefits noted above, the federal government has recognized that while historically, DoD procurements often took the lead in promoting technological developments, more recently, such development occurs primarily in the private sector.(7) Therefore, in addition to promoting a more streamlined procurement process, the less burdensome requirements for commercial items were established in part to encourage commercial item vendors to offer their products and services to the federal government.

In 1996, the CCA added a definition for commercial-off-the-shelf (COTS) items. COTS items are those commercial items that are: sold in substantial quantities in the commercial marketplace; and offered to the Government, under a contract or subcontract at any tier, without modification, in the same form in which it is sold in the commercial marketplace.(8) COTS items are a

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(4) Government Accountability Office, *Acquisition Reform: DOD Acquisition Law Advisory Panel's Operations and Report*, GAO/NSIAD-94-5, December 1993.

(5) See Section 809 Panel Report, *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations*, Vol. I, January 2018 (recounting history).

(6) FAR 12.503, Applicability of certain laws to Executive agency contracts for the acquisition of commercial items, lists the statutes that are not applicable to commercial item procurements, such as those related to: Cost Accounting Standards, Truthful Cost or Pricing Data, Contingent Fees, Requirement for a clause and certain other requirements related to kickbacks and Requirement for a clause under the Fly American provisions.

(7) Office of the Undersecretary of Defense For Acquisition, Technology and Logistics, "Intellectual Property: Navigating Through Commercial Waters: Issues and Solutions When Negotiating Intellectual Property With Commercial Companies", 15 October 2001; Office of Secretary of Defense Acquisition, Technology and Logistics, "Commercial Item Handbook", November 2001.

(8) FAR 2.101, Definitions.

subset of commercial items and have exemptions from procurement laws and regulations in addition to those that do not apply to commercial items; such as component tests of domestic sources under the Buy American Act.(9)

### ***3. Federal Purchase Cards and Lessons Learned***

Among the procurement innovations introduced by FASA and CCA was the expanded use of a purchase card program, which involved contracts with banks to provide standard commercial charge cards for use by federal employees.(10) FASA authorized agency cardholders to make micro-purchases (initially capped at \$2,500 and later raised to \$3,500) without obtaining competitive quotations if the price was considered reasonable and the agencies ‘equitably distributed’ such purchases among qualified vendors.(11) From 1994, when the expanded program was launched, to 2003, the use of government purchase cards increased from \$1 billion to \$16 billion.(12) While the purchase card program offered greater opportunity for streamlined acquisition of small, commercial item purchases, GAO and others found that the program was also plagued by fraud, waste and abuse, as well as inefficient purchasing.(13) In particular, GAO found in 2004 that: “improvements in program management and oversight could save hundreds of millions of dollars by (1) strengthening controls and monitoring transaction activity to minimize fraudulent, improper, and abusive purchase card transactions and (2) leveraging the government’s buying power to achieve discounts with frequently used vendors”.(14)

In response to recommendations from GAO, the General Services Administration (GSA) and the Office of Management and Budget (OMB) took a number of steps to improve the purchase card program, including training programs for agency users, monitoring tools and guidance.(15) OMB guidance required cardholders to maintain documentation to minimize the risk of erroneous and improper purchases.(16) GAO recently conducted a government-wide review of the purchase card program and issued a report in February 2017.(17) GAO

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(9) FAR 12.505, Applicability of certain laws to contracts for the acquisition of COTS items.

(10) Government Accountability Office, “Contract Management: Agencies Can Achieve Significant Savings on Purchase Card Buys”, GAO-04-430, p. 4.

(11) *Ibid.*, p. 9, and pp. 4-5 and ff.

(12) *Ibid.*, p. 11.

(13) Government Accountability Office, “Purchase Cards: Increased Management Oversight and Control Could Save Hundreds of Millions of Dollars”, GAO-04-717T, 28 April 2004.

(14) *Ibid.*, p. 13.

(15) Government Accountability Office, “Government Purchase Cards: Little Evidence of Fraud Found in Small Purchases, but Documentation Issues Exist”, GAO-17-276, 14 February 2017.

(16) *Ibid.*, p. 15.

(17) *Ibid.*

found little evidence of improper or potentially fraudulent purchases among micro-purchase transactions, but noted that incomplete documentation increased the risk that fraud, charge card misuse, and other abusive activity could occur without detection.(18) The lessons learned from the purchase card program may prove useful as the federal government considers further innovations in commercial item procurement, such as the e-commerce portal program discussed below.

#### **4. Commercial Item Purchases – The Next Steps**

Current federal procurement laws and regulations continue the preference established under FASA and CCA for the acquisition of commercial items. Regulations governing agency procurements require agencies to conduct market research to determine whether commercial items or non-developmental items(19) are available to meet the Government’s needs or could be modified to meet the Government’s needs.(20) Thus, in conducting a procurement, an agency is generally required to first determine whether a commercial item exists that can meet its needs.

Despite the continued emphasis on commercial item purchasing, the consensus among many procurement experts is that, particularly for DoD procurements, the process remains overly complex and the use of commercial items to meet agency needs has not been fully realized.(21) Only 18% of DoD purchases in FY 2017 were for commercial items and over the previous five years (2012-2017) DoD spending on commercial items declined by 29%.(22) The limited success of commercial item procurements appears due in part to the fact that despite some exceptions, the procedures for commercial item purchasing are too similar to traditional procurements. In addition, a recently commissioned procurement panel, tasked by Congress with reforming the current DoD procurement process (the Section 809

(18) *Ibid.*, pp. 15, 33 and ff.

(19) Under FAR 2.101, a non-developmental item generally refers to a previously developed item of supply used exclusively for governmental purposes by a Federal agency, a State or local government, or a foreign government with which the United States has a mutual defense cooperation agreement; or a previously developed item that requires only minor modification or modifications of a type customarily available in the commercial marketplace in order to meet the requirements of the procuring department or agency.

(20) FAR 10.002(b); see, e.g., *Palantir USG v. United States*, 904 F.3d980 (Fed. Cir. 2018).

(21) Section 809 Panel Report, *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations*, *op. cit.*, pp. 15, 17 and ff.

(22) *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations*, *op. cit.*, p. 21, see also “Defense Contracts: Recent Legislation and DOD Actions Related to Commercial Item Acquisitions”, GAO-17-645, July 2017.

Panel) found a variety of reasons for the shortcomings in commercial item purchasing. The Panel found inconsistent interpretations of policy, as well as continuous changes to commercial item buying regulations. The panel noted that the FAR has been amended more than 100 times to address commercial buying and thus commercial buying policies have become increasingly difficult to follow.(23) In addition, since FASA was enacted the Panel found that the number of DoD-related commercial buying provisions had increased by 188%.(24) This increase in provisions has also impacted the number of contract clauses applicable to commercial items. In 1995 there were a total of 57 FAR and DFARS clauses applicable to commercial items.(25) In early 2018, that number had increased to 165 FAR and DFARS clauses applicable to commercial items.(26)

Thus, there are a number of issues undermining the federal government's full and effective use of commercial item procurements, which were intended to bring greater efficiency, lower costs and the latest technology to government users. The Section 809 Panel, as of 2018, is proposing a broad range of reforms to DoD procurements, including changes in the acquisition of commercial items. While the Section 809 Panel's recommendations will likely have a significant impact on how the federal government, and DoD in particular, acquires goods and services, as of this writing, they have not yet been finalized.

## 5. Amazon.gov

While, as of this writing, the broader procurement reforms and innovation from the Section 809 Panel remain a work in progress, Congress did enact legislation at the end of 2017 to test an innovative procurement method. In what has become known as the 'Amazon Amendment' or 'Amazon.gov', section 846 of the National Defense Authorization Act for 2018 (2018 NDAA)(27) establishes a framework for the use of commercial e-commerce portals (e-portals) for the purchase of COTS items.(28) By requiring the use of e-portals, on a government-wide basis, the legislation seeks to enhance competition, expedite procurement, enable market research, and ensure reasonable pricing of commercial products through multiple contracts with multiple commercial e-commerce portal providers.(29)

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(23) *Report of the Advisory Panel on Streamlining and Codifying Acquisition Regulations*, *op. cit.*, p. 21.

(24) *Ibid.*

(25) *Ibid.*

(26) *Ibid.*

(27) Section 846, "National Defense Authorization Act for Fiscal Year 2018", *Public Law* No. 115-91.

(28) *Ibid.*, No. 27.

(29) *Ibid.*

As the legislation was being developed, some in the procurement community expressed concerns that the e-portal framework was tailor-made for Amazon, given its dominance in the commerce e-portal marketplace, both in terms of consumer and business purchases.<sup>(30)</sup> While Amazon's inherent advantages may permit it to play an outsized role, the final legislation sought to address some of these concerns, although critics of the plan remained unconvinced.<sup>(31)</sup> Others have noted that while the role to be played by Amazon and other online market retailers has yet to be determined, the provision has substantial implications for companies that sell commercial items to the government, and it also sets up a potential clash between more traditional contractors and large e-commerce platforms.<sup>(32)</sup>

Section 846 of the 2018 NDAA provides for a three-phased approach to establishing the e-portals, occurring over a three-year period. Phase I: Implementation plan; Phase II: Market Analysis and Consultation; and Phase III: Program Implementation and Guidance.<sup>(33)</sup>

Under Phase I, an implementation plan was required within 90 days of when the 2018 NDAA became law (December 12, 2017), "including a discussion and recommendations regarding whether any changes to, or exemptions from, laws that set forth policies, procedures, requirements, or restrictions for the procurement of property or services by the Federal Government are necessary for effective implementation of [Section 846]".<sup>(34)</sup>

Under Phase II, not later than one year after the date of the submission of the implementation plan, the General Services Administration (GSA) (the leading centralized purchasing agency in the U.S. Government) and the Office of Management & Budget (OMB) (within the White House) were required to provide recommendations for any changes to, or exemptions from, existing laws necessary for effective implementation of the program.<sup>(35)</sup> These recommendations were to be made after conducting consultation and anal-

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(30) See for example, D. DAYEN, "The 'Amazon Amendment' Would Effectively Hand Government Purchasing Power Over To Amazon", *The Intercept*, 2 November 2017, which notes: "experts believe only one or two companies would have the wherewithal to participate. That means monopoly or duopoly control of \$53 billion in federal purchasing".

(31) D. DAYEN, "Congress Prepares To Send Major Gift To Amazon While Trump Battles, Amazon Washington Post", *The Intercept*, 10 November 2017: "critics still see the program as tailor-made for Amazon to dominate. First of all, no online retailer has as large a footprint as Amazon, which is responsible for almost half of all e-commerce sales. Procurement officials are as likely to lean on Amazon as any other consumer, especially because of the array of third-party sellers supplying at least a semblance of competition in one site".

(32) R.K. TOMPKINS and R.M. PARRY, "National Defense Authorization Act for Fiscal Year 2018 Analysis: DoD 'Amazon' Bill Poised to Become Law", *Holland & Knight Government Contracts Blog*, 15 November 2017.

(33) Section 846 (c) (1), "National Defense Authorization Act for Fiscal Year 2018", *op. cit.*, p. 27.

(34) *Ibid.*, p. 33.

(35) *Ibid.*, p. 27.

ysis, including: market analysis and initial communications with potential commercial e-commerce portal providers; consulting affected departments and agencies about their unique procurement needs; assessment of the products or product categories that are suitable for purchase on the commercial e-commerce portals; a review of standard terms and conditions of commercial e-commerce portals in the context of Government requirements; an assessment of the precautions necessary to safeguard any information pertaining to the Federal Government, especially precautions necessary to protect against national security or cybersecurity threats; and an assessment of the impact on existing programs, including schedules, set-asides for small business concerns, and other preference programs.(36)

Phase III begins not later than two years after the date of the submission of the implementation plan and provides for the issuance of guidance to implement and govern the use of the program including protocols for oversight of procurement through the program, and compliance with laws pertaining to supplier and product screening requirements, data security, and data analytics.(37)

The legislation provides that a procurement through a commercial e-commerce portal used under the program established must not exceed the simplified acquisition threshold,(38) which was raised from \$150,000 to \$250,000 under the 2018 NDAA.(39)

While it does not specifically reference Amazon or any other vendor, the legislation expressly encourages the government to model the program after e-portals that are widely used in the private sector, in part so the government e-portal will have or can be configured to have features that facilitate the execution of program objectives, including features related to supplier and product selection that are frequently updated, an assortment of product and supplier reviews, invoicing payment, and customer service.(40)

Pursuant to the requirements for a Phase I implementation plan, GSA and OMB held a public meeting in January 2018 to solicit input from the public on development of the e-portal program. Key stakeholders from government, industry, the legal community and others attended the meeting and exchanged ideas on implementation of the plan.(41) The variety of positions from the various stakeholders suggests that as of mid-2018, much work needed to be done. A primary topic of discussion focused on questions regarding the

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(36) *Ibid.*, p. 35.

(37) *Ibid.*, p. 27.

(38) *Ibid.*

(39) *Ibid.*

(40) *Ibid.*

(41) A copy of the transcript of the 9 January 2018 public meeting: Procurement Through Commercial e-Commerce Portals, is available at: [www.interact.gsa.gov](http://www.interact.gsa.gov).

primary purpose of the Section 846. Although the statute calls for the creation of e-portals for purposes of “enhancing competition, expediting procurement, enabling market research, and ensuring reasonable pricing of commercial products,”(42) a number of participants suggested that the language of Section 846 created uncertainty and that GSA and OMB should make a clear statement as to the program’s primary goal. In addition, the discussion and comments made by participants focused on areas such as competition, both that the e-portal level and order level, and the nature and description of the e-portal:

“What does competition mean or pricing mean? Is it by the unit or total spend or what?

Is it a shopping mall? Or is it more interactive where government is seeking a quote based on dollar size of order?

We need to be clear about what we mean about e-commerce portals too. Do we mean e-procurement or e-auction or e-markets?”.(43)

Meeting participants also expressed concern regarding the issue of competition at the e-portal level and sought clarification on whether the government sought a single e-portal or multiple e-portals. A participant suggested that if competition is the government’s overarching goal, then multiple e-portals should be part of the effort.(44)

Another topic of discussion addressed the issue of the government’s interest in a streamlined process that moves more closely to a commercial purchasing experience. For example, Jonathan Aronie, a procurement lawyer experienced in commercial item contracting, recognized the general goal of moving DoD’s purchase of COTS items to more closely resemble commercial purchasing practices. However, Mr Aronie noted the challenge of leveraging “commercial buying practices to the maximum extent possible without abandoning the country’s other national priorities and the need to assure that taxpayer money is spent wisely and appropriately”.(45) Mr Aronie further observed that: “we need to remember that the federal government is not a commercial entity and should not be expected to adopt purely commercial buying practices”.(46) In contrast, representatives of e-portal providers such as Amazon highlighted the benefits of the services they could offer the government and their ability to create a more efficient buying process, using commercial terms and conditions.

(42) Section 846 (a), “National Defense Authorization Act for Fiscal Year 2018”, *op. cit.*, p. 27.

(43) J. MILLER, “What are the goals of OMB, GSA’s e-commerce portal? That is step 1 of phase 1”, *Federal News Radio*, 16 January 2018.

(44) *Ibid.*, p. 43.

(45) J. ARONIE, “Comments”, in U.S. General Services Administration, *Procurement Through Commercial e-Commerce Portals – Implementation Plan*, March 2018, pp. 21-24.

(46) *Ibid.*, p. 45, and pp. 22 and ff.

Thus, as with earlier procurement reforms, such as FASA and FARA, a key element of the debate over implementation of the e-portal program is how far should the government move to adopting commercial practices and removing traditional rules and oversight mechanisms in pursuit of greater efficiency and agency discretion. The e-portal debate is in many ways reminiscent of the prior procurement reforms, which many saw as an opportunity to make the government operate more like a business.(47)

The U.S. General Services Administration's Phase I implementation plan, issued on schedule in March 2018, identified three possible models for portal providers:

- **E-Commerce model**, where product vendors leverage an online platform to sell their own proprietary or wholesale products and the vendor is responsible for fulfillment of orders. There is limited competition under this model.
- **E-Marketplace Model**, where online marketplaces (such as Amazon) connect buyers with a portal provider's proprietary products, third party vendors, or both. This model offers increased competition given access to both proprietary and third-party products.
- **E-Procurement Model**, where e-procurement is a software-as-a-service model that is managed by the buying organization. The portal provider does not sell products in this model, rather contracted suppliers are responsible for fulfilling orders – many from outside marketplaces – which allows a larger supplier pool and horizontal price comparisons.(48)

In May 2019, GSA issued its report under Phase II, which announced GSA's preferred approach: the government will try e-marketplaces. During the next phase GSA will use a proof of concept for evaluating e-marketplaces before making any significant investments and before issuing any regulations.(49) Under the proof of concept plan, although Congress authorized use of the electronic platforms for purchases up to the 'simplified acquisition threshold' (generally \$250,000), GSA will limit users' purchases on the selected e-market places to the micro-purchase threshold (currently \$10,000) to promote the use of the program while mitigating risk.(50) GSA selected the e-marketplace model

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(47) S. Kelman, the Administrator of the Office of Federal Procurement Policy during the Clinton Administration who was a leader of the 1990s procurement reform effort, sought (1) a procurement system defined by greater purchaser discretion, (2) less encumbered by bureaucratic constraint, and (3) a system that was more businesslike. S.L. SCHOONER, "Fear of Oversight: The Fundamental Failure of Businesslike Government", 50 *Am. U. L. Rev.*, 2001, pp. 627, 636-637.

(48) U.S. General Services Administration, *Procurement Through Commercial E-Commerce Portals – Implementation Plan*, *op. cit.*, p. 6.

(49) U.S. General Services Administration, *Procurement Through Commercial E-Commerce Portals – Phase II Report: Market Research and Consultation*, April 2019, p. 3.

(50) *Ibid.*

for the proof of concept, noting that it will continue to assess opportunities to leverage the benefits of the other commercial e-commerce portal models.(51) GSA also recommended increasing the micro-purchase threshold from \$10,000 to \$25,000 for a five-year period to promote adoption of the e-commerce portals.(52) If the threshold is raised as recommended, federal officials – ordinary users – will be able to make purchases up to \$25,000 directly from any e-marketplaces that GSA has endorsed, and in return GSA will receive a small fee from the vendors that run the selected commercial e-marketplaces.

The collection and protection of data is an important issue to be addressed during implementation of the e-portal program. The Phase II report noted conflicting concerns regarding the collection and use of data created under the e-portal program. The e-portal legislation includes restrictions on e-portal provider use of Government-owned data for pricing, marketing, competitive, or other purposes. However, e-portal providers offering the e-marketplace model argue that the data protections will make it difficult to provide appropriate supplier screening, customer service, and warranty work, while the supplier community fears that the e-marketplace model portal providers could use data regarding Government purchases to gain an unfair competitive advantage.(53)

A primary concern of suppliers regarding potential data misuse involves product ‘white labeling’, when an e-portal provider uses supplier sales data to enter the market with its own version of the supplier’s product, often at a lower price point. The supplier community expressed concern that GSA will be unable to determine whether an e-marketplace model portal provider will have used Government data to displace a supplier’s product.(54) As a result, suppliers seek additional data protection, while e-portal providers argue that without access to purchase data they “could not operate their marketplaces effectively or in the best interest of the Government”.(55) GSA anticipates that limiting the proof of concept to purchases below the micro-purchase threshold will decrease the unintended consequences related to data use and enable GSA to make course corrections and adapt to commercial practices.(56)

In addition to addressing the access and use of data during the next phase of the e-portal implementation, GSA will have an opportunity to assess other key issues raised by this new procurement strategy, including: transparency

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(51) *Ibid.*

(52) Note that the Section 809 *Panel Report* (Vol. III) recommended a much more liberal approach to purchasing “readily available” items in the market, which could in effect increase the simplified acquisition threshold to \$15 million.

(53) U.S. General Services Administration, *Procurement Through Commercial E-Commerce Portals – Phase II Report: Market Research and Consultation*, *op. cit.*, p. 5.

(54) *Ibid.*, p. 6.

(55) *Ibid.*

(56) *Ibid.*

(will it be possible to track purchases made by Government users across a private e-marketplace?), bid challenges (discussed further below), competition (although Congress has said purchases under this initiative meet the Competition in Contracting Act's requirement for 'full and open' competition, will ordering online in a commercial e-marketplace provide true competition?), socioeconomic goals (will small and disadvantaged businesses be drowned out by the din of a commercial e-marketplace?), and compliance with international trade laws (how will vendors challenge discriminatory solicitations if there are no solicitations in an e-marketplace?).

Therefore, as the federal government proceeds through the three phases of the e-portal program, key issues to address include: the overall goal(s) of the program; the nature of competition, at both the e-portal and order levels; and the extent to which the government pursues a commercial buying experience, including as provided in Phase III, any exemptions from existing procurement laws.

## ***6. Streamlined Procurements – Lessons Learned***

Establishing well-defined goals for the e-portal program should assist the government in determining appropriate competition requirements, as well as a suitable regulatory regime. Once such goals are established, past efforts in procurement streamlining offer important lessons on how the government can address the above issues in implementing the e-portal program. As discussed previously, the acquisition reforms of the 1990s and related efficiency efforts provide a cautionary tale of potential pitfalls in the effort to simply the acquisition process.

### **6.1. Purchase cards**

As discussed earlier, the government's expansion of the purchase card program, which like the e-portal program, provides a simplified process for commercial item purchases, was plagued by inefficiencies, as well as fraud, waste and abuse.<sup>(57)</sup> The purchase card program was improved by applying fundamental tools of oversight, such as controls and the monitoring of transaction activity to minimize fraudulent, improper, and abusive purchase card transactions.<sup>(58)</sup>

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<sup>(57)</sup> Government Accountability Office, "Purchase Cards: Increased Management Oversight and Control Could Save Hundreds of Millions of Dollars", *op. cit.*, p. 11.

<sup>(58)</sup> Government Accountability Office, "Government Purchase Cards: Little Evidence of Fraud Found in Small Purchases, but Documentation Issues Exist", *op. cit.*, p. 13.

Problems with purchase cards were also experienced by the Department of Homeland Security (DHS),(59) which was given certain exemptions from competition requirements in the wake of the terrorist attacks in September 2001 in support of its mission to secure the homeland and protect it against conventional and unconventional attacks in the U.S. While this special authority was intended to enable DHS to more effectively meet its mission, it led to widespread fraud, waste and abuse.(60) With regard to the DHS purchase card program, GAO found that a weak control environment and breakdowns in key controls exposed DHS to fraud and abuse in its use of the purchase cards.(61) GAO found that DHS cardholders failed to follow the same procedures and that inadequate staffing, insufficient training, and ineffective monitoring also contributed to the weak control environment.(62) The lack of proper training and oversight led to questionable purchases, such as an \$8,000 Samsung 63-inch plasma screen television acquired at the end of the fiscal year.(63) GAO noted that the large-screen television sat unused and in its original packaging 6 months after it was purchased.(64)

Shortcomings in the DHS purchase card program were also highlighted in the agency's procurement activity in response to Hurricane Katrina in 2005. DHS made thousands of purchase card transactions to buy goods and services for hurricane rescue and relief operations.(65) For Katrina-related procurements, Congress authorized DHS an increase to the micro-purchase threshold from \$2,500 to \$250,000,(66) which is the same threshold that potentially could be applied to the current e-portal program. Due to the issues noted above, GAO found problematic purchasing activity including an instance where DHS paid double the retail price for 20 flat-bottom boats.(67) In another instance, weaknesses in DHS's inventory control and procurement practices led to over 100 laptops being lost or misappropriated when shipped to New Orleans as part of the relief efforts.(68)

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(59) DHS was established under the Homeland Security Act of 2002, *Pub. L.*, No. 107-296.

(60) *See*, for example, House Committee on Government Reform, 109<sup>th</sup> Congress, "Waste, Abuse and Mismanagement in Department of Homeland Security Contracts", 2006, i, 3.

(61) Government Accountability Office, "Purchase Cards, Control Weaknesses Leave DHS Highly Vulnerable to Fraudulent, Improper and Abusive Activity", GAO-06-957T, 19 July 2006.

(62) *Ibid.*, p. 53. In addition, GAO and the DHS Office of Inspector General estimated that 45% of DHS's purchase card transactions were not properly authorized, 63% did not have evidence that the goods or services were received, and 53% did not give priority to designated sources, *ibid.*

(63) Government Accountability Office, "Purchase Cards, Control Weaknesses Leave DHS Highly Vulnerable to Fraudulent, Improper and Abusive Activity", *op. cit.*, pp. 53, 5 and ff.

(64) *Ibid.*, p. 54.

(65) *Ibid.*, pp. 53, 1 and ff.

(66) *Ibid.*, p. 56.

(67) *Ibid.*, pp. 53, 5 and ff.

(68) *Ibid.*, p. 58.

GAO concluded that DHS: failed to commit sufficient resources to its purchase card program, including insufficient staffing to effectively manage and oversee the purchase card program; failed to ensure that cardholders received adequate training; and failed to provide sufficient monitoring and oversight, including the use of post-payment audits to monitor and oversee cardholder's compliance with agency-wide and government-wide purchase card policies.(69) GAO recommended action to improve the processes and internal controls to maximize the value and benefit of the purchase card and minimize the potential for fraud, waste, and abuse.(70)

The government-wide and DHS purchase card programs, like the e-portal program, place an emphasis on an efficient process for the purchase of commercial items. The experiences with the purchase card programs reinforce that such streamlined procedures, without adequate safeguards, are subject to mismanagement and inefficiencies. As the government develops the e-portal program, it should keep in mind that oversight mechanisms such as those discussed above are key to a successful streamlined process for commercial item purchases, which can enhance both the integrity as well as the efficiency of the system.

## 6.2. Framework agreements

The government's expanded use of framework agreements or indefinite-delivery/indefinite-quantity (IDIQ) contracts,(71) as part of the 1990s procurement reforms, also offers insights into issues that can arise when promoting streamlined acquisition methodologies. In the US, as elsewhere, framework agreements have been viewed as a critical tool to enhance the efficiency of the acquisition process.(72) However, the increasing popularity of framework agreements in the post-reform era led to concerns regarding reduced levels of competition and a lack of transparency.(73) In addition, while framework agreements are preferred for their perceived efficiencies and flexibility, some argued that they were in fact used to avoid regulations associated with traditional methods, rather than as a means of efficiency.(74) To address these concerns,

(69) *Ibid.*, pp. 53, 7-11 and ff.

(70) *Ibid.*, pp. 53, 30 and ff.

(71) In the U.S. federal procurement system, framework agreements are generally known as indefinite delivery indefinite quantity (IDIQ) contracts. See FAR Subpart 16.5.

(72) See G.L.ALBANO and C.NICHOLAS, *The Law And Economics Of Framework Agreements*, Cambridge, CUP, 2016, p. 4, where the authors note that "framework agreements are considered to have the potential to 'increase dramatically the freedom [given to] public officials to use their judgment in the procurement process' to enhance value-for-money outcomes, as then head of the United States (U.S.) Office of Federal Procurement Policy urged the procurement community to adopt back in 1990".

(73) See, for example, Government Accountability Office, "Contract Management: Few Competing Proposals for Large DOD Information Technology Orders", GAO/NSIAD-00-56, 20 March 2000.

(74) C.R. YUKINS, "Are IDIQ Inefficient: Sharing Lessons With European Framework Contracting", *Pub. Cont. L.J.*, 2008, p. 545.

adjustments were made through laws and regulations that restored certain transparency, oversight and competition features of traditional procurements to the ordering process under IDIQ contracts.(75)

### 6.3. Bid protests

Another oversight mechanism that could be impacted by the use of the e-portals is the bid protest. Bid protests have served as a fundamental element of transparency and oversight for the U.S. federal procurement system for decades. However, as currently proposed, direct ordering under the e-portal process has the potential to permit federal purchasers to bypass the normal pre-award publication on which most pre-award protests are based.(76) Reducing the ability to challenge awards under the e-portal system undermines a critical oversight tool to promote fairness in the award process and reduce the potential for corruption.(77) In addition, as others have noted, direct ordering under the e-portal system may run counter to a number of international trade agreements, such as the Agreement on Government Procurement, to which the U.S. is a party. These agreements generally allow vendors to protest certain ‘covered’ procurements.(78) Creating an ordering system that bypasses the protest process adversely impacts the U.S. commitment to such agreements and opens the door for others – the United States’ trading partners – potentially to do the same.(79)

## 7. Conclusion

As discussed, the work of the Section 809 Panel and the legislation to establish the e-portal program are part of the current initiative to address perceived shortcomings in prior efforts to create a simplified commercial item purchasing process for U.S. federal agencies. As GSA proceeds with its e-portal implementation plan there is the sense of a new beginning in commercial item purchasing. After many years of failure in hosting its own online catalog, GSA

(75) See, for example, the “National Defense Authorization Act for Fiscal Year 2002”, section 803, Competition Requirements, providing that all DOD purchases of services over \$100,000 under multiple award contracts be made on a ‘competitive basis’, in *Pub. L.*, No. 107, § 803 (b)(1), (c)(2); “National Defense Authorization Act for Fiscal Year 2008”, section 843, Enhanced Competition Requirements for Task and Delivery Order Contracts, providing for i) protests of task and delivery orders exceeding \$10 million; ii) enhanced competition requirements for task and delivery orders exceeding \$5 million; and iii) prohibition against single award task or delivery order contract valued at over \$100 million unless approved by agency head, in *Pub. L.*, Nos 110-181, § 843.

(76) See C. YUKINS and D. DAMISH, “Section 809 and ‘E-Portal’ Proposals, by Cutting Bid Protests in Federal Procurement, Could Breach International Agreements and Raise New Risks of Corruption”, *The Government Contractor*, 2 May 2018, Vol. 60, No. 17.

(77) *Ibid.*, p. 67.

(78) *Ibid.*

(79) *Ibid.*

is – at Congress’ insistence – turning to embrace commercial online marketplaces. This new approach, though it will launch on only a small pilot, opens the door to a very different federal marketplace for small-value purchases, one in which users (who are likely to focus more on quality, and less on price) can guide purchasing. At least initially, this may prove to be a small-value marketplace with few real regulatory constraints. This may well transform this corner of the federal market. However, as discussed above, part of the reason prior efforts fell short is that the removal of traditional oversight mechanisms often resulted in the misuse of these simplified procedures. As also noted, these oversight mechanisms are necessary, not only to prevent abuse, but also to promote the efficiency that is sought by simplified procedures. The U.S. federal government’s ongoing effort to create a less complex purchasing process for commercial items reinforces the need for robust oversight and compliance mechanisms. Given these challenges, Congress wisely provided for a three-phase implementation plan for the e-portal program. Thus, the government has an opportunity to test and refine its approach for the program. Nevertheless, given the dynamics of the current commercial e-portal market and the prospect of dominance by a single provider such as Amazon, the challenges are significant. While the e-portal program seeks to move more closely to a purely commercial buying experience for the federal government, past experience suggests that traditional (if cumbersome) protections guaranteeing competition, transparency, accountability and oversight may be necessary to ensure the effectiveness, efficiency and integrity of the program.



**CHAPTER 15**  
**Preliminary Market Consultations**  
**in Innovative Procurement:**  
**A Principled Approach and Incentives**  
**for Anticompetitive Behaviors**

BY

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***1. Fundamentals***

**1.1. Introduction**

A preliminary market consultation (PMC), whether understood as an institution or as a process, is bound up with the development of a future tender. In European Union Law, the procurement threshold in any national law that implements the Directives on public procurement determines if the tenders are covered by the provisions of the said Directives. Nevertheless, there is a unanimous doctrine from the European Court of Justice (ECJ) which holds that every procedure must respect a well-known collection of principles, which act both as inspiration and boundaries. These principles encircle the whole fabric of public procurement. So, they must spread to the other figures that play a role in the development of a tender or in the implementation of a contract, either as a preparatory or an ancillary principle. This is the only way for a procurement to follow a straight line without bringing from the past the seeds for a future nullification.

Directive 2014/24 on public procurement devotes Article 40 to PMC.<sup>(1)</sup> It lodges a minute regulation, which barely picks the essence of the figure. Despite its paucity, the article cites three mandatory principles in designing and implementing any PMC: the principles of non-discrimination, transparency and competition.

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(1) Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC (referred to as 'PPD'), available at [eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0024&from=EN](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0024&from=EN), p. 120. A prior version of this piece was published through the *Ius Publicum Network Review* ([www.ius-publicum.com](http://www.ius-publicum.com)), issue 2, 2017.

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This chapter holds that the dimension of these principles in PMCs differ from their scope in the contracting procedures. The difference comes from the three features of PMC: it is a pre-procedural, not-compulsory, and not-decision-making stage. These attributes justify leaving their over-the-minimum application in the hands of any specific contracting authority. With this insurmountable limit, the contracting authority has a free hand<sup>(2)</sup> to make a general call for advice or restrict the query to a limited number of entities. It is entitled to either summon or to miss the market operators. Lastly, they are to decide the extension for the consulted people of the duty to provide information, the level of confidentiality and the degree of transparency.

## 1.2. Concept

The concept of preliminary market consultations (PMC) roughly encompasses a multi-faceted query whereby a contracting authority asks for experts and market operators to offer their contribution in order to make up the object of the contract and to define the other features of the procedure.

To launch a PMC prior to procurement procedures is a rational decision by any contracting entity, which looks for external advice to improve the terms of selection processes.<sup>(3)</sup> PMC is neither a newborn idea, nor an ignored technique before the EU regulated it in the latest Directives on public procurement. Contracting authorities often consult experts to help them in the preparation of tenders, especially in contractual activities for either new technologies, or even those activities which are hard to define. The contracting authorities and the third-party experts may share information even through the use of informal means such as personal or telephone chats or e-mail exchanges ('pre-procedural contacts').

Pre-procedural PMC are never restricted to any particular typology of contract. No classical category demands *per se* further support from the others. The rule for a typical public contract is to use the contracting unit's previous knowledge and experience as the basis for the preparation of any tender. This factor and the singularity of each procedure are the conditions which make a PMC necessary, convenient or optional. Since every rule has its exception, the service contracts that are linked to an innovative procurement (*i.e.* pre-commercial procurement and the association for innovation) deserve a different treatment. These types of contracts are the most obvious examples of a PMC-bound procurement procedure. It looks inconceivable to start an innovative

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(2) See also O. VODA and C. JOBSE, "Rules and Boundaries Surrounding Market Consultations in Innovation Procurement: Understanding and Addressing the Legal Risks", *EPPPLR*, 2016, p. 179.

(3) Editors' note: On Preliminary Market Consultation, see also the chapter of J.M. GIMENO FELIU in this book. For a discussion of similar preliminary market consultations in U.S. government procurement, see Federal Acquisition Regulation (FAR) 15.201, 48 Code of Federal Regulations, § 15.201.

tender without conducting a previous query (especially for a pre-commercial procedure). Summarizing, the more complex or innovative the procurement, the higher is the demand for better expert advice.

Public procurement of innovation requires technical experts and specific markets which the public buyer may not (in many cases) get from *in-house* experts and available information. The preliminary market consultations play the role of (an effective) instrument for the preparation of innovative procedures where the contracting authority lacks the needed experience or specific expertise in the subject matter of the contract. Thus, PMC is an essential action for a public procurement of innovation to succeed given the complexity of the archetypical contracts. Some of the products may require a complete innovative solution, which triggers an articulation of a technical dialogue between the public buyers and the companies before the publication of a tender. In the field of high technology, buyers may (roughly) know their needs but not the best technical solution to address such needs. As a result, the buyer and the would-be suppliers cooperate in a discussion and/or a technical dialogue that will sort out any possible issues on the contract. This enhanced debate enriches the first phase before the start of contract awarding (*i.e.*, definition of ideas) with high respect for the principle of equal treatment and without restricting competition.<sup>(4)</sup>

However, there are instances wherein the decision of the buyer to limit the use of the PMC to the pre-procedural phase may not be the best practice in innovative procurement. Neither the Directive nor the three studied transposition laws prohibit a public purchaser to start or resume a market consultation during the tender. These laws consider market consultation as one of the tools that the buyer may use within the tender. Nevertheless, a procedural PMC must be developed with considerable care for the principles of transparency and competition. A PMC that is developed during a tender is already a part of the competitive process; hence, it must abide by its seminal rules. The tender ends with a sole winner and multiple losers. The ultimate goal of conducting a consultation during this phase is to help the contracting authority to award the contract; hence, it must adhere to the same principles (*i.e.* transparency and competition) and to the same degree of rigour that is used in the entire procurement process.

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(4) X. GALICIA, “Guía de buenas prácticas para favorecer la contratación pública de innovación en Galicia” (Guide to good practices to promote public procurement of innovation in Galicia), 2015.

### 1.3. Primary and secondary goals of PMC. Expansion of the figure

The main goal for a contracting authority to start a – complex and laborious – PMC is to request information and guidance on the process for a successful contracting procedure. Innovative procurement has driven the PMC beyond its traditional framework. As a new category of public contracts, it has raised a sole issue arising from the ‘fear of the new’ and the stress to update the contract to adopt the latest state-of-the-art technology. In principle, contracting authorities resort to the use of PMCs either because of their inability to describe the contract object, or in order to identify the best selection criteria or the ablest technical solutions. PMC is also often used to assist the contracting bodies to accurately define the public needs that they are bound to satisfy.

The expansive role of PMC achieves its apex when a public purchaser blindly, without prejudice, asks for advice about the ‘what’ (*i.e.*, what its needs are – necessities) and the ‘how’ (*i.e.*, how to meet these needs – ‘procedure’). Generally speaking, the completion of a successful consultation enlightens a contracting authority to come to all kind of conclusions. So, the lack of a feasible solution may drive it to believe that it is inadvisable to launch a contracting procedure. If the discussions in the PMC indicate that there are already workable solutions in the market, the best choice is to opt for the ‘traditional’ types of public contracts. In cases, however, where the necessary technology is not yet available in the market, but it can be made with minimal adaptations and developments, the most feasible alternative for procurement is through the innovation partnership. If it is necessary to develop a new technology, which is non-existent currently and will provide the new solutions or improvements, the preferred procurement choice should be the pre-commercial procurement. Prescinding thereof, it follows that a market consultation is carried out regardless of the type of procurement procedure.

Other secondary goals are also present in PMCs. They are natural outcomes linked to innovative procurement, *i.e.* favouring permanent contacts between innovative firms and contracting bodies. Ongoing interaction between them will not only improve the implementation of the contract but will also strengthen new industrial and commercial sectors. The sheer fact of being consulted in a PMC may easily stimulate experts and firms to channel their financial and labour resources towards the development of new or innovative products. Indeed, innovation is useful not only to the public entities, but also to the industry because it may lead the firms to a new line of market business. Lastly, the PMC and innovative procurement foster technological, logistical

and managerial development, which by themselves make a relevant economic contribution to society.

## 2. Regulation

### 2.1. Precedents

Although the provisions on PMCs are considered as one of the main innovations in the Directive 2014/24 of the European Parliament and of the Council, of 26 February 2014, on public procurement and Directive 2004/18/EC, on the preparation of public contracts, ‘preliminary market consultations’ is not a new concept either in EU public procurement or in national legislations.

Prior to PMC, Community law recognized the importance of preliminary consultation through what was called a ‘technical dialogue’. Recital 8 of Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works, supply and service contracts provided that “before launching a procedure for the award of a contract, contracting authorities may, using a technical dialogue, seek or accept advice which may be used in the preparation of the specifications provided, however, that such advice does not have the effect of precluding competition”.<sup>(5)</sup>

The European Commission recommended the use of technical dialogue even before the recognition of PMC in the EU Directive. In its Communication of 27 November 1996, the Commission advised the use of technical dialogue between contracting authorities and private companies in complex projects, more particularly those projects which required novel solutions. The Communication of 11 March 1998 emphasized the meaning of technical dialogue as a procedure whereby a contracting authority initiates technical discussions with potential suppliers at the stage of the definition of requirements but before the start of the procurement procedure.<sup>(6)</sup> Technical dialogue must adhere to the principle of equal treatment, and it cannot restrict competition (pt 10 of the Communication).<sup>(7)</sup>

Although these regulatory precedents on the basic conditions for the efficient use of ‘technical dialogue’ existed in the European context, the application of this instrument was rarely used by EU Member States (*i.e.* in Spain, it was not introduced by any law).

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(5) Dir. 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.

(6) EU Comm., “Communication to the Council and the European Parliament on Public Procurement in the European Union”, 2 November 1998, COM(98)0143.

(7) *Ibid.*, p. 5.

## 2.2. Directive 2014/24, on public procurement

Article 40 of EU Directive 2014/24 sets out a minimum regulation of PMC, specifically:

*“Before launching a procurement procedure, contracting authorities may conduct market consultations with a view to preparing the procurement and informing economic operators of their procurement plans and requirements.*

*For this purpose, contracting authorities may for example seek or accept advice from independent experts or authorities or from market participants. That advice may be used in the planning and conduct of the procurement procedure, provided that such advice does not have the effect of distorting competition and does not result in a violation of the principles of non-discrimination and transparency”.*(8)

Article 40 stresses the several features of public market consultations. It limits the use of PMC to the preparatory phase, and, as such, it can only be managed before launching the procedure. However, the article does not prohibit a contracting authority from conducting a query during the development of the tender. In this case, the consultation is no longer a ‘preliminary’ procedure but a built-in procedure. As such, the public procurement principles are fully-operational.

Article 40 also does not impose a duty to adopt a PMC before starting any tender. The Directive considers PMC as an optional tool. All the decisions (e.g. PMC design, start, and management) are left at the discretion of the contracting unit.

PMC has a twofold function: (a) preparatory of the procedure, and (b) informative to possible bidders. A public purchaser may use a PMC as a preliminary query with an intent to provide workable information on multiple topics in a procurement. In doing so, it must decide the extent of the PMC. The experts, independent authorities, and market operators are allowed to comment on topics such as the necessity of the procurement, the most appropriate procedure, and the selection criteria. Their participation varies depending on the previous knowledge of the public purchaser and the singularity of the contract. For the third category of advisors (market operators), taking part in a PMC is presumably of the utmost importance since they are the possible bidders in the subsequent tender. In fact, their two-staged participation can be an issue in the correct implementation of the non-discrimination and competition principles in the procurement. Article 41 of Directive 2014/24 deals with the twofold nature of the competing firms in the PMC and in the ultimate tender.

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(8) Dir. 2014/24/EU, aforesaid, 1 (emphasis added), pp. 120 and ff.

The list of possible advisors, *i.e.*, independent authorities, experts and market operators, in Article 40 of Directive 2014/14 are not restrictive; hence, it does not limit other types of entities from participating in the query.

Further, the Directives allow the national transposition laws to decide on the definition, extension and boundaries of PMCs. The only limitation on the provisions for the use of PMC in national legislations, aside from its general role, is the adherence to the procurement principles on competition, non-discrimination and transparency (e.g., the stretched Spanish Draft).

The other advisors cited in Article 40 are the economic operators in the market which is the subject of the public procurement, who include those who may easily present a bid to the tender. They consider a PMC as important because it may work as a catalyst for the participants (more particularly the market operators) to agree or coordinate their responses to the query. Some may take advantage of this behavior for the purpose of rigging the tender; others may, however, do otherwise. In fact, the ablest of the consulted market operators may even influence the contracting authority to design the tender in their favour with an objective of making it easier for them to compete for the contract.<sup>(9)</sup>

### 2.3. Transposition to national laws

National transposition laws have adopted the features set out in Directive 2014/24 for PMC, with additional elements. Spain, United Kingdom and France have obviously met the requirements imposed by the Directive. But only the first country has added more substantial provisions. The other two did nothing but reproduce Article 40.

#### 2.3.1. Spain

The Public Sector Contracts Law (PSCL) devotes Article 115 to preliminary market consultations. The precept seeks to transpose Article 40 of the Directive. Because it regulates a pre-procedural phase, the first article in the section is devoted to “the preparation of public administration contracts”. Article 115 states that contracting authorities may carry out market research, consult the active economic operators in the market in the preparation of the invitation to tender, and inform the concerned economic operators of the plans and the requirements for the submission of bid. Contracting authorities may rely on the advice

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(9) A. SEMPLE, “Socially Responsible Public Procurement (SRPP) under EU Law and International Agreements”, *EPPPLR*, 2017, p. 293. Unlike the 2014 EU Directives, Art. X (5) of the WTO Government Procurement Agreement and Art. 19(19)(5) of the Comprehensive Economic Trade Agreement (CETA) between Canada and the EU prohibit accepting vendor advice on a prospective solicitation if this precludes competition. Editors’ note: the U.S. Government regulates these types of potential “organizational conflicts of interest” under FAR Subpart 9.5.

of third parties, who may be experts or independent authorities, professional associations, sectoral representatives, or even, exceptionally, the active economic operators in the market. The proceedings (*i.e.*, actions and decisions during the preliminary market consultations), as far as possible, shall be published online to make them accessible to all potential stakeholders who are interested in participating in the consultations and make the necessary contributions.

The contracting authority may use the advice extended by experts during the preliminary market consultation either in planning the tender procedure or during the procedure, provided that this will not result in distorting competition or violating the principles of non-discrimination and transparency.

Consultations cannot justify the design of so specific a contractual object that only one of the consulted experts may meet the technical characteristics. The studies and advice should provide generic characteristics, general requirements or abstract formulas that ensure a better satisfaction of public interests, provided that in contract award, no consultations will give an undue advantage to the companies that participated in the contracts.

Article 115 requires the contracting authority to record in a report all its actions in carrying out the consultations. The report will include, among other things, the studies that are carried out and their authors, the entities that are consulted, and the questions that are raised, including the answers to them. The report will be part of the recruitment file. In no case during the consultation process is the public purchaser allowed to disclose to the participants the solutions proposed by the other participants. The public purchaser should have the sole access to these solutions. It will weigh each one, and when appropriate, use these solutions in preparing the bidding process.

### 2.3.2. United Kingdom

The Public Contracts Regulation 2015 devotes Article 40 to PMC by copying *in toto* the provision of Article 40 in the Directive 2014/24.(10)

### 2.3.3. France

Article 4 of Decree No. 2016-360 of 25 March 2016 on public procurement does not add anything remarkable to Article 40 of Directive. In fact, it states that:

“In order to prepare for the award of a public contract, the buyer may consult or carry out market studies, solicit opinions or inform economic operators of his project and requirements.

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(10) Statutory Instruments 2015, No. 102, “Public Procurement, Public Contracts Regulation 2015”, 5 September 2015, available at [www.legislation.gov.uk/ukSI/2015/102/pdfs/ukSI\\_20150102\\_en.pdf](http://www.legislation.gov.uk/ukSI/2015/102/pdfs/ukSI_20150102_en.pdf), p. 44.

The results of these studies and preliminary exchanges may be used by the buyer, provided that they do not distort competition and do not lead to a violation of the principles of freedom of access to public procurement, equal treatment of candidates and transparency of procedures”.

#### 2.4. Full regulation may not be the best option

The acknowledged importance of PMC for the design and success of innovative procurement procedures does not justify submitting it to the statutory rules of the EU Commission or the national authorities. On the contrary, a rigid code may cause a failure of this tool since (first) developing a market consultation is not compulsory but a faculty for the contracting authorities. Therefore, (second) each PMC should be tailored to the needs of the procurement case.

The above reasons do not mean that PMC must be inordinate and ‘anarchic.’ On the contrary, no contracting body should proceed with a market consultation without a sound and well-established ‘table of contents’, complete enough to guide the participants. There are two sets of rules that are suitable as a basis for consultations: (a) ‘soft law’ from public authorities, and (b) self-regulation from the concerned contracting authority.

The EU and the national authorities can provide recommendations to the contracting entities which engage in innovative procurement. The soft law on PMC may take the form of guidelines and offer two types of content: a code of good practices, and a list of malpractices. The effectiveness of soft law depends to a large extent on the authorities’ ability to lay out a workable and versatile scheme based on successful cases of innovative procurement. There are two other factors that are essential for the guidelines to be useful: (a) dissemination (Web pages etc.), and (b) quick adaptation to changes in innovative procurement.

Any contracting authority may (and must) set an array of requirements to rule on PMCs (or the ‘hard law’), which requires strict compliance by those who are consulted. Mainly, the requirements should rein in the operators that are interested in taking part in innovative procurement. Since they are actual rivals in the market and would-be bidders in future tenders, the rules must ensure that their advice is autonomous, and will not coalesce into future collusive bids.

### ***3. Some Features of the Public Market Consultation***

#### **3.1. The PMC as a process**

Even though it is not the core of this study, it is advisable to sketch several elements of the PMC taken as a process. In that conception, a regular PMC follows the next three steps:(11)

1. Decide the scope of consultation (*Decide what information needs to be gathered and shared, and which market players to target*): 1) The initial research and needs assessment should identify the area(s) of focus and the specific user needs, as well as the potential innovations to meet them. 2) Further information may be needed to develop a specification and choose an appropriate procurement procedure. 3) Analyse the market to determine which tiers to target (e.g. manufacturers, service providers, subcontractors, systems integrators, researchers and third sector etc.).

2. Choose a format and plan (*Choose the best format for the consultation and prepare the resources and people involved*): 1) Determine the best way to engage the identified suppliers / stakeholders. 2) Consider using a questionnaire or survey, written submissions, face-to-face, phone or web-based meetings, open days and supplier demonstrations. 3) Be clear on the timelines and resources needed to make it work. 4) Prepare the documents to be circulated as part of the consultation, e.g. a 'prospectus'.

3. Consult and capture information (*Conduct the consultation, keep a good record, and ensure an equal treatment*): 1) Publish a *Prior Information Notice* (PIN), publicise the consultation on relevant industry or other websites, and notify the suppliers directly wherever possible. 2) Keep records of all contacts and be prepared to follow up with respondents. 3) Prepare a summary of the findings and implications for procurement. Be sensitive towards the confidentiality of any information provided by respondents.

Before launching a procurement process, consider the measures to be taken to avoid any distortion of competition arising from the undertakings made by those who have been involved in preliminary market consultation. For example, the same information should be shared with other operators, and there should be an adequate time for the preparation of tenders. The exclusion of those who are involved in the consultation can only be done if there is no other means to ensure equal treatment to all the operators in the process, and

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(11) "Guidance for public authorities on Public Procurement of Innovation, Procurement of Innovation Platform", available at [www.innovation-procurement.org](http://www.innovation-procurement.org), p. 19.

the operators who are involved must be given a chance to disprove any claim of unequal treatment.

### 3.2. Formats

Consultations may comprise a plurality of methodologies, which may be used cumulatively or alternatively. They consist of: ‘Meet-the-Market event’ (MTM), market surveys, industrial fairs (which do not require any kind of organizational effort on the part of the purchasing entity), open days, publication of annual public procurement plans in official or/and commercial journals and on Internet (this option is very attractive because it does not involve a great organizational effort or an added cost), the provision of information directly through governmental websites (Public Procurement Platforms, or even if the information becomes fragmented and makes transparency difficult, the contracting authority’s Profile), webinars, electronic platforms etc.

A PMC can also be carried out through other means, such as commissioning analyses or reports on the experiences of other countries, developing documents, consulting experts and scientists, or promoting discussion of public bodies with potential contractors. In addition to the consultations with potential participants, public purchasers can prepare tenders through consultations aimed at research staff, scientists, professional associations, specialized public authorities, and centers of knowledge. In general, queries should spread to any person or institution that enables the contracting authorities to gain a better knowledge of the market where the contract is to be developed, provided that such actions do not distort competition and do not give rise to violations of the principles of non-discrimination and transparency.

### 3.3. Advisor

The approach to this topic in Article 40 of Directive 2014/24 and in the three national implementations seen above can be summarized in two assertions: the specific mention of three categories of subjects, and the list is not *numerus clausus*.

There are three types of interlocutors: (a) experts, (b) independent authorities, and (c) market participants. As regards the experts, their independence vis-à-vis the economic operators competing in the market appears as an insurmountable precondition. Only those persons who do not belong or are not related to the would-be bidders in the future tender should be entitled to sign their contributions as ‘experts’. The ones linked to the bidders will take part in the query as staff or representatives of the market participants. They can be consulted as well; but the query is subjected to all the obvious connotations of the third category (market operators).

The word ‘independent authorities’ refers to public institutions that are able to give support to the innovative contracting bodies. Article 40 does require them to be independent because, by definition, laws ensure the independence of every public institution. The most evident public authorities are the other innovative contracting entities that have successfully dealt with (similar) innovative procedures. Other institutions, *i.e.*, regulatory agencies, scientific institutions, and even Ministries, may also be admitted as “independent authorities.”

‘Market participants’ are the third category of advisors. The concept has several meanings, depending on the understanding of the word ‘market’. If it refers to any economic activity, then any firm may be consulted, but it does not seem to support the intended meaning for market participants in the Directive. It is more appropriate to narrow the concept in favour of the firms that are competing in a market for the subsequent innovative tender. Preferably, it must be the same one. However, this restricted option assumes that the public purchaser has a good knowledge of the market. The real situation may easily be the opposite. For instance, in the purest pre-commercial procedures, the public purchaser may know that an outreach to the market is useless because it knows what it lacks, and what its necessities are. Perhaps it even has a good idea on how to meet them. Nevertheless, it may still ignore the technological, managerial or industrial information available on how to make the idea become real. In these cases, the contracting authorities will publish a loose market definition as result of the consultation; that is, they may well make an overbroad call for advice.

Market operators participating in a PMC cannot be forbidden to submit their bids to the future tender. To avoid possible conflicts of interests or the infringement of the competition and non-discrimination principles, Article 41 of Directive sets two rules. First, the contracting authority cannot prohibit vendors from bidding in the tender on the sole basis of their role in the PMC. They must be given the chance to show that their previous advice does not put them unfairly on a better footing than the other bidders. Second, if the prior advice *does* lend a vendor an unfair advantage, the public purchaser must expel him from the tender. Article 41 will be discussed below.

Article 115 of the Spanish PSCL imposes two additional constraints on market participants. The first one is that the operators who are required to give advice must be “active” in the market. The reason for this precise requirement is based on the assumption that only those firms that are currently present in the concerned market are capable of providing workable suggestions. It does not, however, prevent the authority from appealing to former market operators as part of the group of experts.

The second restriction is more important. Article 115 states that market operators may be called on in ‘exceptional cases’. It appears to be a subsidiary solution when previous consultations with the experts and institutions have failed. This means that the contracting body can only call up the actual market operators when the consultations with the independent advisors have been made and they fail to deliver workable solutions. The Spanish legislator probably set this rule as a buttress against competition infringements during a PMC. However, it looks like an ‘Alice in Wonderland’ provision. In practice, innovative authorities appeal to market participants in PMCs as the only way to ensure the participation of workable bids in the subsequent tenders.

Although Article 40 of the Directive quotes an exemplary relationship of advisors (independent authorities, experts and market operators), it does not prohibit other types of persons or entities from participating in the query. For example, other contracting bodies, or operators that are no longer ‘active’ in the market at stake or are already trading in different markets may still be allowed to participate in the PMC.

#### ***4. Principles of Public Procurement in PMC: Non-discrimination, Transparency and Competition***

##### **4.1. Principle of non-discrimination**

For the *Guidance*, the application of the principle of non-discrimination is directly linked to the principle of competition. The new Directive states that a preliminary market consultation should not distort any later competition. By applying the same interpretative criteria that are pervasive for the procedural phase (the tender), that is, the above statement should be understood as imposing on the contracting authority the duty of requesting the participation in the PMC of as many experts, independent authorities and operators as possible. With this meaning, the Treaty principles of transparency and non-discrimination also apply to preliminary market consultations, together with the principle of publicity, and so will reach the high standard of universally accepted principles for public procurement.

Equal treatment and transparency are two facets of the principle of non-discrimination. Equal treatment requires that comparable situations are not treated differently, and that different situations are not treated similarly, unless such a difference or similarity in treatment can be justified objectively.<sup>(12)</sup>

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(12) See, e.g., ECJ, 1963, *Italy v Commission*, case C-13/63, *ECR*, p. 165, at par. III, (4)(a); ECJ, 1994, *SMW Winzersekt v Land Rheinland-Pfalz*, case C-306/93, *ECR*, p. I-5555, at par. 30.

A contracting authority must act fairly during the public procurement by ensuring that all competitors have an equal opportunity to compete for the contract. Transparency demands a transparent decision-making process to show that the purchaser is following the principle of equal treatment. Although the contracting authority remains free to define the subject of the contract in any way that meets the public's needs, including the technical specifications and the award criteria that promote horizontal policies, it must do so in a way that ensures transparency in awarding the contract.

In the European Union, the principle of non-discrimination prohibits all unreasonable discrimination based on nationality. No contracting entity may, for example, give preference to a local company simply because it is located in the municipality. Similarly, the principle of equal treatment requires that all suppliers be treated equally. All suppliers that are involved in a procurement procedure must, for example, be given the same information at the same time.

Taken literally, Article 40 of the Directive means that an innovative contracting authority will fulfil the principle of non-discrimination during the PMC if it imposes no unfair difference on the consulted firms based on their nationality. Moreover, the public purchaser must hand out to all the participants the information needed to submit a successful tender. It is, however, presumed that the principle of non-discrimination is satisfied when all of the participants in this phase belong to the same EU Member State. Since Article 40 does not impose the obligation to make an 'EU wide' invitation, then there is no discrimination when there is no foreign operator that is admitted to the PMC, provided, however, that the same-nation candidates are treated on equal terms. This circumstance, among others, explain the non-inclusion of the principle of publicity in Article 40.

Although the discussion in the preceding paragraphs appears straightforward and indisputable as a rule of three, its formal and nationwide interpretation of the non-discrimination principle is fallacious. Not only does it reduce the scope of collaborating firms and is contradictory with the sheer essence of innovative procurement (new ideas or technologies demand the best contributions), what is more significant is that it appears to suggest that the Directive exempts the seminal principle of publicity from a category of contracts, which negates the materialization of an internal market on public procurement.

A rational and imperative rule on this significant topic is hard to find due to the lack of an objective threshold. There is, however, a rule of thumb which addresses the publication requirement in two ways; that is, either use the procurement threshold in Article 4 of Directive 2014/24 or make the publication

in the *Official Journal of the European Union* a minimum requirement in every preliminary market consultation.

The first option applies accurately in the preliminary market consultations for innovation partnerships, since it is a type of procurement that is regulated in the Directive. In pre-commercial procurement (PCP), there is no workable quantitative threshold, thereby, making the second option more suitable. After all, in a sheer PCP a number of elements are ignored by the contracting authority. The definition of the idea, the solution, the prototype, and the costs of the project call for every feasible contribution. Since most of these cases are related to top-of-the-league technological sectors, it is inconceivable that the contracting authorities that are engaged in PCP will decide to restrict the international participation in PMCs. Since PCP is not regulated at an EU level, the Commission's soft law and the contracting authorities' own rules have the upper hand in choosing a solution.

Both rules of thumb admit a significant number of exceptions where the principles at stake only work in the abstract. The contracting body always has in its hands the power to make a universal call for advice, by publishing a notice in an official journal. But the concurrence of factors ('barriers') reduces the number of participants in the PMC. An exemplificative relation distinguishes among legal barriers, business barriers and geographical barriers.

The archetypical legal barrier for a general entry in the PMC is the ownership of IP rights. Where only one firm owns a patented product or technology lacking any alternative and, so, it is necessary for the innovative contract to be implemented, all the operators but the patent's holder have no role in the PMC. Of course, the innovative contract may have among its goals to find a substitute for the patented product. This is generally a difficult and long-lasting task. In many sectors, the presence of standard essential patents will make that goal a never-ending labyrinth. And even if it is found, the patent incumbent will possibly launch a patent war.

Business barriers relate to the corporate purpose, capacities, experience and other features which make the difference between capable or non-capable firms for the contract. The more innovative the procurement, probably the fewer the companies that will qualify for implementing it. Principles of non-discrimination, transparency and publicity are not infringed when contracting authorities restrict the calls and exclude those firms alien to the contract and incapable of delivering sensible recommendations. Last, geographic or territorial barriers may dissuade certain operators whose business is mostly focused far from the contracting authority's jurisdiction.

As said above, the presence of one or more of these barriers does not bar the contracting authority from looking for the widest participation in the PMC

(there is no barrier on the offer side since contracting authorities enjoy unilateral power over official journals). However, they reduce the number of *de facto* participants in the PMC, and also the probable number of feasible solutions and, in the end, the effectiveness of the contract.

Anyway, the principle of non-discrimination demands that where the contracting authority sets the requirements as a pre-condition to participate in a PMC, all the firms that fulfill them must be admitted. Those requirements must be suitable, proportionate and accept equivalent solutions to achieve the result that the innovation procurement pursues. The principle of suitability is not met where the participant does not ensure that the public purchaser will enjoy the untroubled use of the product or service of the contract.

#### 4.2. Principle of transparency

The principle of transparency is derived directly from the freedoms of establishment and the provision of services<sup>(13)</sup> and from the principles of equal treatment and non-discrimination between tenderers. These principles impose an obligation of transparency on the contracting body, which must guarantee – for the benefit of all potential tenderers – an adequate publicity to open the competition for the award of services, and to monitor the impartiality of the award procedures.

This principle is indisputable in European public procurement due to its role in the fight against corruption. A transparent procedure leaves little room for discretion to the contracting body; thus, it reduces the incentives to bribe the contracting body's members or to indulge in collusion. There are multiple manifestations of the principle of transparency in the contracting procedure, which can be summarized in a single maxim: the right of the interested parties (mainly, the bidders) to obtain certain, relevant, complete, and updated information about the different phases and elements of the procedure through a plurality of means (e.g., official bulletins, contractor profiles, contracting platforms).

However, the excess of transparency will allow each tenderer to monitor the behavior of its competitors. In cases of collusion, this would discourage alleged cartel owners from bidding against the agreement for fear of retaliation. If excessive opacity favours corruption, excessive transparency paves the way for collusion. Where contracting procedures are repeated and foreseeable, as well as for homogenous and standardized products, an intelligent use of legal advertising will make it unnecessary to resort to a stable collusive structure. Sometimes it will be enough to revitalize the cartel when

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(13) TFEU, Art. 49 and 56.

the call is published or the invitations to participate in the next tender are disseminated.

Even if there is no competition problem, an absolutely transparent procedure may make tacit collusion between tenderers possible. Protecting confidentiality for competitive reasons acquires a greater relevance in the new contractual modalities based on the generation of ideas and technologies; in particular, the pre-commercial procurement.

The principle of transparency in PMC does not necessarily possess all the strength that it has in a regular public procurement. Even though PMC has been regulated by Directive 2014/24, it is a pre-procedural phase. This entails that the innovative contracting authority has the upper hand to increase or reduce the scope of the principle. Such level of definition grants the purchaser a considerable power of definition over the boundaries of the confidentiality principle (*i.e.*, over the extension of the data disclosure obligation imposed on it and on the bidders).

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As a preliminary conclusion, the principles of transparency and confidentiality do not work in the preliminary market consultations in the same way they do in a regular public procurement. There are variations in the application of these principles due to the differences in the nature and on the kind of relationships that are established in these two phases. In a preliminary market consultation, the only relationship that is established is a collaborative link between each consulted operator and the innovative contracting authority, wherein both parties may exchange ideas that will be used in a subsequent tender. There is no link nor relationship that is created among the consulted operators.

On the other hand, there are two types of relationships that are established in a regular public procurement. The first one links the contracting body with each bidder. It is a procedural and hierarchical direct connection, since the latter participates in a tender decided by the former and is bound by its decision. The second link connects the bidders in an indirect relationship based on competition and mutual exclusion. They do not share anything, because the selection of one means the exclusion of the others. Transparency, transmission of information and limited confidentiality play a role during the tender. They tend to ensure that the procedure is presided over by legal certainty, non-discrimination, protection of fair competition, and lack of conflicts of interest. All in all, their implementation allows the contracting authority to guarantee that the selected bidder is the one who

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deserves the contract, and that the other bidders can check it by reviewing the documents.

Since there is no competition nor links among the operators (and would-be bidders), where any of them may be selected and the rest excluded in a preliminary market consultation, none is entitled to demand the disclosure of information pursuant to the Directive. Nevertheless, the contracting body may opt to either act in that way (*i.e.*, waive the disclosure of information) or restrict the access to information with a goal of protecting any possible collaboration with one operator.

### 4.3. Principle of competition

One of the most important features of the preliminary market consultation is its non-competitive nature. In this phase, the firms are not rivals. They do not fight to the death to convince the public purchaser of the quality of their recommendations. In fact, they have no particular relationship with each other. Each one has an individual link with the contracting authority, which channels all the singular proposals in to one formula.

Although there is no competition among firms during a preliminary market consultation, the participants may still manifest an anticompetitive behavior during this stage. It is possible for the participants to commit collusion or to abuse a dominant position from the inception of preliminary market consultation, which deserves a sanction if the behavior brings about anticompetitive outcomes. Their effects may be delayed until the awarding of the contract. Competition law infringements during this preliminary phase are to be fined by competition agencies. And their authors can be disqualified for future tenders on the basis of Article 57 of Directive 2014/24 and national public procurement laws.

Preliminary market consultation gives the operators a chance to compete or to cartelise. Several elements may influence them to decide in one way or the other. Some decisions depend on the PMC design; the others are based on the firms' behavior. However, there is a precondition for collusion to succeed in this phase: that the ring possesses more and better information than the contracting authority over the relevant elements of the tender or the procurement.<sup>(14)</sup> When the asymmetry of information exists and is relevant, the cartel can proceed.

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(14) See also P.A. GIOIA, "Division of Public Contracts into Lots and Bid Rigging: Can Economic Theory Provide an Answer?", *EPPPLR*, 2018, pp. 26-30. Bid rigging is possible in procurement of innovative solutions due to the difficulty of the contracting authority to map the competitive landscape and calculate the expected number of participants.

#### 4.3.1. Information asymmetries

In summary, the main purpose of preliminary market consultation is to balance the different degree of information in the hands of the innovative public purchaser and the consulted entities (experts, operators in the market, other contracting authorities) for the benefit of the purchaser.

The differences in the degree of information are the essence for PMC, thereby making PMC useless if the contracting authority has already accumulated enough data to start an innovative tender. These differences are also an essential factor to account for the degree of dependence of the purchaser on the data provided by the advisors, and the feeling of defencelessness if the advisors take on a coordinated strategic behavior and engage in any kind of collusion. Based on the foregoing, every PMC process must set clear-cut rules to impede or thwart the participation of the operators in a query with a view to rig the tender. A good start would to replace the ‘meet-to-the-market’ sessions by other formulas that will hinder the communication among firms.

On another level, since not all the participants possess the same level of information and knowledge of a market, no contracting authority should be obliged to stretch the call for advice beyond what is reasonable. Very often, general publicity of a future PMC is desirable and convenient for the success of the query. However, no allegation of discrimination is to be admitted where the contracting body has the reasons to restrict the number or features of the consulted entities. Hence, the authority can choose between two degrees of dissemination: 1) ‘carpet bombing’, (*i.e.*, general publicity of the PMC, e.g., official journals, consultation days, open-door meetings); 2) or ‘selected bombing’ (*i.e.*, by calling a limited number of specialists through singular mailing or face-to-face meetings).

#### 4.3.2. Incentives for competing in PMC

In recent years, public opinion in many countries has been puzzled by the multiplication of collusion cases in public procurement. The anti-collusion spree owes more to a renewed action of some competition authorities than to a sudden ‘collusive fever’ affecting bidders. Actually, a traditional public contracting is a mature sector in terms of antitrust law. Public works, supply, services and concessions have always been infested with anticompetitive agreements.

At this point, and in many other features, innovative procurement differs from the above-mentioned types of public contracts. The sheer nature of the innovative contracts and the position of the parties in the tender can foster rivalry and discourage cartelisation. However, the same features can also give rise to more successive, long-lasting and dangerous collusive schemes.

FEATURES FOSTERING COMPETITION IN INNOVATIVE PROCUREMENT	
Contracting authority	<p>Monopsony</p> <p>Unilateral design of the whole process (preliminary market consultation, pre-commercial phases, tender...)</p>
Bidders	<ul style="list-style-type: none"> <li>– Rivals in private markets</li> <li>– Subjected to the tender rules</li> <li>– Winner-take-all</li> <li>– Exclusive/advantageous use in private markets of the new solutions</li> </ul>

On the one hand, innovative procurement implies the search for either a non-existent technology (pre-commercial), or a new good or service, or a variation of an actual one (innovation partnership). A contracting authority wishes for a new and innovative product if the existent one does not meet preexisting necessities. Therefore, the former and the new products cannot be used as substitutes to meet the same requirements; which means that they do not belong to the same market. The innovative purchaser will thereafter enjoy the monopsony over the new (product & geographic) markets. Theoretically, monopsonistic power strengthens and (tends to) immunize its holder against the bidders' aggressive and anti-competitive behaviors.

On the other hand, innovative procurement disposes of several tools to lure bidders into a competitive battle for the contract and to counter their temptation to engage in collusive agreements (which means to rig the tender and decide the winner of the contract) through any of these three means: (a) the submission to self-drawn procedural rules; (b) the *winner-take-all* outcome; and (c) the advantageous position in private markets.

The EU Directives and the national laws entrust contracting authorities with the power/obligation to unilaterally draw the rules for any particular tender. Competition for the market is at the core of this system. One of its goals is to ensure a competitive process where a contract is awarded to an operator which offers the best bid. These features are common to every type of contract. What distinguishes innovative procurement, particularly the pre-commercial procurement, is the wide degree of freedom that contracting authorities enjoy in designing the rules. This freedom runs to the point that a pre-commercial procurement is considered as atypical; that is, it lacks specific regulation in a law. Therefore, a contracting authority may be particularly stringent on the requirements to impede bid rigging from infecting a procedure (*i.e.*, banning or

restricting joint bids, or strictly enforcing the exclusion grounds set in Art. 57 of the Directive).

The *winner-take-all* doctrine is a basic property of public procurement. It means that the contractor reaps all the fruits of the contract because its rivals are either excluded or have lower scores in the evaluation (*winner-take-all the contract*). In case that most private customers buy the innovative product designed for public entities, the contractor may acquire not only the monopsony on the contract but also monopolizes the market (*winner-take-all the market*), a situation that may last until the market is penetrated with other substitutable products or services.

In addition, the fact of winning an innovative public contract is likely to generate important positive side effects in the other business of the successful contractor. Pre-commercial procurement offers the purest example that both parties have a share in the output. In innovation partnership, the awardee receives additional benefits, such as the advantage of having the know-how needed to implement the contract or to develop a new business line.

These three collusion-deterrent factors have their own place during the innovative procurement procedure. But they should play a key role in the PMC, too. The PMC preparatory documents must state that the whole process has been designed with a view to preventing cartelization, fostering future candidates to fight for the contract, and pointing out that the public contract may be profitable for the contractor's other business.

#### 4.3.3. Incentives for colluding in PMC

Nonetheless, the sheer features of innovative procedures can encourage some firms to form a cartel for the purpose of improving their chances to win a contract. Some elements favour cartelisation, such as the vagueness of the procedures and the object of the contracts. In particular, the development of a PMC can help operators to decide whether to engage in collusive practices. On this note, the collusive firms' anti-competitive behaviors and the types of collusion do not substantially differ from the ones in other categories of public contracts.

INCENTIVES AND OBSTACLES TO COLLUDE IN PMC	
INCENTIVES	OBSTACLES
Restricted call for advice.	General call for advice.
Limited invitation to participate in the queries.	Maximum dissemination of actions on the web.

Selection of the advisors in a tiny geographic scope.	Selection of advisor in a wide geographic scope.
Bilateral or multilateral physical meetings with all potential operators.	Separate meetings or interviews with potential operators. Public consultation process similar to that of normative projects.
Consultation to organizations and business associations.	Avoiding or lessening the consultation to organizations and business associations.
<b>INCENTIVES</b>	<b>OBSTACLES</b>
Small number of advisors show an oligopolistic market.	Large number of operators/advisors.
A sole operator/advisor monopolised the market.	Large number of operators/advisors
One prevalent operator/advisor leads a certain number of satellite-competitors bound up to follow his opinions.	Independent operators.
Important presence of groups of firms among the consulted.	Independent operators.
Operators/advisors share the market or engage in tacit collusion.	Independent operators.

Generally, there are two main reasons that entice some of the consulted operators to cartelise at such early stage and rig the subsequent innovative tender: (a) the setting out of collusion-fostering selection criteria on the part of the contracting authority; and (b) the anticompetitive practices of the operators/advisors.

#### 4.3.4. Risk for competition from the PMC design

The setting of narrow requirements by a public purchaser may reduce the number of firms able or disposed to participate in the PMC (and future would-be bidders), which may entice these firms to coordinate with each other in providing their answers to the queries of the contracting authority. The same effect may happen in an open but restricted call for advice and in a narrow invitation to a limited number of operators. The collusive outcome is likely to worsen when all the consultants' trade in the same geographic market and the contracting authority impedes or dissuades outsiders to take part.

The width of the admittance to meetings works in a counter-intuitive way. The more firms join to a meeting as advisors, the more dangerous the meeting is to ensuring competition. Bilateral encounters are strongly recommended because they ensure the secrecy of the proposals to a certain extent. On the

contrary, multilateral physical meetings allow the participants to know about the positions of the other participants, who may reckon the chances of success, and assess the convenience of bidding on a competitive basis or forming a cartel for participating in a future tender. In short, general gatherings may serve as substitutes for information exchanges.

Further, the inclusion of business associations among the consulted firms may also bring about cartelisation. Their tasks include making contact easier and reconciling the interests of their members, which will likely make up a significant number of the consulted operators in a lot of cases. Industrial fairs are a second source of risk. A great number of them are managed – directly or indirectly – by operators and associations. An easy way for them to win over the contracting authority is to forge a new fair or similar meeting where the public purchaser is ‘encircled’ by the cartel.<sup>(15)</sup>

#### 4.3.5. Risk for competition from the consulted firms

The abovementioned factors require an active engagement of the consulted firms to raise a danger for competition. However, participants in a PMC may produce the same result by taking advantage of market flaws. Two sets of defects must be described here. First, the oligopolistic or monopolistic market structure may easily end in [tacit or open] collusion or in [collective or individual] abuse of dominant position. Second, the lack of autonomy of the consulted firms qualifies as the first point to collusion.

To ensure a fair PMC and a competitive tender, it is important for the contracting authority to be knowledgeable about the operators. The authority should get information about the possible links among the participants. Independent operators are supposed to compete by the same market rules until the best of them expels or dwarfs the others. It is difficult to say the same regarding firms that belong to the same group of business affiliates.

In case a link exists, the purchaser has leeway to use at will the information given by the non-independent operators. This attitude does not infringe the principles of non-discrimination, competition and transparency for two reasons: first, as stated above, the PMC is a pre-procedural phase, whereby the participants in a PMC neither compete nor have to interact at all. Second, the contracting authority must be free to reject or take advantage of the information in the best way for a successful tender. Since no rigged tender is fruitful, the suspicion that the information has been fixed may well drive him to set it apart. This attitude does not infringe the above principles, since the firm(s)

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(15) See also P.A. GIOSA, “Division of Public Contracts into Lots and Bid Rigging: Can Economic Theory Provide an Answer?”, *EPPPLR*, 2018, p. 30, esp. pp. 26-30.

whose contributions have been unattended are not forbidden to participate in the tender in equal terms with the others.

#### 4.3.6. Incentives for an autonomous competition in PMC

During the planning and implementation of a PMC, the contracting authority may lessen the chances of collusion by increasing the number of consulted firms, and widening their geographic scope. In either case, the authority must act independently during the preliminary market consultation, as it must in the future tender. Therefore, the conduct of general meetings, as well as the participation of business associations, must be avoided, or at the very least, reduced if possible.

The public purchaser that foresees a risk of collusion from either market flaws or the firms' behavior must react in order to encourage the participation of a large number of independent operators.

#### 4.3.7. Position of the Spanish Competition Authority

In the Report on the Draft of Public Sector Contracts Law, the National Commission of Markets and Competition (CNMC, in Spanish) made an insightful study of the PMC concerns for competition.<sup>(16)</sup> As was written above, the Draft regulates in its Article 115 the possibility of conducting market research and consulting with economic operators in order to prepare the tender correctly and to inform operators about their plans and the requirements they will require to attend the procedure.

The CNMC claims that the positive aspects of a better knowledge of the market derived from the queries to operators do not hide the problems from the perspective of competition. They may lead to a considerable risk of being caught by the contracting authority and may lead to an infringement of the principles of equal access to tenders, non-discrimination and non-distortion of competition.

The CNMC recommends the introduction of a number of corrective measures: 1) bilateral or multilateral physical meetings with all potential operators should be avoided given the risk of collusion between them; 2) no query with specific operators (*i.e.* queries should be limited to independent experts or authorities); 3) queries with professional organizations and business associations should be avoided; 4) the introduction of a public consultation process in which these preliminary consultations are carried out, similar to that in normative projects; and 5) maximum dissemination of actions on the web so that all potential stakeholders have access and possibility of making contributions.

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(16) IPN/CNMC/010/15, 16 October 2015.

## 5. Prior Involvement of Tenderers in PMC

### 5.1. *Fabricom* and Article 41 of Directive 2014/24

Article 41 of Directive 2014/24 deals with the issue raised by a “candidate or tenderer or an undertaking related to a candidate or tenderer (that) has advised the contracting authority, whether in the context of Article 40 or not, or has otherwise been involved in the preparation of the procurement procedure”. The ulterior participation of that firm in the tender for which preparation it had been working is a challenge to the principle of non-discrimination, and to the actual effectiveness of competition.

Article 41 is the normative development of a clear-cut doctrine enacted by the Court of Justice in *Fabricom*.<sup>(17)</sup> The case judged a Belgian presumption stating that any person who has been instructed to carry out research, experiments, studies or development in connection with public works, supplies or services was not allowed to participate in or to submit a tender for a public contract for those works, supplies or services, although that person was not permitted to prove that, in the circumstances of the case, the experience which he had acquired was not capable of distorting competition.

The defendant (Belgian State) stated that all tenderers must have equal opportunity when formulating their tenders. On the contrary, a person who had participated in certain preparatory works may be at an advantage when formulating his tender on account of the information concerning the public contract in question which he has received when carrying out that work. Furthermore, that person may be in a situation which may give rise to a conflict of interests in the sense that, he may, without even intending to do so, where he himself is a tenderer for the public contract in question, influence the conditions of the contract in a manner favourable to himself. Such a situation would be capable of distorting competition between tenderers.

The judgement claimed that a rule such as that at issue in the main proceedings does not afford a person who has carried out certain preparatory work any possibility to demonstrate that the problems referred to in paragraphs 29 and 30 of the judgment do not arise in his particular case. Such a rule goes beyond what is necessary to attain the objective of equal treatment for all tenderers. Indeed, the application of that rule may have the consequence that the operators who have carried out certain preparatory works are precluded from the award procedure even though their participation in the procedure entails no risk whatsoever for competition between tenderers.

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(17) ECJ (2nd Ch.), 3 March 2005, *Fabricom S.A. v Belgian State*, cases C-21/03 and C-34/03, *Fabricom*.

“Article 3(2) thereof, Directive 93/36 and, more particularly, Article 5(7) thereof, Directive 93/37 and, more particularly, Article 6(6) thereof, and also Directive 93/38 and, more particularly, Article 4(2) thereof, preclude a rule [...] whereby a person who has been instructed to carry out research, experiments, studies or development in connection with public works, supplies or services is not permitted to apply to participate in or to submit a tender for those works, supplies or services and where that person is not given the opportunity to prove that, in the circumstances of the case, the experience which he has acquired was not capable of distorting competition”.

## 5.2. Direct and indirect participation in the previous PMC

*Proprio modo*, the scheme set out by the Directive is applicable where an economic operator intervenes in the preparatory phase and afterwards takes part in the subsequent tender. This general statement demands a further explanation, related to both the kind of participant and the type of participation.

First at all, Article 41 sets a wide circle of operators bound to the special rule of compatibility. It mentions the “candidate or tenderer or an undertaking related to a candidate or tenderer”. Therefore, not only are the bidders at risk of being excluded, but also the firms linked with them that contributed to develop the preparatory phase, working for the contracting authority as managers, consultants or advisors. The Article is not precise about the nature of the bonds between the tenderer and the related undertaking. This inconclusiveness should be understood as encompassing both corporative and business relationships. The intensity of the link is also opened to interpretation. The link is indisputable where the third undertaking and the tenderer belong to the same corporate group; even more where the latter is or acts as a group head. In cases where the firm and the bidder only have a business relationship, the closeness sketched by Article 41 should be assessed on a case-by-case basis.

## 5.3. Scope and limits of the exclusion

The ECJ doctrine set two rules. First, the person or firm concerned is given a sort of right of defence, to show that its participation does not affect the competition during the procurement. Second, the exclusion is a measure of last resort, only implementable when the other measures have failed.

### 5.3.1. Right of defence and right to appeal

In applying the first rationale, Article 41 of the Directive requires the contracting authority to act *ex officio* to check the behavior of the candidate. The contracting body can request information from all the participants. The bidder at stake has the main interest in claiming that his behavior during

the PMC phase is lawful.<sup>(18)</sup> The right of defence calls for an active implication. Prior to any exclusion, he shall be given the opportunity to prove that his involvement in preparing the procurement procedure is not capable of distorting competition.

The other bidders also have a legitimate say on the matter since one of them may have also incurred a conflict of interest different from the one laid down in Article 24 of Directive. This bidder is most likely to become the awardee. So, the contracting authority is bound to communicate to the other candidates or tenderers the relevant information exchanged with the candidate at stake in the context of his involvement in the preparation of the procurement procedure and the fixing of adequate time limits for the receipt of tenders.

The last measure – the disclosure of the information exchanged – may not be enough to ensure transparency and, above all, to heal the appearance of favoritism as a result of vendors' intervention in the PMC and in the tender. It is right that the knowledge of the formal documents may give a hint about the degree of a bidder's influence in the PMC and on its participation in the wording of the procedural documents. But these data are not enough to rule out a breach in the principles of equal treatment and competition. The influence of the bidder at stake may go far beyond the mere draft of those documents. It also encompasses its relationships with officials, experts and other staff and the gathering of information about the quality of the contracting authority. Summarizing, the knowledge of the documents showing the participation in the PMC is just a linear way to make an assessment. The documents may not, in themselves, be enough to allow other vendors to resolve the uncertainties.

The third interested party in the investigation is the contracting authority itself, whose concerns tracks those of the bidders. The situation that gives rise to an investigation may easily come from misbehaviors on the part of some officials, such as conflicts of interests or corruption. Inquiries can also shed light on other illegal behaviors of the bidders, such as unlawful concerted actions, collusion in multiple forms and even the infringement of other laws, admitted or tolerated by the public procurement official. All these situations are easier in innovative procurement than in more traditional procedures. In many cases, contracting authorities will be at the mercy of the consultants during the PMC. The consultants may seek to define the entirety or a substantial part of the procurement. A future bidder can easily 'hide' some clues helpful in the future tender. In the face of these risks, the contracting authority is not limited simply to request the

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(18) See also C. MOUKIOU, "The Principles of Transparency and Anti-Bribery in Public Procurement: A Slow Engagement with the Letter and Spirit of the EU Public Procurement Directives", *EPPPLR*, 2016, p. 83. The burden of proof lies on the bidder to prove that his/her involvement did not lead to the distortion of competition.

vendors' participation. On the contrary, the contracting authority is entitled to decide and implement his own measures, since Article 41 clearly requires the contracting authorities to take appropriate measures to ensure that competition is not distorted by the participation of that candidate or tenderer.

The measures taken shall be documented in the individual report required by Article 84.1.e) of Directive 2014/24 ("conflicts of interests detected and subsequent measures taken").

### 5.3.2. Exclusion

Only when actions to mitigate potential conflicts of interest have been applied unsuccessfully, and there are no other means to ensure compliance with the principle of equal treatment, may a candidate or a concerned tenderer be thrown out or excluded from the procedure. The removal of a bidder under this circumstance looks like an unusual ground for expulsion. On the first hand, it presupposes that the expulsion of a participant during the procedure is based on its own irregular behavior. But, on the other hand, Article 57 of Directive 2014/24 sets a *numerus clausus* relationship of exclusion grounds, which does not include the above-mentioned ground. Moreover, unlike Article 57, Article 41 limits its future sanctions to the sacking of the same tender, but it does not include the prohibition for the bidder to participate in future tenders.

Besides the principle of non-discrimination, Article 41 builds the argument for an exclusion based on the principle of competition. The participation in a tender of a firm that previously took part in a PMC will be anticompetitive if (by virtue of its behavior during the preliminary market consultation) it is "capable of distorting competition". This sentence must be understood as tantamount to thwarting competition in the market as well as competition for the market; that is, the participant will be excluded where its former intervention in the PMC extends to the said participant (would-be bidder) unfair advantages in the tender which are not available to the other bidders (*i.e.*, a biased design of the procedure); or when it has colluded in the PMC phase to rig the tender. In both cases, the goal is the same: to unlawfully win the contract.

A decisive feature for the accurate application of Article 41 lies in the standard of unlawfulness. The participation in the preparatory phase may increase the level of influence of the participant and enhance its chances to win the contract in breach of principles of equal treatment and competition. Although it is in the end a case-by-case question, several clues can be provided to help contracting authorities to decide whether the participant should stay in the procurement.

The first one is the hard-core restrictive admission option. The special incompatibility provided for in Article 41 would apply if there is *the slightest indication*

that participation may lead to restrictions on attendance or involve privileged treatment and, in the end, violate the principles applicable to public procurement. In other words, compatibility would only be admitted in case that it could be completely ruled out that the participation would restrict competition in the tender or place the company in a position of competitive advantage over the other tendering companies.<sup>(19)</sup> This position formally shelters competition and vetoes any chance of taking advantage of the previous intervention in the preparatory phase. Therefore, it appears to foster participation and ensure the rights of the other bidders. However, a mechanical application might infringe Article 41's prohibition of an automatic ban against the participant at stake.

A second option is to base the admission decision on the evidence provided by the participants and future bidders during the preliminary market consultation. This option restrains the contracting authority's ability to decide since it does not conduct its own research or investigation. Article 41 calls for contracting authorities to engage in all the actions that are useful to investigate the compatibility. They are not sheer recipients of information. They are entitled and obliged to conduct their own investigation.

Therefore, the most accurate way to implement Article 41 is to join a treble investigation plus a case-by-case perspective. First, the contracting authority must take all the measures to ease the 'beleaguered participant', the other bidders and the authority itself. Second, it must conduct its own investigation and not merely rely on the evidence provided by the concerned tenderer. Third, the contracting body must decide the case based on the evidence from its own investigation

Whether the automatic exclusion of the participant in a PMC is unfair and counterproductive (it will deter firms from taking part in that phase), the solution provided by Article 41 of Directive 2014/24 shows a decisive flaw: it relies on the contracting authority to decide on the firm's independence. Although it seems the obvious way – the independence is disputed within a tender, so the purchaser, which is the judge of the tender, is the competent authority to sort out the problem – the solution forgets that a typical contracting authority may well lack the means, the time, and the will to dig deep in the question. Moreover, a careful reading of Article 41 shows a rebuttable presumption of lawfulness. The bidder at stake must bring in the evidence supporting its innocence. The contracting authority must assess these evidences, and it can also evaluate other materials.

So, it is doubtful that many authorities start with strictly proper investigations. The likeliest result instead is that they will fulfill the right of the

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(19) Decision 395/2015, Tribunal Administrativo de Recursos Contractuales de la Junta de Andalucía, Seville, 20 November 2015.

concerned tenderer to be heard, and except in cases of evident violations of competition during the PMC, the purchaser will take note of the allegations against the firm and the limited evidence at its disposal, and decide that 'the show must go on', even with the suspected firm on board.

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# CHAPTER 16

## On the Non-tariff Barriers Obstructing Free Trade in the Transatlantic Defense Procurement Market

BY

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### 1. Introduction

Defense is the most protected field in the public sector.(1) It constitutes not only a large share of public procurement but also of overall public and private spending.(2) Yet given the massive scale of transatlantic trade,(3) defense forms only a small part.(4) Transatlantic defense liberalisation has been

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\* This essay is derived from a draft of one chapter of his dissertation, which considers more broadly how the EU and U.S. federal public procurement systems' mutual foreignness creates non-tariff barriers. The author is grateful to his advisors, Peter Trepte and Craig Rotterham, for their guidance and to his wife, Alicia, for her patience and support. Free access to the law libraries at Nottingham, George Washington, Harvard, Virginia, and Yale was indispensable. The views expressed here are his own and do not reflect an official position of the Department of the Air Force, Department of Defense, or any other U.S. government agency.

(1) S. MARTIN, K. HARTLEY and A. COX, "Defence Procurement of Dual-use Goods: Is There a Single Market in the European Union?", *Defence & Peace Economics*, 1999, 10:1, p. 55, writing: "Of all procurement markets, defence is probably the most protected and thus the most difficult sector within which to eradicate buy national policies", p. 56. See also C. GRANT, "Transatlantic Alliances and the Revolution in Military Affairs", in *Europe's Defence Industry: A Transatlantic Future?* (G. ADAMS et al. eds), London, Centre for European Reform, 1999, p. 63, observing, "The defence industry, more than any other, has defied globalisation".

(2) M. TRYBUS, "European Defence Procurement: Towards a Comprehensive Approach", *Eur. Pub. L.*, 1998, Vol. 111, p. 4.

(3) G. GAMBINI, R. ISTATKOV and R. KERNER, "USA-EU – International Trade and Investment Statistics, EU and United States form the largest Trade and Investment Relationship in the World", accessed 4 July 2019 at [https://ec.europa.eu/eurostat/statistics-explained/index.php?title=USA-EU\\_-\\_international\\_trade\\_and\\_investment\\_statistics&oldid=368909](https://ec.europa.eu/eurostat/statistics-explained/index.php?title=USA-EU_-_international_trade_and_investment_statistics&oldid=368909), reporting that EU-U.S. trade accounts for nearly one-third of global imports and exports and that "together they have the largest bilateral trade relationship in the world".

(4) U.S.-Crest, "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries", 2009, accessed 4 July 2019 at <https://ec.europa.eu/docsroom/documents/10489/attachments/1/translations/en/renditions/native>, 85, reporting that "overall level of transatlantic defence trade is extremely low" in that it composes a "very small fraction of the overall transatlantic trade and is much smaller than other technology related sectors such as civil aerospace". In fact, when compared to the latter, defense "can be considered almost non-existent", p. 41.

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a longstanding goal.(5) Because this sector has been mostly excluded from free trade pacts, the gains that would accrue from liberalizing this highly protected sector would be greater than from any other.(6)

Tariffs are not the main problem. They are relatively low and do little to impede trade.(7) Non-tariff barriers are the main culprit. These come in several varieties, including domestic preferences, collateral policies, illegitimate practices, and certain commercial procurement policies.(8) Some are overt, such as the Buy American Act. Others are not. Sue Arrowsmith identifies a subtle class of non-tariff barrier that she calls “structural restrictions.”(9) These arise from the dissonance among foreign procurement systems and the inexperience of foreign vendors attempting to sell abroad. Such restrictions “raise practical barriers to entry as foreign vendors run headlong into dense and alien procurement regimes”.(10)

Despite a common Western legal tradition and much shared history, the U.S. federal government and the EU public procurement systems are no less susceptible to structural restrictions. This essay seeks to bridge the resulting gap insofar as the arms market is concerned. It attempts to answer this question: if the overt trade barriers were removed, what would remain? And it thus assumes a hypothetical world where a robust version of the Transatlantic Trade and Investment Partnership (TTIP) has passed and that this version of the TTIP covers defense procurement.

Comparing the U.S. and the EU public procurement systems is tricky for several reasons. First, the two systems are asymmetric, making comparisons difficult.(11) Further, although some piecemeal work has been done, no one has

(5) See M. EDMONDS (ed), “International Military Equipment Procurement Partnerships: The Basic Issues”, in *International Arms Procurement: New Directions*, Oxford, Pergamon, 1981, pp. 12-13.

(6) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, Cambridge, CUP, 2017, pp. 491-492.

(7) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defence Market and the Implications for U.S. National Security*, Middleburg, Center for Transatlantic Studies, 2009, pp. 65, 68.

(8) S. ARROWSMITH, *Government Procurement in the WTO*, The Hague, Kluwer, 2003, pp. 14-18.

(9) *Ibid.*, pp. 18-19.

(10) C.R. YUKINS and S.L. SCHOONER, “Incrementalism: Eroding the Impediments to a Global Public Procurement Market”, in *Georgetown J. Int'l L.*, Vol. 38, 2007, pp. 529-576, citing S. ARROWSMITH, *Government Procurement in the WTO*, *op. cit.*, p. 558.

(11) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 14. The EU and U.S. federal procurement systems are asymmetric in at least two senses. First, they are asymmetric in that the U.S. national government is a federal system, whereas the EU form of government resists comparison with other systems as “it contains some features of a traditional international organization” as well as “some features of a federation”. See T.C. HARTLEY, *The Foundations of European Law*, Oxford, OUP, 2014, pp. 11-12. Second, they are asymmetric in that the U.S. federal system encompasses “many aspects of the procurement process which are otherwise not explicitly regulated under EU law, from source selection decisions through to contract performance”. L.R.A. BUTLER, *Transatlantic Defence*

attempted a comprehensive comparison of the two systems.(12) Thus, finding one's way requires proceeding without map or compass. Moreover, a cursory account can be misleading because superficial resemblances are sometimes illusory.(13)

Notwithstanding these challenges, it is worth considering how the two legal systems' differences impede trade flows, even though they are both ostensibly open and competitive.(14) The essay posits that the *foreignness* of the two systems substantially affects the transatlantic defense market. Vendors are deterred from competing in an unfamiliar system that they are unsure how to navigate.(15) This essay sketches a crude map, which requires elaboration. As others contribute, perhaps cumulatively such efforts may lead a few more buyers and sellers to take an interest in opportunities across the pond.

The essay proceeds in three parts. Sections 2. and 3. summarize the histories, constitutional features, and laws of the U.S. and the EU defense procurement systems. Section 4. considers points of comparison between the two and the mutual benefits that would accrue from freer trade. Section 5. summarizes three possible lines of effort to free up defense trade. It bears mentioning at the outset that this essay does not attempt to delve into the Member States' 28 distinct versions of defense procurement and restricts itself comparisons between the U.S. federal government and a generic EU Member State.(16) The author is keenly aware of the difficulties with attempting a comparison in this manner. He devotes an entire chapter of his doctoral thesis (from which this piece is derived) to acknowledging and addressing such challenges. He submits, however, that there is nonetheless value in this exercise – and invites the skeptical reader to temporarily suspend her disbelief as to the profound structural

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*Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 249-250.

(12) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 10-11, 14, 435, explaining that his book presents the first attempt at a systematic comparison of U.S. and the EU public procurement law for defense.

(13) J.I. SCHWARTZ, "United States of America", in *Droit Comparé des Contrats Publics*, (R. Noguellou and U. Stelkens eds) Brussels, Bruylant, 2010, noting that the U.S. system's complexities have developed over two centuries and warning that "a cursory account therefore risks misleading even those with an extensive knowledge of other procurement law systems", p. 614.

(14) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 270, 276-277.

(15) U.S.-Crest, "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries", *op. cit.*, p. 8, explaining that barriers can be "numerous and diverse in nature" and that "[t]hey can be direct or indirect, political, cultural, economic, technological, or military".

(16) This essay restricts its attention to the EU level for two reasons. First, for the sake of brevity. Second, because "there are no detailed studies on the national implementation of the Defence Directive", *Ibid.*, p. 5, 161. For a brief introduction to the defense procurement practices of about half of the Member States, see European Defence Agency, "Vademecum on Member States Defence Procurement Practices for Defence Procurement Gateway", 10 October 2014.

differences between U.S. and EU institutions and consequent difficulties with comparing their procurement systems.

## *2. Defense Procurement in the United States*

The U.S. federal government acquires only a small portion of goods and services from foreign suppliers.<sup>(17)</sup> While that is partly due to explicitly protectionist policies, that is not the whole story. In the closing chapter of his book on transatlantic defense procurement, Luke Butler makes the following observation about the existing literature on this subject: “A fundamental aspect that has not been considered in any detail concerns the significance of what might loosely be termed “constitutional features” of the United States, EU, and EU Member State procurement law systems”.<sup>(18)</sup> American scholars have likewise noted that the U.S. federal system’s “fundamental values” are especially ill-defined.<sup>(19)</sup> This section aims to narrow that, especially for European vendors who are considering competing for U.S. defense contracts.

### 2.1. History

Justice Oliver Wendell Holmes wrote, “A page of history is worth a volume of logic”.<sup>(20)</sup> So it is with U.S. defense procurement. Often its nuances and idiosyncrasies can only be explained from a historian’s perspective:

“If someone were asked to devise a contracting system for the federal government, it is inconceivable that one reasonable person or a committee of reasonable people would come up with our current system. That system is the result of thousands of decisions made by thousands of individuals, both in and out of government. It reflects the collision and collaboration of special interests,

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(17) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, op. cit., pp. 84-87, providing a detailed analysis of U.S. defense spending and what sorts of procurement are subject to foreign competition. *Ibid.*, pp. 273-275, elaborating on the difficulties with ascertaining what proportion of U.S. defense spending includes foreign competition. Anecdotal evidence suggests that very little goes to foreign suppliers. *Ibid.*, pp. 660-661, finding that four large U.S. contractors alone receive 69% of defense spending at the prime level. Foreign suppliers’ share is higher at the subcontract level. *Ibid.*, pp. 662.

(18) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, op. cit., p. 7, 317.

(19) S.L. SCHOONER, “Fear of Oversight: The Fundamental of Businesslike Government”, *Am. U. L. Rev.*, Vol. 50, 2001, p. 627, saying “a constantly changing patchwork of statutes defies efforts to identify broad Congressional aims, and the literature is strangely silent with regard to efforts to define the system’s fundamental values”, p. 675, and citing J. WHELAN and E.C. PEARSON, “Underlying Values in Government Contracts”, *J. Pub. L.*, Vol. 10, 1962, p. 298, saying “The Federal Government has been making contracts for as long as it has existed, yet little attempt has been made to rationalize this phase of governmental activity in its relation to the functions of government and to the persons and firms with whom contracts are made”.

(20) *New York Trust Co. v. Eisner*, 256 U.S., 1921, 345, 349.

the impact of innumerable scandals and successes, and the tensions imposed by conflicting ideologies and personalities”.(21)

The authoritative volume on the history of the U.S. government’s procurement system to date runs to 597 pages.(22) Only a few pages are devoted here. It is hoped, however, that this outline may illustrate how this system was forged in the crucible of war and explain how its framework derives from the federal government’s history and experience.

Although the United States has from colonial times been a bellicose nation,(23) actively engaged in warfare with the native population and the rival European powers competing for dominance in North America, it has also been deeply ambivalent about warfare.(24) If Congress has infrequently formally declared war, the United States has for two and a half centuries regularly engaged in “savage wars of peace”.(25) Many are blissfully unaware or forgetful that the United States fought small wars against insurgencies spanning the globe long before Vietnam, Iraq, or Afghanistan.(26) Americans conquered a continent in pursuit of manifest destiny(27) yet cast a wary eye on colonialism.(28) This cognitive dissonance has existed from the founding of the Republic and features of this ambivalence are embedded in the Constitution.(29)

(21) J.F. NAGLE, *History of Government Contracting*, 2nd ed., Washington, George Washington UP, 1999, p. 519.

(22) *Ibid.*, p. 597.

(23) See gen. B. BAILYN, *The Barbarous Years: The Peopling of British North America*, New York, Knopf, 2012, whose closing chapter summarizes British colonists’ first century in North America as follows: “They lived conflicted lives, beset with conflicts experienced, rumored or recalled – unremitting racial conflicts, ferocious and savage; religious conflicts, as bitter within as between confessions; conflicts with authority, private and public; recurrent conflicts over property rights, legal obligations, and status; and conflicts created by the slow emergence of vernacular cultures, blending of disparate subcultures adjusting to the demands of heightened aspirations and local circumstance”; J.F. NAGLE, *History of Government Contracting*, *op. cit.*, p. 497.

(24) See D.S. REVERON, N.K. GVOSDEV and M.T. OWENS, *U.S. Foreign Policy and Defense Strategy: The Evolution of an Incidental Superpower*, Georgetown, GUP, 2015, p. 45, explaining that the “creation and expansion” of a national security establishment “went against the grain of U.S. political culture”; J.Q. ADAMS, “Address of July 4, 1821”, in *John Quincy Adams and American Continental Empire: Letters, Papers, and Speeches* (W. LAFEBER ed), New York, Quadrangle Books, 1965, pp. 42, 45, observing that America “goes not abroad in search of monsters to destroy”.

(25) See gen. M. BOOT, *The Savage Wars of Peace: Small Wars and the Rise of American Power*, New York, Perseus, 2002, describing the many small wars fought in the course of U.S. history.

(26) See gen. *ibid.*

(27) See J.T. HEIDLER and D.S. HEIDLER, “Manifest Destiny, in *Encyclopaedia Britannica*”, available at [www.britannica.com/event/Manifest-Destiny](http://www.britannica.com/event/Manifest-Destiny), accessed 4 July 2019, describing the quasi-religious movement that led the United States to seize the Oregon country, Texas, New Mexico, and California before the Civil War and then to declare war with Spain and to annex Hawaii in the 1890s.

(28) Some argue that Americans have long opposed colonialism to a fault. See gen. W.R. LOUIS, “American Anti-Colonialism and the Dissolution of the British Empire”, *Intl Affairs*, Vol. 61:3, 1985, p. 395, arguing that unrest during the Cold War had as much to do with America’s push for rapid decolonization as with Soviet meddling.

(29) See D.S. REVERON, N.K. GVOSDEV and M.T. OWENS, *U.S. Foreign Policy and Defense Strategy: The Evolution of an Incidental Superpower*, *op. cit.*, pp. 45-47, citing U.S. Constitution, Art. I, sec. 8, which gives Congress the power to raise armies only “in times of war” but giving it unequivocal authority to maintain a navy,

Due in some part in some part to Madisonian fears about a large standing army and in some part to a treasury that was underfunded until the passage of the Sixteenth Amendment, national security was ad hoc from 1775 to 1945.(30) World War II and Cold War experiences were formative to the contemporary defense procurement system.

During the interwar years, sentiment shifted away from interventionism. Americans sought to avoid further entanglements in foreign wars; isolationism was the word of the day.(31) Then came the attack that irrevocably changed the course of U.S. history. The United States was unprepared for a two-front war.(32) In hindsight, perhaps the outcome seems inevitable. It was, in fact, a close-run thing.(33) The lesson was learned: never again would the United States fail to prepare. Pearl Harbor informed defense planning for decades.(34)

U.S. politicians – and not only the current resident of the White House – are wont to complain about European allies' failure to build up their militaries. But the disparity is due in part to historical accident. The buildup of massive forces that are deployable around the globe owes to the nature of the Soviet threat and America's geographic advantages. During the Cold War, Communists sought to foment revolution in virtually every corner of the world, and the United States responded in kind.(35) Building a military specializing in fighting abroad would have been impractical had America faced existential threats on its borders as in Europe, whose armies naturally concentrated on territorial defense. But with oceans providing buffers on east and west, friendly neighbors to its north and south, and a menacing Soviet threat farther afield, the United States built a fearsome arsenal geared toward extraterritorial warfare.

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reflecting the Founders' concerns that a standing armies would lead to tyranny but tacitly approving of adventurism abroad with a navy that would protect U.S. commercial interests.

(30) D.S. REVERON, N.K. GVOSDEV and M.T. OWENS, *U.S. Foreign Policy and Defense Strategy: The Evolution of an Incidental Superpower*, *op. cit.*, p. 49.

(31) *Ibid.*, p. 3, stating that “[r]ight up to the Second World War [...] the preferred American position was”, quoting F.L. Schuman, *International Politics: An Introduction to the Western State System*, 2<sup>nd</sup> edn, New York, McGraw-Hill, 1937, p. 481, “to protect its world interests without involving itself in entanglements abroad”.

(32) See K.P. O'BRIEN, “The United States, War, and the Twentieth Century”, in *The Cambridge Companion to American Culture*, Cambridge, CUP, 2006, pp. 235, 242.

(33) A.J. Levine criticized a tendency among popular historians to cast the Allied victory as narrow or near-run for dramatic effect. See A.J. LEVINE, “Was World War II a Near-Run Thing?”, *J. Strategic Studies*, 1985, p. 38. However, whatever the reality, Americans *perceived* that the outcome of World War II was too close for comfort.

(34) See W.B. BURNETT and W.E. KOVACIC, “Reform of United States Weapons Acquisition Policy: Competition, Teaming Agreements, and Dual Sourcing”, 6 *Yale J. Regulation*, 1989, pp. 249, 257.

(35) D.S. REVERON, N.K. GVOSDEV and M.T. OWENS, *U.S. Foreign Policy and Defense Strategy: The Evolution of an Incidental Superpower*, *op. cit.*, p. 5, explaining that the “Soviet threat required the United States to develop a global logistical system to reinforce its allies”.

Post-Cold War history is still unfolding. This much can be said so far. Defense underwent deep cuts in the 1990s in pursuit of the peace dividend, even as the U.S. military deployed at an unprecedented pace to Somalia, Rwanda, Haiti, the Balkans, and beyond. Spending spiked to nearly Cold War levels during the prosecution of the War on Terror in the first decade after the 9/11 attacks, only to subside again following the 2007 financial crisis. But fighting dispersed terrorist groups and counterinsurgencies in Iraq, Afghanistan, Libya, and Yemen, and beyond reinforced the procurement spending centered on operational requirements for a military that could rapidly deploy to far-flung reaches of the globe.

What does this history lesson say about the legal framework of defense procurement? At least three lessons can be drawn. First, from colonial times America has long favored competitive procedures.<sup>(36)</sup> But *competitive* doesn't mean openness to *foreign* competition.<sup>(37)</sup> This is due in equal parts to post-Pearl Harbor security of supply concerns and longstanding protectionist sentiments.<sup>(38)</sup> Further, because the United States enjoyed a technological lead in the Cold War, it was cautious about exporting weapons technology that could land in enemy hands. Third, post-war military purchasing has been structured around a specialized defense industrial base and a system endowing the federal government with considerable flexibility.<sup>(39)</sup> Nagle identifies several other trends that lie beyond the scope of this short essay.<sup>(40)</sup>

## 2.2. Constitutional features

A full understanding of the U.S. defense procurement system requires looking beyond the Federal Acquisition Regulation (FAR). Turning to the U.S. Constitution, one finds only limited guidance because “[t]here is no express provision” about government contracts there.<sup>(41)</sup> Yet there is a “large and complex body of law” on defense contracts.<sup>(42)</sup> In addition to some hints contained in the Constitution itself,<sup>(43)</sup> legal scholar Francis Laurent has suggested that this “large and growing body of law respecting defense

(36) J.F. NAGLE, *History of Government Contracting*, *op. cit.*, p. 7, describing a preference for sealed bidding since the early Republic, even though this contracting method “is often the least efficient way to contract and has often obstructed America’s ability to prepare for war.”

(37) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 273-277.

(38) W.B. BURNETT and W.E. KOVACIC, *Reform of United States Weapons Acquisition Policy: Competition, Teaming Agreements, and Dual Sourcing*, *op. cit.*, p. 258.

(39) See below Section 2.2.3.

(40) See J.F. NAGLE, *History of Government Contracting*, *op. cit.*, pp. 5-8.

(41) F.W. LAURENT, *Legal Aspects of Defense Procurement*, Madison, U. Wisc. Press, 1962, p. 17.

(42) *Ibid.*, p. 23.

(43) *Ibid.*, pp. 1-3, 17.

procurement programs and activities” is composed of statutes, common law, and executive orders.(44)

The Constitution does not expressly mention government contracts, but some guidance can be pieced together. Article I grants Congress “dominant influence over procurement for defence purposes”.(45) Congress’s power encompasses the power to impose and collect taxes “to pay the Debts and provide for the common Defence and welfare of the United States”;(46) to raise and support armies;(47) and to provide and maintain a navy.(48) Article II designates the President as the commander-in-chief of the armed forces,(49) but Congress’s “power of the purse” curtails this authority: “No Money shall be drawn from the Treasury, but in consequence of Appropriations made by law”.(50)

While the Constitution, statutes, and executive orders are surely familiar sources to anyone with even a passing familiarity with U.S. federal law, that a separate common law for government contracts exists may come as a surprise. Laurent explains that “the Federal courts gradually formulated a distinctive system of rules, the federal ‘common law’ of contracts”.(51) This unique body of federal law is composed of treatises, State court rules, and federal precedents on government contracts.(52) The Supreme Court first recognized the existence of this separate corpus of law governing federal public contracts in 1944:

“The validity and construction of contract, through which the United States is exercising its constitutional functions, their consequences on the rights and obligations of the parties, the titles or liens which they create or permit, all present questions of federal law not controlled by the law of any State”.(53)

Two years later, the Supreme Court held that interpreting the meaning of contracts to which the United States is a party “the governing rules of law must be finally declared by this Court”.(54)

What general principles can be drawn from these “constitutional features”?(55) To be sure, this is a “large and complex body of law”(56) and

(44) *Ibid.*, p. 3.

(45) *Ibid.*, p. 1.

(46) U.S. Const., Art. 1, Sec. 8, Cl. 1.

(47) *Ibid.*, Art. 1, Sec. 8, Cl. 12.

(48) *Ibid.*, Art. 1, Sec. 8, Cl. 13.

(49) *Ibid.*, Art. 2, Sec. 2.

(50) *Ibid.*, Art. 1, Sec. 9.

(51) F.W. LAURENT, *Legal Aspects of Defense Procurement*, *op. cit.*, pp. 69-70, 208-209, writing that this common law “had its sources in authoritative text writings, rules adhered to by State courts generally, and precedents developed in prior litigation”.

(52) *Ibid.*, pp. 69, 208.

(53) *United States v. Allegheny County*, 322 U.S. 174, 183, 1944.

(54) *S.R.A., Inc. v. Minnesota*, 327 U.S. 558, 564, 1946.

(55) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 317.

(56) F.W. LAURENT, *Legal Aspects of Defense Procurement*, *op. cit.*, p. 23.

space does not allow a full summary here. But a few of the more distinctive features can be mentioned.

### 2.2.1. Built-in gridlock

Perhaps the most salient feature of U.S. Constitution was that its aim was not efficiency or good government but protection from the tyranny of an over-mighty central government. It was to this end that checks and balances,(57) federalism,(58) and the Bill of Rights(59) were established. Few would disagree that the U.S. Constitution has served this purpose well. But a government set up to foil itself comes at a cost. Compromise is frequently required to carry out business and finding common ground in so large and diverse a republic is devilishly hard. Such a system of deliberate gridlock has predictable results for defense procurement.(60) With reason a *New York Times* columnist infamously wished that America could be China for a day.(61)

### 2.2.2. A strong legislature

Butler posits that the prime example of a U.S. constitutional feature that would require further research “concerns the legislative processes involved in the formulation of procurement and associated legislation”.(62) He continues,

“in the U.S. system of government, Congress exercises a significant impact on all aspects of procurement, its functions ranging from the determination of budgetary appropriations, to the formulation of procurement legislation and the oversight of the procurement function. Inevitably, Congress may, therefore,

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(57) “Checks and balances” refer to the “horizontal” division of power, whereby the executive, legislative, and judicial functions are divided between three competing branches of government. See A.R. AMAR, “Of Sovereignty and Federalism”, *Yale L.J.*, 1987, pp. 1425, 1441-1444. James Madison’s classic formulation of this principle is frequently quoted: “[T]he great security against a gradual concentration of the several powers in the same department consists in giving to those who administer each department the necessary constitutional means and personal motives to resist encroachments of the others. [...] This policy of supplying, by opposite and rival interests, the defect of better motives, might be traced through the whole system of human affairs, private as well as public ... [T]he private interest of every individual may be a sentinel over the public rights”, J. MADISON, *The Federalist*, 9 February 1788, No. 51, pp. 321-322.

(58) Federalism is the “vertical” division of power between the federal government and the States. See A.R. AMAR, “Of Sovereignty and Federalism”, *op. cit.*, pp. 1444-1451.

(59) The bill of rights refers to the first ten amendments that were appended to the Constitution as a condition of ratification and to appease the anti-federalist movement.

(60) D.S. REVERON, N.K. GVOSDEV and M.T. OWENS, *U.S. Foreign Policy and Defense Strategy: The Evolution of an Incidental Superpower*, *op. cit.*, p. 46, borrowing from William Corwin the notion that the Constitution is “an invitation to struggle between the executive and legislative branches” and arguing that this description applies to “control of the military instrument”.

(61) T. FRIEDMAN, *Hot, Flat, and Crowded: Why We Need a Green Revolution – and How It Can Renew America*, New York, Farrar, Straus and Giroux, 2008, pp. 343-370.

(62) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 317.

affect procurement decision-making in a whole host of respects that can impact significantly on the extent to which U.S. federal procurement is accessible to foreign competition as well as the character of procurement legislation.(63)”

His observation is keen. Sometimes the literature talks about defense procurement as if it were purely an administrative function.(64) It is not. Because of its spending power, Congress plays an outsized role in the process.(65) Studies show, for example, that weapons programs live or die based on support in the congressional armed services committees or lack thereof.(66)

### 2.2.3. The centrality of defense

Understanding U.S. federal procurement requires understanding defense procurement; delving into constitutional history will explain why. For the first decade after the Revolution, America had operated under a weak central government under the Articles of Confederation. What led to the passage of a constitution with a stronger federal government? One underappreciated factor was the young nation’s humiliation by pirates operating along the Barbary Coast.

Following America’s break with Great Britain in 1776, her commercial ships no longer sailed under the protection of the Union Jack.(67) And under the

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(63) *Ibid.*, p. 63.

(64) S.L. SCHOONER, *Fear of Oversight: The Fundamental of Businesslike Government*, *op. cit.*, pp. 714-717, criticizing reformers in 1990s for their failure to appreciate some of the fundamental differences between public and private sectors and arguing that the effort to reinvent government so that it would behave more like a business was, therefore, fatally flawed. Schooner cites G.A. CUNEO and E.H. CROWELL, “Impossibility of Performance – Assumption of Risk or Act of Submission?”, *L. & Contemporary Problems*, 1964, pp. 531, 548, who observed that “the myth of the government descending to the market place and negotiating like any other businessman is being slowly exploded”.

(65) Congressional meddling results in pork-barrel spending and the manipulation of the procurement system to favor special interests; in short, “democracy is a messy form of government”. See M. CANCIAN, “Acquisition Reform: It’s not as Easy as it Seems”, *Acquisition Rev. Q.*, Summer 1995, pp. 189, 191-192.

(66) For a good example of how important Congressional support can be, compare how the Marine Corps’s V-22 and the Army’s Crusader programs fared. In the former case, then-Secretary of Defense Dick Cheney repeatedly sought to cancel the V-22 program but was repeatedly thwarted in Congress. Production was distributed among 42 states and predominantly in two large and politically powerful states, Texas and Pennsylvania. The Crusader’s production was less widely distributed and most of the work was to take place in Oklahoma and Minnesota, two less populated states. So Secretary of Defense Donald Rumsfeld succeeded in canceling the Crusader program. See C.M. JONES and K.P. MARSH, “The Politics of Weapons Procurement: Why Some Programs Survive and Others Die”, *27:4 Defense & Security Analysis*, 2011, pp. 359, 364-368. For empirical studies, see U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, pp. 45-47, noting that “Congress is in the business of micromanaging defence programs and their industrial consequences” and the U.S. system “nurtures fierce competition for defence industrial activities among the 50 states and some 455 districts”; B.S. RUNDQUIST and T.M. CARSEY, *Congress and Defense Spending: The Distributive Politics of Military Procurement*, Norman, U. OK Press, 2002, pp. 158-59, finding that the distribution of defense expenditures tracks representation on defense committees; T.L. MCNAUGHER, *New Weapons, Old Politics: America’s Military Procurement Muddle*, Washington, Brookings Institution, 1989, pp. 39-40, 69-70, 166-167, describing the systemic failure of defense procurement resulting from Congress’s constitutional role.

(67) M.B. OREN, *Power, Faith, and Fantasy: America in the Middle East, 1776 to Present*, New York, W.W. Norton, 2007, p. 17.

Articles of Confederation, America lacked a navy of its own to protect itself. This was no small matter for a seafaring nation with its population “[c]oncentrated along the eastern seaboard”.(68) A critical “maritime lifeline” was the route “to the blue water ports of the Mediterranean”,(69) which “represented one of the world’s last remaining spheres free of European domination, where enterprising Americans could still seek their fortunes unchecked”.(70) By the 1770s, one-fifth of America’s exports were bound for this destination.(71) Self-styled mujahedeen hailing from Morocco and the Ottoman regencies of Tripoli, Tunis, and Algiers were kept at bay during the Revolutionary War with the help of the French fleet, but when the “fighting ended in 1783, most of America’s warships had either been captured, sold off, or sunk” and its commercial vessels were therefore easy prey for the Barbary pirates.(72)

In October 1784, corsairs attacked the *Betsy*, a Massachusetts vessel, and took its crew hostage in North Africa; three months later the same fate awaited the *Dauphin* and the *Maria*.(73) America panicked.(74) Previously, they had primarily feared the dangers to liberty that a peacetime military buildup would portend, and so the Articles of Confederation had prohibited national taxation(75) and the formation of a peacetime navy.(76) “It will not be an easy matter, to bring the Americans to act as a nation,” Britain’s Lord Sheffield observed, “America cannot retaliate”.(77)

When the delegates met in Philadelphia in May 1787 to refashion the constitution, they did so “[u]nder the specter of imprisoned sailors in North Africa”.(78) George Washington urged delegates against “talk of chasing the Algerines” until “the wisdom and force of the union can be more concentrated and better applied”,(79) and direct references to the Barbary pirates in the

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(68) *Ibid.*, p. 17.

(69) *Ibid.*, pp. 17-18.

(70) *Ibid.*, p. 18.

(71) *Ibid.*, p. 71.

(72) *Ibid.*, pp. 18-22, quoting Lord Sheffield, “The Americans cannot protect themselves [from the Barbary pirates]; they cannot pretend to a Navy”.

(73) *Ibid.*, p. 22.

(74) *Ibid.*, pp. 22-23.

(75) Articles of Confederation, Art. VIII 1 March 1781, providing that defense expenses be charged to the common treasury supplied by each state.

(76) A.C. McLAUGHLIN, *A Constitutional History of the United States*, New York, Simon, 1935, p. 1068; S. PRAKASH, “Unleashing the Dogs of War: What the Constitution Means by ‘Declare War’”, *Cornell L. Rev.*, 2007, pp. 45, 85-86, noting that Alexander Hamilton complained during the constitutional convention that the Articles of Confederation barred the States from having navies or armies “before war is actually declared”, citing M. FARRAND (ed), *The Records of the Federal Convention of 1787*, New Haven, Yale U. Press, 1966, p. 200.

(77) M.B. OREN, *Power, Faith, and Fantasy: America in the Middle East, 1776 to Present*, *op. cit.*, p. 23.

(78) *Ibid.*, p. 29.

(79) *Ibid.*, p. 29-30.

constitutional convention are few. But James Madison did observe, “Weakness will invite insults”, and “The best way to avoid danger is to be in [a] capacity to withstand it”,<sup>(80)</sup> which no doubt referenced how America should respond to the piracy that was on everyone’s mind.

If the threat from Barbary pirates was downplayed at the convention, it played a more prominent role in the ratification debate.<sup>(81)</sup> Peter Markoe’s satirical novel, *The Algerine Spy*, did its part for the cause, telling of an Algerian agent scouting out America’s defenses, mocking weaknesses that he found, and recommending seizure of Rhode Island.<sup>(82)</sup> Two of *The Federalist Papers* called for a navy to protect U.S. commercial interests<sup>(83)</sup> and a third specifically referenced the North African threat as reason for greater “maritime strength”.<sup>(84)</sup> Such concerns “helped to tip the balance”<sup>(85)</sup> and the new constitution gave Congress the power both to declare war<sup>(86)</sup> and “to provide and maintain a Navy”.<sup>(87)</sup> Thus, wrote historian Thomas Bailey, “In an indirect sense the brutal Dey of Algiers was a Founding Father of the Constitution”.<sup>(88)</sup>

This digression into U.S. constitutional history explains why defense has become so central to U.S. federal procurement: “common defence”<sup>(89)</sup> has been a core purpose of the U.S. federal government since 1789. The EU was formed as a primarily customs union, perhaps with an ulterior motive to foster peace in Europe,<sup>(90)</sup> and seven decades later is still developing a common defense

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(80) *Ibid.*, p. 30.

(81) *Ibid.*, p. 82, quoting Reverend Thomas Thacher of Massachusetts, who argued that the enslavement of “our sailors [...] in Algiers is enough to convince the most skeptical among us of the want of a general government”; Nathaniel Sargent, who called the idea that America could adequately defend itself under the Articles of Confederation from “piracies and felonies on ye high seas” “preposterous”; Hugh Williamson of North Carolina who questioned, “What is there to prevent an Algerine Pirate from landing on your coast, and carrying your citizens into slavery?”; and Kentucky’s George Nicholas, who wrote, “May not the Algerine seize our vessels? Cannot they [...] pillage our ships and destroy our commerce, without subjecting themselves to any inconvenience?”.

(82) *Ibid.*, p. 31.

(83) See A. HAMILTON, *The Federalist*, 23 November 1787, No. 11, at 321-322, warning that without a “federal navy” of “respectable weight” “the genius of the American merchants and navigators [...] would be stifled and lost”; A. HAMILTON, *The Federalist*, 19 December 1787, No. 24, pp. 321-322, writing, “If we mean to be a commercial people, or even to be secure on our Atlantic side, we must endeavor, as soon as possible, to have a navy.”

(84) J. MADISON, *The Federalist*, 19 January 1788, No. 41, pp. 321-322, arguing that a strong central government was necessary to protect America’s “maritime strength” from the “rapacious demands of pirates and barbarians”.

(85) M.B. OREN, *Power, Faith, and Fantasy: America in the Middle East, 1776 to Present*, *op. cit.*, p. 31.

(86) U.S. Const., Art. 1, Sect. 8, Cl. 11.

(87) *Ibid.*, Art. 1, Sect. 8, Cl. 13.

(88) T.A. BAILEY, *A Diplomatic History of the American People*, Upper Saddle River, Prentice-Hall, 1980, p. 65.

(89) U.S. Const., Preamble, stating that the federal government would “provide for the common defence”.

(90) The Schuman Declaration (9 May 1950), available at [europa.eu/european-union/about-eu/symbols/europe-day/schuman-declaration\\_en](http://europa.eu/european-union/about-eu/symbols/europe-day/schuman-declaration_en), accessed 4 July 2019, justified the creation of the European Coal and Steel Community on the basis of eliminating the rivalry between France and Germany:

policy.(91) The United States's founding, by contrast, centered on a Hobbesian bargain for mutual protection from monsters abroad(92) (pace John Quincy Adams).(93)

This foundation led to a procurement system dominated by defense. Joshua Schwartz has observed, "it would require a willful blindness to the main currents of United States history to miss the fact that military and defense contracting has played the central role in the United States's federal procurement system".(94) The salience of defense has led to an "exceptionalist flavor" in that system.(95) Schwartz lists termination for convenience,(96) the *Christian* doctrine,(97) the sovereign acts and unmistakability doctrines,(98) and the deferential standard of review in bid protests(99) among the unique doctrines and practices that share a military lineage.(100) These are among the core doctrines that distinguish public and private contract law in the United States.

This close connection between defense procurement and federal procurement generally has given rise to a feature that Christopher Yukins considers a model for duplication abroad – namely, that there is no divide between military

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"The solidarity in production thus established will make it plain that any war between France and Germany becomes not merely unthinkable, but materially impossible".

(91) H. KRIEGER, "Common European Defence: Competition or Compatibility with NATO?", in *European Security Law* (M. TRYBUS and N. WHITE eds), Oxford, OUP, 2007, pp. 174, 178, contrasting Member States' extensive economic cooperation with their unwillingness "to transfer any sovereignty in defence matters".

(92) The Barbary pirates were not the colonies' first common enemy. They had united against foreign foes in the French and Indian War (known in Europe as the Seven Years' War) and, of course, in the Revolutionary War. During the latter, at the signing of the Declaration of Independence, Benjamin Franklin famously quipped, "We must, indeed, all hang together or, most assuredly, we shall all hang separately". Three decades of conflict with French, British, and North African powers led America's founders to establish a constitutional order that would include a common defense at its core.

(93) J.Q. ADAMS, "Address of July 4, 1821", *op. cit.*, p. 45, observing that America "goes not abroad in search of monsters to destroy".

(94) J.I. SCHWARTZ, "The Centrality of Military Procurement: Explaining the Exceptionalist Character of United States Federal Public Procurement Law", Washington, GW Law Faculty Publications & Other Works, Paper 1077, 2004, [scholarship.law.gwu.edu/faculty\\_publications/1077](http://scholarship.law.gwu.edu/faculty_publications/1077), p. 51.

(95) *Ibid.*, p. 53.

(96) *Ibid.*, pp. 55-65, citing *United States v. Corliss Steam-Engine Co.*, 91 U.S. 321, 1875.

(97) J.I. SCHWARTZ, "The Centrality of Military Procurement: Explaining the Exceptionalist Character of United States Federal Public Procurement Law", *op. cit.*, pp. 66-68, citing *G.L. Christian & Assoc. v. United States*, 312 F.2d 418, Ct. Cl., 1963, cert. denied, 382 U.S. 821, 1965.

(98) J.I. SCHWARTZ, "The Centrality of Military Procurement: Explaining the Exceptionalist Character of United States Federal Public Procurement Law", *op. cit.*, pp. 68-79, citing *Deming v. United States*, 1271 Ct. Cl. 190, 1865, appeal dismissed, 76 U.S. (9 Wall) 145, 1870; *Jones v. United States*, 128 1 Ct. Cl. 383, 1865.

(99) J.I. SCHWARTZ, "The Centrality of Military Procurement: Explaining the Exceptionalist Character of United States Federal Public Procurement Law", *op. cit.*, pp. 79-80, citing *M. Steinthal & Co. v. Seamans*, 455 F.2d 1289, 1298-1299, 1300-1306, D.C. Cir., 1971.

(100) Schwartz lists several other examples of "military-derived exceptionalism" in U.S. federal procurement doctrine, including the strict compliance doctrine, the right to submit change orders, competitive negotiation procedures, the cost-reimbursement contracting method, and the government contract defense. J.I. SCHWARTZ, "The Centrality of Military Procurement: Explaining the Exceptionalist Character of United States Federal Public Procurement Law", *op. cit.*, pp. 80-82.

and civil procurement in the United States.(101) In private correspondence with Martin Trybus, Yukins elaborated on the benefits of this integrated public procurement system:

“The practical effect of this is that the Defense Department and the civilian agencies share lessons learned in developing new regulations and implementing old ones, and it is quite easy for trained procurement personnel to move between the civilian and military worlds. When there are difficult debates over regulatory reform – such as the debate over how to handle organizational conflicts of interest – the exchanges between the Defense Department (which handles the majority of U.S. federal procurement, by dollar value) and the civilian agencies (which tend to be more nimble and entrepreneurial) can be quite useful”.(102)

The United States’s favorable experience with an integrated system suggests that abolition may be the best course for the EU’s separate defense procurement regime.(103) The benefits of such a monistic system have been recognized elsewhere.(104) A contrary view is touched upon in Section 4.1.

### 2.3. Law

The U.S. federal procurement laws that could affect transatlantic trade are voluminous. These include not only “internal” laws on the operation of the procurement system(105) that may be off-putting to foreign vendors(106) but also “external” laws that regulate relations with foreign buyers and sellers in various ways.(107) Concerning the latter, this essay assumes a hypothetical world in which the TTIP has passed and overt barriers have been removed.

(101) C.R. YUKINS, “Barriers to International Trade in Procurement After the Economic Crisis, Part II: Opening International Procurement Markets: Unfinished Business”, *West Government Contract Year in Review Covering 2010* (2011), Int’l 2–10, Int’l 2–18, Washington, GW Law Faculty Publ., 2011. He writes: “policymakers may wish to address the regulatory divide between civilian and defense procurement systems. Systems around the world are beginning to close that traditional divide, and there are substantial arguments, including lower transaction costs, reduced corruption, and enhanced professionalism, to press for uniformity across civilian and military procurement systems. The GPA is not yet a ready means of achieving that uniformity across domestic and military systems, but it could be pointed in that direction”. *Ibid.*

(102) Correspondence dated 8 April 2016, on file with author.

(103) *Ibid.*, replying to Trybus’s query about the merits of the Defence Directive: “abolish it!”.

(104) See *Guide to Enactment of the UNCITRAL Model Law on Public Procurement*, 2014, par. 46-49, explaining that the current version of the model law “brings national defence and national security sectors, where appropriate, into the general ambit of the Model Law so as to promote a harmonized legal procurement regime across all sectors in enacting States, and to enable all procurement to benefit from the Model Law’s provisions.”

(105) These internal laws are much more than the FAR. They include the Constitution, statutes, the federal common law for government contracts, and executive orders. See above Section 2.2.

(106) See C.R. YUKINS and S.L. SCHOONER, “Incrementalism: Eroding the Impediments to a Global Public Procurement Market”, *op. cit.*, p. 558, arguing foreign procurement systems “raise practical barriers to entry as foreign vendors run headlong into dense and alien procurement regimes”.

(107) External laws would include the Buy American Act, the Berry Amendment, and the Trade Agreements Act, as well as the export control regulations and restrictions on foreign acquisitions discussed below.

Regardless, the effect of such overt barriers is limited for most European countries.(108) Some examples of the internal and external laws in question are considered below.(109)

### 2.3.1. Internal federal procurement laws

It is worth considering, Butler suggests, that “the ways in which foreign access may be affected even within a legal framework of ostensibly full and open competition that does not impose specific legal limitations on foreign participation”.(110) Certainly procurement authorities’ discretion could be abused in a variety of ways to deliberately exclude foreign competition.(111) But the examples considered here concern inadvertent and unintentional discrimination.

U.S. federal government contracting is fraught with peril for the uninitiated – and not only for foreign firms but also for domestic firms with little experience competing for federal government contracts and for counsel who are inexperienced at the government contracts bar.(112) For example, requests for proposals use the jargon of technical military specifications that only a few privileged vendors fully comprehend.(113) Timely filing of bid protests is another example; even domestic firms inexperienced with federal government contract litigation are sometimes caught unaware of various traps and miss unforgiving filing deadlines.(114)

(108) See J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, op. cit., p. 91, noting that “despite constant Congressional Buy American pressures, formal domestic content rules are not by and large a major factor in defense markets” and that these laws “are more important symbolically than in practice”. Cf. D. PIOTT, “The ‘TTIP-ing Point’: How the Transatlantic Trade and Investment Partnership Could Impact European Defence”, 48:3 *Int’l Spectator*, 2013, pp. 15, 17, observing that a “web of protection presently marks transatlantic defence markets”.

(109) If the reader finds the internal/external terminology disagreeable, Trepte offers corresponding terminology that perhaps better captures the dichotomy between laws that apply differently to foreign and domestic vendors: distinctly and indistinctly applicable laws. P. TREPTE, *Public Procurement in the EU: A Practitioner’s Guide*, 2nd ed., Oxford, OUP 2007, pp. 330-331.

(110) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, op. cit., pp. 276-277.

(111) *Ibid.*, pp. 277-279, suggesting that requests for proposals could be rigged to favor domestic firms; *ibid.*, pp. 281-802, noting that the time limit for proposals could be shortened to minimize the competition.

(112) J.S. PRZEMIENIECKI, *Acquisition of Defense Systems*, Wright-Patterson, Air Force Institute of Technology, 1993, p. 174, claiming that it should be apparent “that Government contracting is highly regulated, fraught with peril to the legally uninitiated”.

(113) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, op. cit., pp. 283-284, reporting that the DoD is moving away from military-specific specifications and toward commercial standards.

(114) M.J. NAVARRE, “GAO Reminds Offerors of Timeliness Traps for the Unwary”, Steptoe & Johnson, 28 April 2016, [www.steptoelaw.com/publications-11230.html](http://www.steptoelaw.com/publications-11230.html), explaining that a disappointed offeror’s failure to protest right after being eliminated from the competitive range rendered the subsequent protest untimely; M.D. MALONEY, “Agency’s ‘Brief Explanation’ Was a Trap for Unwary Protester”,

Butler observes that procurement officials' discretion "is likely to be the primary cause of foreign discrimination and the most significant barrier to transatlantic defense trade".(115) Surely he is right. This section barely scratches the surface of ways in which the federal acquisition system's byzantine legal framework may deter foreign competition.

### 2.3.2. External federal procurement laws

The Buy American Act and Berry Amendment are perhaps the most notorious external laws affecting the transatlantic defense trade, but they are mostly waived for NATO partners.(116) Other external laws, though lesser known, may have a greater effect. Their motives range from national security to protectionism.(117) Two of these merit special consideration – both because of their significant influence on transatlantic trade and because their connection to national security could shield them from the TTIP.

The first is not a single law, but a body of laws and regulations controlling technology exports. These are perhaps the most significant obstacle to transatlantic defense trade.(118) The worst offender is the International Traffic in Arms Regulation (ITAR), which has been called the "the largest inhibitor of the transatlantic defence trade".(119) ITAR has long delayed and even "actively denied... European firms from entering the US market".(120) ITAR was designed to prevent transfers of critical technology to America's enemies, but it has a perverse effect on trade as European firms design around or out U.S. components or subsystems to avoid entanglements with ITAR.(121)

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Denver, Holland & Hart, *GovCon Insider*, 29 May 2015, holding that whether a protest period is mandatory or discretionary determines whether the period for filing bid protest is tolled.

(115) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 310-311.

(116) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defence Market and the Implications for U.S. National Security*, *op. cit.*, p. 91.

(117) Defense Science Board, *Final Report of the Task Force on Globalization and Security*, 1999, p. 14, observing that the "complex and often politically motivated statutes underlying the FAR and DFARS often restrict DoD's ability to purchase" from foreign suppliers.

(118) U.S.-Crest, "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries", *op. cit.*, p. 47, naming technology and security control policies as "the biggest inhibitors" of transatlantic defense trade; *Ibid.*, p. 50, reporting that the European defense industry considers these policies the "first inhibitor to greater transatlantic defence trade flow."

(119) *Ibid.*, p. 68. See also L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 212, noting that ITAR "has been the subject of extensive criticism in light of the perception of excessive controls, extensive delays, and resulting risks impacting on the global competitive position of US contractors."

(120) D. FIOTT, "The 'TTIP-ing Point': How the Transatlantic Trade and Investment Partnership Could Impact European Defence", *op. cit.*, p. 17, quoting D. MOORE *et al.*, "U.S. Export Controls and Technology Transfer Requirements – A United Kingdom Perspective", *Int'l J. Defense Acquisition Management*, 2010, pp. 24, 43.

(121) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defence Market and the Implications for U.S. National Security*, *op. cit.*, pp. 16, 20. See also U.S.-Crest, "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries",

The Obama administration updated the ITAR control lists in 2013, moving control of some technologies from the State Department to the Commerce Department.(122) Although a welcome reform, this did not entirely solve the problem.(123)

The second item deserving special treatment is the Committee on Foreign Investment in the United States (CFIUS), which regulates foreign purchases of U.S. companies based on national security. European experience suggests “the best and arguably the only sustainable model to do business with the DoD is not to export European products to the US but to set up US subsidiaries”(124) or to affiliate with a U.S.-based contractor through mergers and acquisitions.

The perception is that CFIUS discourages foreign purchases of U.S. companies.(125) At least one study suggests that this perception may be inaccurate based on several examples of foreign investors being allowed to purchase U.S. defense firms,(126) though mere proof that foreign investors are sometimes

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*op. cit.*, p. 52, noting that ITAR is a “double edged sword” because manufacturers go out of their way “to avoid using American technology when it is not indispensable simply to avoid a costly and cumbersome ITAR process”. Europeans designing around U.S. technology has had two knock-on effects. First, second- and third-tier U.S. defense firms are being replaced by European competitors who are ITAR-free. N. TUSHE, “U.S. Export Controls: Do They Undermine the Competitiveness of U.S. Companies in the Transatlantic Defense Market”, *Pub. Cont. L.J.*, 2011, pp. 57, 70-72. Second, restrictive export controls have “chilled collaboration on defense and technology matters with even our closest allies” and “eroded trust with traditional partners”. *Ibid.*, p. 72.

(122) See Bureau of Industry and Security, Department of Commerce, *United States Export Reform Initiative*, 2013, [www.bis.doc.gov/index.php/forms-documents/pdfs/1094-ecr-brochure-nov-14-2014/file](http://www.bis.doc.gov/index.php/forms-documents/pdfs/1094-ecr-brochure-nov-14-2014/file), explaining that on 16 April 2013 the U.S. Departments of Commerce and State published the Export Control Reform (ECR), which transferred jurisdiction over thousands of items from the Department of State’s ITAR to the Department of Commerce’s Export Administration Regulations, which expedited review of items “that do not provide a critical military or intelligence capability”.

(123) M.A. GOLDSTEIN, “Status and Adverse Consequences of U.S. Export Control Reform”, 3:6 *Thomson Reuters Practical Trade & Customs Strategies*, June 2014, available at [goldsteinpllc.files.wordpress.com/2014/07/thomson-reuters-ecr-article-july2014.pdf](http://goldsteinpllc.files.wordpress.com/2014/07/thomson-reuters-ecr-article-july2014.pdf), p. 6, explaining that while the ECR made thousands of control list transfers, it needlessly increased the complexity of the process by unhitching the regulation from the statute.

(124) U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 35.

(125) S. DE VAUCORBEIL, “Reforming the Transatlantic Defence Market”, in *The Estonian Foreign Policy Yearbook* (A. KASEKAMP ed), Tallin, Estonian Foreign Policy Institute, 2008, pp. 115, 122, reporting that Member States are concerned about U.S. ownership in European defense companies because “US defence companies have been protected from much foreign investment by law”; A. ASHBORNE, “Introduction”, in *Europe’s Defence Industry: A Transatlantic Future?*, *op. cit.*, pp. 1, 5, complaining that U.S. “legal and structural obstacles [...] would make any transatlantic mergers extremely difficult to undertake”; Defense Science Board, *Final Report of the Task Force on Globalization and Security*, *op. cit.*, pp. 16-17, noting that a “consistent complaint” among Europeans is that the “DoD’s policy on major cross-border defense industry mergers and acquisitions is unclear”.

(126) U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 8, reporting that “CFIUS does not appear to be a barrier to European investments in the United States”, *ibid.*, p. 33, noting that in 2007 CFIUS approved “at least 14 cases involving critical defense technology for a total value of 55 B\$”.

allowed to buy U.S. defense firms is inconclusive. Further, even if CFIUS ultimately approves a transaction, evidence suggests that the process can unduly delay foreign investments, and the timing “is often critical to the financial viability of the transaction”.(127)

Interest in U.S. restrictions on foreign investments increased following the 2006 Dubai Ports affair and passage of the Foreign Investment and National Security Act of 2007.(128) Dubai Ports concerned the purchase of a U.S. port operator by a Middle Eastern firm. Both CFIUS and the President initially approved the transaction but their approval was withdrawn following a public outcry.(129) The 2007 Act expanded CFIUS’s review process beyond defense firm to include “critical infrastructure”.(130) Since 2006, available data indicate that there has been a track record of “increased CFIUS scrutiny of foreign acquisitions”.(131) “What is missing from the data”, however, “are the acquisitions not pursued because of foreign firms’ awareness of the U.S. government’s policies in this area”.(132)

A bellwether of the transatlantic defense trade “concerns the ability to buy into a foreign market through mergers and acquisitions of domestic companies”.(133) Perhaps in part because of CFIUS and related restrictions, there are not “any truly ‘transatlantic’ defense companies comprising multiple nationalities”(134), nor have there been any major transatlantic mergers in recent years.(135)

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(127) Defense Science Board, *Final Report of the Task Force on Globalization and Security*, *op. cit.*, pp. 17-18.

(128) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 676.

(129) *Ibid.*, p. 130.

(130) *Ibid.*, pp. 676-677.

(131) *Ibid.*, pp. 679-680.

(132) *Ibid.*, p. 681, reporting that the authors have anecdotal experience “with a number of these case in the defense industry”, where “foreign firms chose not to proceed on their own in light of their awareness of U.S. policies”.

(133) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 63-64, reporting that the Clinton administration’s support for European investors’ acquisitions led to an uptick in the 1990s, that European acquisitions of U.S. defense firms dropped in the aftermath the 9/11 attacks (2001-04), and then increased again in 2004-08.

(134) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 80. BAE Systems is an outlier; however, its relationship with the United States is bilateral – a British vendor doing business mainly with the United States. Thus, Butler’s claim that there is not a *multinational* transatlantic firm holds.

(135) *Ibid.*, p. 86. Though there is a dearth of multinational defense firms in the north Atlantic and there have been few transatlantic mergers of late, there is evidence of European defense firms’ organic growth in the U.S. market. Indeed, European firms “are achieving an increasing degree of market access through investment and organic growth in the US” and that such growth is “typically achieved through partnering with, or sales to, U.S. primes rather than directly to the US DoD”, *ibid.*, p. 137.

### 3. Defense Procurement in the European Union

As the last section did for the United States, this section identifies and describes the constitutional features of EU defense procurement<sup>(136)</sup> and breaks this into history, constitution, and law. The hope is that a better understanding the two systems may help bridge the gap, especially for American firms considering whether to compete for European defense contracts.

#### 3.1. History

“Since the long-headed men first drove the short-headed men out of the best land in Europe”, wrote Walter Bagehot, “all European history has been the history of superimposition of the more military races over the less military”.<sup>(137)</sup> Intra-European Union rivalry is emblematic of the continent’s tumultuous history.<sup>(138)</sup> With three millennia of recorded history to cull from, what follows highlights a few points relevant to defense procurement.<sup>(139)</sup> This starts with the modern conception of the nation State, considers the Second World War and the Cold War that followed, and concludes with a preliminary sketch of the Post-Cold War environment.

##### 3.1.1. The Treaty of Westphalia

“The Treaty of Westphalia”, writes Norman Davies, “set the ground plan of the international order in central Europe for the next century and more”.<sup>(140)</sup> The ravages of the Thirty Years War (1618-1648)<sup>(141)</sup> concluded with the signing of a historic document that signaled the first recognition of the modern nation State.<sup>(142)</sup> Westphalia “symbolically indicated a sea-change in inter-

(136) *Ibid.*, p. 438.

(137) W. BAGEHOT, *Physics and Politics* (first published 1872), Chicago, Ivan R. Dee 1999, p. 46. Long- and short-headed referred to the now discredited cephalic index that was used by anthropologists to categorize the human populations.

(138) N. DAVIES, *Europe: A History*, Oxford, OUP, 1998, pp. 15-16, observing in his magisterial tome that one should not “forget the sorry catalogue of wars” that have “dogged every stage of the tale”.

(139) “The best history”, Bagehot said, “is like the art of Rembrandt; it casts a vivid light on certain selected causes, on those which were best and greatest; it leaves all the rest in shadow and unseen”. W. BAGEHOT, *Physics and Politics*, *op. cit.*, p. 56.

(140) N. DAVIES, *Europe: A History*, *op. cit.*, p. 565.

(141) *Ibid.*, p. 568, recounting that Germany, the epicenter of the conflict, “lay desolate” with its population falling from “21 million to perhaps 13 million” and “[b]etween a third and half of the people dead” and that “Germany was not alone in its misery” as a “concatenation of catastrophes” befell Spain, France, England, Poland-Lithuania, and Sweden.

(142) The signing of the Treaty of Westphalia is shorthand in two senses. First, two treaties were signed in 1648, the Treaties of Münster and Osnabrück, which “taken together are known as the Peace of Westphalia”. Second, these two treaties memorialized incremental changes to the international order that had been slowly evolving over 150 years. See C. BROWN, “Sovereignty, Rights, and Justice: International Political Theory Today”, *Polity*, 2002, p. 22.

national organisation – the transition to a system of modern States”.(143) It “paved the way for a system of States to replace the hierarchical system under the leadership of the Pope and the Hapsburg families that linked the Holy Roman and Spanish Empires”.(144) While this treaty recognized several principles of international law,(145) two are of most interest here: sovereignty and the nation State’s right to self-defense.(146)

These two principles are closely related. Sovereignty is bound up with a State’s capacity to defend itself. In the modern age, where weaponry matters as much as manpower, the State’s capacity for self-defense depends on its internal industrial base.(147) It was not always so. In mediaeval times, private armies employed “foreign armourers, gunsmiths, and shipwrights”.(148) It was not until the 16<sup>th</sup> century that “domestic monopolies in the production of weapons and munitions” became the norm.(149) Perhaps the coincidence with the creation of the modern State was no accident.(150) Newly sovereign States sought a monopoly on the legal use of force.(151)

(143) C. HARDING and C.L. LIM (eds), “The Significance of Westphalia: An Archaeology of the International Legal Order”, in *Renegotiating Westphalia: Essays and Commentary on the European and Conceptual Foundations of Modern International Law*, New York, Springer, 1999, pp. 1, 5-6.

(144) K.J. HOLSTI, *Peace and War: Armed Conflicts and International Order, 1648-1989*, Cambridge, CUP, 1991, pp. 25-26.

(145) The Treaty of Westphalia stands for such principles as sovereign immunity, equality among States, non-intervention, and non-aggression; it also recognized procedural rules “governing the practice of diplomacy and such matters as the making of treaties”. See C. BROWN, “Sovereignty, Rights, and Justice: International Political Theory Today”, *op. cit.*, pp. 22, 35.

(146) *Ibid.*, p. 33, explaining that Westphalia enshrined the rule that “the balance of power may just be preserved by preventative war”. Westphalia codified what was the prevailing view among the founders of international law. See H. GROTIUS, *The Rights of War and Peace* (1st publ. 1625), A.C. CAMPBELL tr., New York, M. Walter Dunne, 1901, bk II, ch I, P XVI, holding that notwithstanding the differences between persons and States, right of self-defense of persons may be “applied to public hostilities, allowing for the difference of circumstances”; E.D. VATTEL, *The Law of Nations* (1st publ. 1758), Joseph CHITTY tr., Philadelphia, Johnson, 1844, bk 2, ch 4, p. 154, writing, “Every nation, as well as every man, has, therefore, a right to prevent other nations from obstructing her preservation, her perfection, and happiness – that is, to preserve herself from all injuries”. Indeed, “the right of self-defense is one of the oldest legitimate reasons for States to resort to force” under customary international law. A.C. AREND and R.J. BECK, *International Law & the Use of Force: Beyond the UN Charter Paradigm*, London, Routledge, 1993, p. 72, citing Aristotle, Aquinas, *et al.*

(147) See J. MAWDSLEY, “The Gap Between Rhetoric and Reality: Weapons Acquisition and ESDP”, Paper 26, Bonn, International Center for Conversion, 2002, pp. 4-5, arguing defense firms and the nation State have a “symbiotic relationship”, that a nation’s defense production “touches the heart of the concept of sovereignty”, and that “[w]ithout weapons to defend its territorial sovereignty [...] a State cannot truly be sovereign”.

(148) M. EDMONDS, “International Military Equipment Procurement Partnerships: The Basic Issues”, *op. cit.*, pp. 1, 3.

(149) *Ibid.*, p. 150.

(150) If modern European States’ pursuit of self-sufficiency in arms production did not occur in precisely 1648, neither did the Westphalian reforms happen all at once. See *ibid.*, p. 144.

(151) M. WEBER, “Politics as Vocation”, in *From Max Weber: Essays in Sociology* (H.H. GERTH and C. WRIGHT MILLS (eds and trs) (1st publ. 1946), London, Routledge, 1998, p. 78, defining a State as a group that successfully “claims the monopoly of the legitimate use of physical force within a given territory” (emphasis original).

Even free market advocates like Adam Smith favored protection of strategic industries.(152) Whatever the rationale, economic or otherwise, European powers sought defense autarkies for the three centuries after Westphalia.

### 3.1.2. Cold War

Following two devastating world wars(153), where the Allied powers were uncomfortably reliant on imported war material, and with a mounting Soviet threat on its doorstep,(154) Europe spent generously on defense, favoring “autonomous weapons policies”.(155) After watching the United States abandon France and Britain during the Suez crisis,(156) the lesson was learned: “great stress was placed on security of supply, and defense industries everywhere were regarded as prized national assets” and Member States “retained exceptional freedom to pursue autarkic policies”.(157) The “instinct in every country in the years following World War II was to internalize the development and manufacture of military equipment”.(158) “[N]o real ‘European’ defense market” existed at the close of the Cold War.(159)

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(152) A. SMITH, *The Wealth of Nations* (1st publ. 1776), New York, Knopf 1991, pp. 405, 461-462, advocating that Great Britain should offer bounties for military necessities such as gunpowder and sail-cloth because “it might not always be prudent to depend upon our neighbours for the supply.”

(153) See A. HERMAN, *Freedom’s Forge: How American Business Produced Victory in World War II*, New York, Random House, 2012, pp. 125-127, 166-167, 216-219, describing the Allies’ humiliating reliance on U.S. industry when their own resources proved inadequate; A. ROBERTS, *The Storm of War, A New History of the Second World War*, New York, Harper, 2010, pp. 352-354, arguing that Hitler might have pushed Britain out of the war had he recognized the potential of U-boats and Britain’s dependence on imports (“It was to be one of his greatest blunders of the war”).

(154) W. WALKER and P. GUMMETT, “Nationalism, Internationalism, and the European Defence Market”, 9 *Chaillot Papers*, Pretoria, Institute for Security Studies, 1993, p. 10, writing that in the post-war years that “the international conflicts of the previous decades cast long shadows”.

(155) See A. GOLDSTEIN, “Discounting the Free Ride: Alliances and Security in the Postwar World”, 49 *Int’l Organization*, 1995, pp. 39, 63, 65, reporting that after Suez the UK and France decided they “could not count on adequate U.S. backing unless vital American interests were at stake” and planned their strategies accordingly.

(156) See N. STONE, “The Atlantic and its Enemies: A History of the Cold War”, *Basic*, 2010, pp. 136-142, summarizing the Suez crisis and its aftermath.

(157) W. WALKER and P. GUMMETT, “Nationalism, Internationalism, and the European Defence Market”, *op. cit.*, pp. 10-11.

(158) *Ibid.*, p. 11.

(159) N. TUSHE, “U.S. Export Controls: Do They Undermine the Competitiveness of U.S. Companies in the Transatlantic Defense Market?”, *op. cit.*, pp. 57, 63.

### 3.1.3. Post-Cold War

With communism's demise, defense budgets plummeted.<sup>(160)</sup> EU Member States initially opposed industry consolidation.<sup>(161)</sup> Instead, their defense firms sought exports to spread costs. With the U.S. market largely closed off due to protectionist tendencies,<sup>(162)</sup> their efforts concentrated on the Middle East and developing countries.<sup>(163)</sup> European firms succeeded in some measure and exports lessened their defense spending burdens.<sup>(164)</sup> But EU firms were not alone in this effort, which tightened margins.<sup>(165)</sup> Sharpening

(160) See S.G. NEUMAN, "Defense Industries and Global Dependency", *Orbis*, Summer 2006, pp. 429, 435, reporting that defense budgets had fallen by almost one third; J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, pp. 46-47, noting that European spending dropped after the Cold War, that it has not recovered despite post-9/11 threats, and that much of Europe has been generally "debellicized".

(161) See B. SCHMITT, "From Cooperation to Integration: Defence and Aerospace Industries in Europe", in *Chaillot Papers*, Pretoria, Institute for Security Studies, 2000, pp. 13-14, 59-60, recounting Europe's belated transnational cooperation and consolidation; J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, pp. 180-181, describing Europe's slow move "away from buying national and national champions"; R. HOOKE, *The Defence Industry in the 21st Century*, London, Price Waterhouse Coopers, 2005, p. 14, [https://www.pwc.pl/en/publikacje/defence\\_industry\\_ads.pdf](https://www.pwc.pl/en/publikacje/defence_industry_ads.pdf), accessed 4 July 2019, reporting that the United States led the way as to consolidation.

(162) Because the United States is the biggest spender, penetrating the U.S. market is critical to EU defense firms' survival. See W. WALKER and S. WILLETT, "Restructuring the European Defence Industrial Base", *Defence Economics*, 141, 1993, pp. 154-156; J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 133, writing that the long-term survival of European defense firms hinges on their competition with U.S. defense firms. The challenge is that the United States maintains nearly an autarky in defense. See E. KLEPSCH, *Two-way Street: USA-Europe Arms Procurement*, London, Brassey's, 1978, p. 36, quoting P. DANKERT, "A European Armaments Policy", Assembly of the Western European Union, 23rd Sess., Part 1, Doc. 738, 10 May 1977, p. 17, reporting that "So far the United States has persisted, both for strategic reasons and as a result of political and industrial pressure, in a policy of near autarky in weapons procurement". Thus far EU firms have had little success at penetrating the United States. See U.S. Department of Defense, Office of the Deputy Undersecretary of Defense for Industrial Policy, "Study on Impact of Foreign Sourcing Systems", June 2004, pp. 33-35, reporting that in fiscal year 2002 only 4% of total Pentagon procurement went to foreign sources and less than 1% of that to military hardware. But European firms are pursuing "the American option" by using subcontracting, joint ventures, mergers and acquisitions, and buyouts. See S.G. NEUMAN, "Defense Industries and Global Dependency", *op. cit.*, pp. 443-445.

(163) See W. WALKER and S. WILLETT, "Restructuring the European Defence Industrial Base", *op. cit.*, pp. 154-156, explaining that European defense firms turned to developing countries and the Middle East in particular. European firms depend on exports far more than their U.S. rivals. See J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 132, reporting that whereas European firms receive 66-75% of revenues from non-domestic sources, U.S. firms typically derive only 15-30% from exports.

(164) C.H. ANDERTON, "Economics of Arms Trade", in *Handbook of Defense Economics: Defense in a Globalized World* (K. HARTLEY and T. SANDLER eds), Vol. 1, Amsterdam, North-Holland, 1995, pp. 523, 540.

(165) See T. GUAY and R. CALLUM, "The Transformation and Future Prospects of Europe's Defence Industry", *Int'l Affairs*, 2002, pp. 757, 765, explaining that the post-Cold War arms market "has become both crowded and severely competitive".

the competition even further was the end of Cold War subsidies; importing countries now paid full price and became more demanding customers.(166)

Exports alone could not close the gap. Due to a “changed operational and political context, reduced budgets, industrial over-capacity, duplication between domestic industries, lack of standardization, and dependence” on the United States,(167) the market was transformed, from “a collection of medium-sized, nationally oriented firms to one dominated by two giants, with several smaller firms closely linked to these leaders”.(168) Despite this consolidation,(169) Europe’s defense industry remains protected and fragmented.(170)

### 3.2. Constitutional features

Though “constitutional features” may primarily evoke the EU treaties, this expression is used in a broader sense.(171) It includes the politics, practices, and cultural assumptions that underlie EU defense procurement. And at this level, “there is currently a fundamental debate as to the purposes” of the procurement directives: that is, whether they are solely to promote the internal market or are also to promote competition.(172)

First, a word about the EU legal system is in order. Defense procurement must comply with the general principles set forth in the treaties, unless an exclusion applies.(173) These general principles include non-discrimination based on nationality, transparency, proportionality, and equal treatment.(174) While the Article 346 exemption has been commonly invoked in the past, the

(166) C.H. ANDERTON, “Economics of Arms Trade”, *op. cit.*, pp. 532-533.

(167) B. HEUNINCKX, “Defence Procurement and the European Defence Equipment Market: The Virtues of Kissing the Frog”, *Procurement L.J.*, 2015, pp. 319, 336.

(168) T. GUAY and R. CALLUM, “The Transformation and Future Prospects of Europe’s Defence Industry”, *op. cit.*, pp. 757, 761-762, describing the political pressure for rationalization of the U.S. defense industry in the 1990s and how this, in turn, affects the European defense industry.

(169) Europe’s consolidation should not be overstated. The EU has never undergone the same degree of consolidation that the United States underwent in the 1990s. See M. STAPLES, *The Future of European Defence: Tackling the Productivity Challenge*, New York, McKinsey & Company, 2013, explaining, “The European defence industry has integrated to a degree but remains fragmented”. Europe is still “a series of atomistic defence procurement markets”. P. TREPTE, *Public Procurement in the EU: A Practitioner’s Guide*, *op. cit.*, pp. 241-242.

(170) B. HEUNINCKX, “Defence Procurement and the European Defence Equipment Market: The Virtues of Kissing the Frog”, *op. cit.*, p. 336, writing that the EU defense market “is still very much in a misshapen state” and maintaining that it “has evolved into a difficult relationship between cash-strapped buyers in an oligopsony position that are hardly able to drive the market as they did earlier, and a defence industry finding itself caught between an uneasy survival as a cluster of protected entities fragmented along national lines and an evolution into an oligopoly at the European level”.

(171) See L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 438.

(172) *Ibid.*, pp. 255-256 (citations omitted).

(173) See P. TREPTE, *Public Procurement in the EU: A Practitioner’s Guide*, *op. cit.*, pp. 239-240.

(174) *Ibid.*, pp. 5-6, 13-27; S. ARROWSMITH, *The Law of Public Utilities and Procurement: Regulation in the EU and UK*, Vol. I, London, Sweet & Maxwell, 2014, pp. 262-279, 301-302, 628-632.

European Court of Justice has tightened down the use of this exemption.<sup>(175)</sup> And because the Defence Directive creates a separate system for defense, use of Article 346 will be increasingly unnecessary.<sup>(176)</sup> Lastly, the Directives are separately implemented in each State's domestic legislation; and it is, of course, at the Member State level where the vast majority of defense procurement happens.

### 3.2.1. Protectionism and fragmentation

Member States collectively maintain the second largest military in the world and spent €203 billion on defense in 2015;<sup>(177)</sup> however, the EU achieves less “bang for its buck” than does the United States.<sup>(178)</sup> That is in part due to fragmentation and protectionism.<sup>(179)</sup> For example, one study conducted in 2005 indicated that 80% of the Member States' budgets were spent on defense materiel from domestic suppliers and only 13% came from other Member States.<sup>(180)</sup>

The EU is not alone. What has been described are widespread problems in defense economics. “In defense procurement”, two defense economists explain, “preferential purchasing and tariff protection represent government-created

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(175) See B. HEUNINCKX, “Security of Supply and Offsets in Defence Procurement: What's New in the EU?”, *PPLR*, 2014, pp. 33, 39, summarizing the ECJ's jurisprudence on the Art. 346 exemption: it concerns only “exceptional and clearly defined cases”; there is no “general exception”; it is “interpreted strictly”; appeals to security are limited cases where there is “a genuine and sufficiently serious threat to a fundamental interest of society”; “aims of a purely economic nature” do not suffice; Member States enjoy a “particularly wide discretion in assessing the needs receiving protection”, but mere reliance on such interests are insufficient; security “interests have to be specifically expressed”; and for a measure to be necessary to an essential security interest, States must show that “such protection could not have been addressed by a less restrictive measure” (internal citations omitted).

(176) See T. BRIGGS, “The New Defence Procurement Directive”, *PPLR*, 2009, NA 129, NA 130, explaining that the objective of the Defence Directive was “to reduce unjustified reliance” on Art. 346 “by providing a bespoke procurement regime in the field of defence and security”; M. TRYBUS, *Buying Defence and Security in Europe: The EU Defence and Security Procurement Directive in Context*, Cambridge, CUP, 2014, p. 253, explaining that one purpose was to “accommodate most national security needs of the Members States” and thereby “the need to derogate from the procurement regime on the basis of Article 346 TFEU”.

(177) Z. STANLEY-LOCKMAN and K. WOLF, “European Defence Spending 2015: The Force Awakens”, *European Institute for Security Studies: Brief Issue*, March 2016.

(178) See M. STAPLES (ed), *The Future of European Defence: Tackling the Productivity Challenge*, *op. cit.*, p. 4, observing, “Everybody knows that the bang-to-buck ratio in Europe today is unacceptable”.

(179) See R. SEIDELMANN, “Costs, Risks and Benefits of a Global Military Capability for the European Union”, *Defence & Peace Economics*, 1997, pp. 123, 129, arguing Europe would have to spend 10-15% more on defense than the United States to achieve similar results; H. KUECHLE, “The Cost of Non-Europe in the Area of Security and Defence, Study for the European Parliament”, *No EP/ExPol/B/200513*, 2006, pp. 4, 25, estimating that the EU would need to spend four or even five times as much as the United States, citing Unisys, “Innergemeinschaftliche Transfers von Verteidigungsgütern Endbericht der Studie: Bewertung der Gemeinschaftsinitiativen im Zusammenhang mit dem innergemeinschaftlichen Transfer von Rüstungsgütern”, Brussels, EC, 2005, p.116.

(180) M. TRYBUS, *Buying Defence and Security in Europe: The EU Defence and Security Procurement Directive in Context*, *op. cit.*, p. 28 (citations omitted).

market failures”.(181) This market failure inflates prices, reduces transparency, and hinders innovation. Europe overpays by at least 20%.(182)

Fragmentation causes several problems. A fragmented market cannot benefit from economies of scale.(183) If European demand were consolidated to the same extent as in the United States, “batch sizes would be 570% bigger”.(184) “Closed procurement environments” undermine transparency and grant local firms “a special status” that eliminates incentives for innovation.(185) Not least, fragmentation leads to the duplication of efforts: although the EU spends less than half what the United States does, it funds six times as many weapon systems;(186) and only five percent of EU defense R&D spending is collaborative.(187) While it is tempting to speak of a “European” market, “there is no unified EU defense market, but a complex structure characterised by [28] national marketplaces”.(188) On paper, defense should be no less a part of the common market project than any other business sector. “There is”, however, “no common market for armaments in practice”.(189)

In the last decade, there have been “tentative steps away from national buying”. But EU procurement is still characterized by the same protectionism and fragmentation that plagued it for the half century after World War II.(190) Nationalist *juste retour* and offset policies only “sustain” and “accelerate” protectionism and fragmentation.(191)

(181) T. SANDLER and K. HARTLEY (eds), “Defense in a Globalized World: An Introduction”, in *Handbook of Defense Economics*, Amsterdam, Elsevier, 2007, pp. 607, 620.

(182) D. KEOHANE (ed), “Introduction”, in *Towards A European Defence Market*, 113 *Chailott Papers*, Pretoria, ISS, 2008, pp. 5, 6.

(183) T. SANDLER and K. HARTLEY, *The Political Economy of NATO, Past, Present, and into the 21st Century*, Cambridge, CUP, 1999, pp. 121, 124, explaining that defense is thought to be “economically strategic” and such industries are characterised by economies of scale, significant R&D spending in high technology, and “technical spillovers to the rest of the economy”.

(184) M. STAPLES (ed), *The Future of European Defence: Tackling the Productivity Challenge*, *op. cit.*, p. 15.

(185) S.R. SANDLER, “Cross-border Competition in the European Union: Public Procurement and the European Defence Equipment Market”, *Wash. U. Global Studies L. Rev.*, 2008, pp. 373, 383-385.

(186) M. STAPLES (ed), *The Future of European Defence: Tackling the Productivity Challenge*, *op. cit.*, p. 14.

(187) S.G. NEUMAN, “Defense Industries and Global Dependency”, *op. cit.*, p. 430.

(188) C. MÖLLING, “Options for an EU Regime on Intra-Community Transfers of Defence Goods”, *Towards A European Defence Market* (D. KEOHANE ed), *op. cit.*, pp. 51, 53.

(189) M. TRYBUS, “The Tailor-made EU Defence and Security Procurement Directive: Limitation, Flexibility, Descriptiveness, and Substitution”, *EL Rev.*, 2013, pp. 3, 5.

(190) See M. TRYBUS, *Buying Defence and Security in Europe: The EU Defence and Security Procurement Directive in Context*, *op. cit.*, pp. 138-139, writing that the “dominant view of economist and policy-makers is that defense spending in Europe is inefficient”; A.C. ALLEBACK, “The European Union: From the EC to the European Union”, in *Arms Industry Limited* (H. WULF ed), Oxford, OUP, 1993, p. 191, recounting that the European arms market has historically been “characterised by protected national markets”.

(191) P. PLATZGUMMER, “The EDA and Defence Offsets: Trailing After the Commission”, in *The European Defence Agency: Arming Europe* (N. KARAMPEKIOS and I. OIKNOMOU eds), London, Routledge, 2015, pp. 225, 227.

The costs of protectionism and fragmentation are considerable. Noting that Member States had abused Article 346, Sir Leon Brittan lamented “highly protected high cost national producers” dominate the market which has “led to grotesque distortions” and has been to Europe’s grave detriment.(192) Writing a decade later, Andrew Cox decried this “imperfect market structure” that results in

“feather-bedded companies, collusive relationships between national suppliers and purchasers and gross inefficiencies in production. This has led, in all but the most technologically advanced equipment markets where the United States has dominated, to the duplication of R&D and of production systems. This system of national production and protection worked passably well in an environment of Cold War certainties: the Soviet threat allowed politicians, defence establishments and arms manufacturers to engage in a *conspiracy of inefficiency against the public*. In the new post-Cold War environment, in which there is no self-evident threat and a declining world export market for defence goods, the maintenance of this conspiracy of inefficiency is much more difficult to achieve”.(193)

Americans complain that NATO allies spend less than the agreed upon target of two percent of GDP, but protectionism and fragmentation are more serious problems as they undermine economies of scale and ensure that “the modest European resources are spent unwisely”.(194)

Hope lies in Herbert Stein’s Law: “If something cannot go on forever, it will stop”.(195) “Under the twin constraints of increasing costs and diminishing resources”, maintaining 28 separate defense autarchies has become unsustainable.(196) “Thus, traditional notions of national independence in arms production is not, and indeed cannot, continue to be the whole picture for the future of the defense industry”.(197) History, alas, has not ended.

(192) J.B. WHEATON, “Defence Procurement and the European Community: The Legal Provisions”, *PPLR*, 1992, pp. 432, 433-434.

(193) A. COX, “The Future of European Defence Policy: The Case for a Centralised Procurement Agency”, *PPLR*, 1994, pp. 65, 77 (emphasis added).

(194) A. GEORGOPOULOS, “The European Armaments Policy: A Conditio Sine Qua Non for the European Security and Defence Policy?”, in *European Security Law* (M. TRYBUS and N.D. WHITE eds), Oxford, OUP, 2007, pp. 198, 204, explaining that “modest European resources are spent unwisely” due to fragmentation and protectionism.

(195) H. STEIN, “What I Think: Essays on Economics, Politics, and Life”, *AEI*, 1998, p. 32.

(196) J. BECKER, “The Future of Atlantic Defense Procurement”, *Defense Analysis*, 2010, pp. 9, 13; M. STAPLES (ed), *The Future of European Defence: Tackling the Productivity Challenge*, *op. cit.*, p. 171, observing that “European governments are pinched between two pressures – a need to commit more resources to their collective defence and straitjacketed finances” and averring that the solution to this dilemma lies in “address[ing] a highly fragmented supplier base”.

(197) J. BECKER, “The Future of Atlantic Defense Procurement”, *op. cit.*, p. 13.

### 3.2.2. Common security and defense policy

As costs rise, separately equipping Member States has become unaffordable,(198) and as common threats proliferate, it has become difficult to justify 28 separate security policies.(199) A common policy – whereby resources are pooled, redundancies eliminated, and efficiencies made – has been a longstanding goal.(200) These efforts culminated with the Maastricht Treaty in 1991(201) and the Treaty of Nice in 2001.(202) But from a practical standpoint, there has been little to show for these efforts. Progress has been modest since Member States resist relinquishing this last vestige of sovereignty.(203) Authority for integration already exists.(204) What is lacking is the political will.(205) It is unclear if such resolve will ever coalesce. Despite a profusion of agencies tasked with devising a coherent procurement system, their accomplishments are few.(206)

Common security lacks a ready definition. That is partly because Member States favored “constructive ambiguity” to reach a compromise at Maastricht, partly because of a “general problem” that “there has never been consensus” among

(198) H. KRIEGER, “Common European Defence: Competition or Compatibility with NATO?”, *op. cit.*, pp. 174-175, describing a common defense and security policy as “inevitable” given that “a single Member State is no longer capable of providing for its military security on its own”.

(199) See ECJ, *Fritz Werner Industrie Ausrüstungen GmbH v Germany*, case C-70/94, *E.C.R. I-3189*, 1995, p. 26; ECJ, *Criminal Proceedings against Leifer*, case C-83/94, *E.C.R. I-03231*, 1995, p. 27, holding that “it is becoming increasingly less possible to look at the security of a State in isolation, since it is closely linked to the security of the international community at large”.

(200) C. LENZER, *Co-operation on the Procurement of Defence Equipment – Lessons Drawn from the Symposium*, Report on behalf of the Technological and Aerospace Committee to the Western European Union, Doc. 1587, 4 November 1997, p. 4, explaining that cooperation “has been a political and military objective since the end of the Second World war”.

(201) See M. TRYBUS, N.D. WHITE *et al.*, “An Introduction to European Security Law”, in *European Security Law*, *op. cit.*, p. 3, recounting that the Maastricht Treaty created the Common Foreign and Security Policy (CFSP) as a second pillar of the Treaty on the European Union.

(202) See H. KRIEGER, “Common European Defence: Competition or Compatibility with NATO?”, *op. cit.*, p. 179, explaining that together the Maastricht and Nice treaties created a Common Security and Defence Policy.

(203) See *ibid.*, pp. 92, 178, contrasting Member States’ economic integration with their unwillingness “to transfer any sovereignty in defence matters”. See also S.G. NEUMAN, “Defense Industries and Global Dependency”, *op. cit.*, p. 442, explaining that “attempts to create a unified market and to end costly industrial duplication have foundered on concerns about national sovereignty, the security of supply, and the conflicting strategic interests of Europe’s small and large countries”.

(204) See H. KRIEGER, “Common European Defence: Competition or Compatibility with NATO?”, *op. cit.*, pp. 179-180, citing the authority deriving from the Maastricht and Nice treaties.

(205) See A. GEORGIOPOULOS, “The European Armaments Policy: A *Conditio Sine Qua Non* for the European Security and Defence Policy?”, *op. cit.*, pp. 212-213.

(206) See T. GUAY and R. CALLUM, “The Transformation and Future Prospects of Europe’s Defence Industry”, *op. cit.*, p. 773, writing that “previous efforts to institutionalize (or at least coordinate) defence procurement have yielded a litany of acronyms but few tangible accomplishments”; A. GEORGIOPOULOS, “The European Armaments Policy: A *Conditio Sine Qua Non* for the European Security and Defence Policy?”, *op. cit.*, p. 221, concluding that “institutional congestion” did little for the “rationalization” of the European defense industry.

stakeholders “about what the proper aims of a European defence policy should be”.(207) Cox wrote 20 years ago: “There is a pressing need for European nations to decide what they have in common and what ends their security policy seeks to serve”.(208) Despite some progress,(209) his observation remains largely true.

Whatever the definition of common security, any sensible understanding must include procurement.(210) Any truly integrated common defense policy would require interoperability among the constituent armed forces, which would require some cooperation in procurement.(211) Indeed, it is not a stretch to say that procurement should lie “at the heart of any future defense policy structure”.(212) Of late, greater significance has been attached to procurement.(213) Case in point, Article 17 TFEU designates procurement as a part of the common security policy.(214) This is a promising development.

### 3.2.3. Separateness of defense

Perhaps this point has already been driven home: unlike the U.S. procurement system, where defense is central, defense is a niche subject in Europe. One can be deemed an expert in EU public procurement and know next to nothing about defense procurement. That is partly a function of Member States’ post-Westphalian preference to safeguard their national sovereignty and domestic production capabilities at the national level, partly due to more

(207) A. COX, “The Future of European Defence Policy: The Case for a Centralised Procurement Agency”, *op. cit.*, p. 51.

(208) *Ibid.*, p. 68.

(209) The European Defence Agency (EDA) provides a glimmer of hope, and has in some measure succeeded in reducing fragmentation of the European defense industry. See A. GEORGIOPOULOS, “The European Armaments Policy: A *Conditio Sine Qua Non* for the European Security and Defence Policy?”, *op. cit.*, p. 219, explaining that the EDA “brought European armaments cooperation under the ambit of the EU” and that this was “an important development in its own right and not only because of its symbolic value”; “The EDA and EU Defence Procurement Integration”, in *The European Defence Agency: Arming Europe*, *op. cit.*, pp. 118, 132, calling the “contribution of the EDA in the process of European integration in the field of defence ‘fundamental’”.

(210) See M. TRYBUS, “Defence Procurement”, in *EU Public Contract Law: Public Procurement and Beyond* (M. TRYBUS, R. CARANTA and G. EDELSTRAM eds), Brussels, Bruylant, 2013, pp. 249, 253, arguing that “Defence procurement forms part of defence policy”; B. SCHMITT, “The European Union and Armaments: Getting a Bigger Bang for the Euro”, 63 *Chailot Papers*, Pretoria, ISS, 2003, pp. 32-33, observing that a “European armaments agency has continually haunted the process of building European defence” precisely because coordinated defense procurement is central to any common security policy.

(211) See A. COX, “The Future of European Defence Policy: The Case for a Centralised Procurement Agency”, *op. cit.*, p. 77.

(212) *Ibid.*, p. 213.

(213) See B. SCHMITT, “The European Union and Armaments: Getting a Bigger Bang for the Euro”, *op. cit.*, p. 5, writing that “one is bound to be satisfied with the importance now attached to the armaments dimension of European security and defence policy”.

(214) See A. GEORGIOPOULOS, “The European Armaments Policy: A *Conditio Sine Qua Non* for the European Security and Defence Policy?”, *op. cit.*, p. 199, citing TEU, Art. 2, Protoc. 23, and Art. 17, sent. 4, and arguing that cooperation in defense procurement is a *sine qua non* for a common defense policy; TEU, Art. 17, sent. 4, “the progressive framing of a common defence policy will be supported [...] by cooperation in the field of defence”.

general protectionist tendencies, and partly because of the EU's deference to abuses of Article 346. But whatever the origin, there exists a fundamental difference between the EU, which is at core a customs union, and the United States, which unified a nation around a common defense policy in 1789.(215) The two systems are so different in this respect that they resist comparison.

### 3.3. Law

Some worry that the Defence Directive contains a built-in "Buy European" preference.(216) That may be. But this essay is framed on a hypothetical where the TTIP has passed that would eliminate overt discrimination. As with the summary of U.S. system provided above, this section presents Europe's legal system from two perspectives, internal and external. The former considers the normal operation of the system that may be off-putting to foreign vendors and the latter on laws that directly regulate commerce with foreign buyers and sellers, often with clear protectionist intentions.(217)

#### 3.3.1. Internal laws

The single biggest obstacle for U.S. defense contractors in the EU is dealing with 28 separate national markets.(218) Member States are all subject to the Defence Directive, but their national legislation transposing these rules differ. Deciphering this national legislation is not for novices; this entails "adapt[ing] to idiosyncratic national legal and policy regimes concerning third country contractor participation".(219) Further, the Defence Directive does not mandate that Member States do business with non-EU defense suppliers but rather leaves to each State the choice to include or exclude these vendors.(220) In fact, at present the EU is mostly agnostic as to third-country access and treatment, leaving this to Member States' discretion.(221)

(215) See above, Section 2.2.3.

(216) See M. TRYBUS, *Buying Defence and Security in Europe: The EU Defence and Security Procurement Directive in Context*, *op. cit.*, p. 30, observing that while the Defence Directive does not explicitly favor European suppliers, "it has raised American concerns to that effect".

(217) See also P. TREPTE, *Public Procurement in the EU: A Practitioner's Guide*, *op. cit.*, pp. 330-331.

(218) D. FIOTT, "The 'TTIP-ing Point': How the Transatlantic Trade and Investment Partnership Could Impact European Defence", *op. cit.*, p. 18.

(219) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 191.

(220) See *ibid.*, pp. 156-157, quoting Defence Dir. 2009/81/EC, Recital 18, noting that Member States "retain the power to decide whether or not their contracting authorities may allow economic operators from third countries"; M. TRYBUS, *Buying Defence and Security in Europe: The EU Defence and Security Procurement Directive in Context*, *op. cit.*, p. 30, noting that "the Directive leaves the choice on whether to open a procurement to bidders from third countries such as the United States to the individual Member States".

(221) See B. HEUNINCKX, "The EU Defence and Security Procurement Directive: Trick or Treat?", *PPLR*, 2011, pp. 9, 12.

Perhaps the second biggest problem is Article 346. It has long been used to shield EU defense suppliers from competition under the guise of protecting national security interests.<sup>(222)</sup> Recently, the European Court of Justice has cracked down and the opportunities for abusing Article 346 have been curtailed.<sup>(223)</sup> At the same time, its applicability remains unclear.<sup>(224)</sup> Further, notwithstanding the Court's, the system will only work if Member States use Article 346 in good faith, which is often lacking.<sup>(225)</sup>

A third barrier for U.S. contractors is the workings of the new Defence Directive itself. This is not a concern that the Defence Directive does so purposefully<sup>(226)</sup> but that it may do so inadvertently in the same way that U.S. procurement system discourages the uninitiated from participating.<sup>(227)</sup> Further, the Directive sanctions the use of exemptions for the security of supply and of information, and such justifications are susceptible to abuse.<sup>(228)</sup> Butler gives a thorough treatment of this question, and ultimately maintains that the Directive makes considerable provision to accommodate third-countries.<sup>(229)</sup> He acknowledges, however, that "it is open to question whether the Defence Directive could better accommodate third country considerations".<sup>(230)</sup>

(222) K. HARTLEY, "The Arms Industry, Procurement, and Industrial Policies", in *Handbook of Defense Economics*, *op. cit.*, pp. 1139, 1148, unfavorably compares Art. 346 and the Buy American Act as two examples of legislation that limit foreign competition and create domestic monopolies.

(223) See B. HEUNINCKX, "Security of Supply and Offsets in Defence Procurement: What's New in the EU?", *op. cit.*, p. 39, summarizing the ECJ's jurisprudence on Art. 346.

(224) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 87, observing that the "EU courts have not yet been presented with a credible invocation of Article 346" and it is, therefore, "uncertain the circumstances in which Article 346 TFEU could conceivably be validly invoked".

(225) See S. R. SANDLER, "Cross-border Competition in the European Union: Public Procurement and the European Defence Equipment Market", *Wash. U. Global Studies L. Rev.*, 2008, pp. 373, 385, describing the resistance to transparency and noting that derogations under Art. 346 have been "invoked with impunity".

(226) But see L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 193, noting that some U.S. commentators have warned that "provisions on technical specifications, security of supply and security of information, in particular, could potentially form disguised market access barriers for US contractors".

(227) *Ibid.*, p. 195, reporting that "it has long been argued that the Defence Directive's technical specifications provisions could become an intended or unintended" market access barrier.

(228) See *ibid.*, pp. 204-205, describing the potential for abusing the Defence Directive's security of supply provisions; P. TREPTE, *Public Procurement in the EU: A Practitioner's Guide*, *op. cit.*, p. 240, observing that there is "a clear tendency to overstate the need for security".

(229) See gen. L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, Chapter 5, "The Defence Directives as a Barrier to Trade with the United States".

(230) *Ibid.*, p. 245. This chapter, he concludes, "pointed debate towards the need for a more sustained legal discourse that digs behind claims of latent potential for discrimination based on limited empirical evidence towards one encouraging open engagement on the issues of how the EU and US legal systems are configured and calibrated to deal with the issue of foreign contractor participation and treatment in the field of defence procurement."

### 3.3.2. External laws

Several U.S. observers have expressed concern that the Defence Directive will create a “fortress Europe” that excludes U.S. suppliers from defense procurement.(231) Following this essay’s hypothetical that overt discrimination is eliminated under the TTIP, the concern here is not so much with *de jure* but with *de facto* restrictions arising from the structure of non-transparent and exclusive European defense clubs.(232)

In terms of external laws, perhaps the most important obstacle is export restrictions that resemble the workings of the States’s own tightly controlled technology export regime.(233) Further, the Defence Directive compounds the problem by allowing European firms to design around ITAR.(234) Even passage of the TTIP and the prohibition of unfair discrimination would not necessarily preclude restrictions based on concerns about security of supply.(235) Governments are prone to exaggerate security of supply concerns(236) and, therefore, the EU’s own version of technology export controls are likely a trade barrier, or at least have the potential to become one.(237)

Another major obstacle looms on the horizon. Since 2012, the EU has been considering the International Procurement Instrument (IPI), which is to be used as a negotiation tool to encourage liberalization. Though not intended as a protectionist measure, if enacted in its present form (updated in 2016), the

(231) See C.R. YUKINS, “Assessing the New European Defense Procurement Directive”, West Government Contracts Year, in *Review Conference: Conference Briefs*, 2010, pp. 3-1, 3-7, 3-10, noting the Defence Directive hints at the power to exclude third-country suppliers; J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, pp. 220-225 describing the Defence Directive’s “subtle areas of potential discrimination” against the United States.

(232) See S.N. FERRARO, “The European Defence Agency: Facilitating Defense Reform or Forming Fortress Europe?”, *Transnational L. & Contemporary Problems*, 2007, pp. 549, 569-570, 613-614, describing latent “competitive obstacles” that “may have the effect of creating a *de facto* European preference” in part due to the lack of transparency and organizational structure of the EDA and the Organisation for Joint Armament Cooperation.

(233) See C.R. YUKINS, “Assessing the New European Defense Procurement Directive”, *op. cit.*, pp. 3-2, describing “cumbersome licensing requirements for transferring sensitive technologies across borders”.

(234) See J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, pp. 2, 16, 222-223; L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 217-218; U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 52.

(235) This exemplifies how fortress-like conduct can be interactive and reciprocal. J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 4.

(236) P. TREPTE, *Public Procurement in the EU: A Practitioner’s Guide*, *op. cit.*, p. 240.

(237) This is doubly unfortunate. Art. 346 not only impedes free trade by authorizing an exclusion for dubious security of supply concerns, it also “legitimizes antiquated thinking that domestically derived technology provides the best defense capability”. See R. SANDLER, “Cross-border Competition in the European Union”, *op. cit.*, p. 426.

IPI would create additional barriers for American firms competing for public contracts in the EU. However, this essay assumes a hypothetical wherein a TTIP is in effect and that preclude the IPI. The two would be mutually exclusive.

National access rules are a final barrier that the TTIP's rules against overt discrimination would not necessarily overcome. That is because such national access rules are not necessarily discriminatory against non-EU suppliers as they can be made to apply as much to EU suppliers as to third-country suppliers. In practice, having 28 different national access procedures serves as a significant barrier to entry. The cost of separately adapting to each market discourages foreign commercial interests. Further, acquisition of a domestic firm in one EU Member State does not grant foreign suppliers reciprocal access to other nations' markets.(238)

#### 4. *Toward a Free Market in Defense*

##### 4.1. Comparisons

Now that a summary of each system has been provided, some general observations and comparisons are possible. Both sides of the Atlantic suffer from illiberal defense markets: the United States from duopolies;(239) the EU from monopolies at the Member State level;(240) both from oligopsonies on the demand side;(241) and both from double monopolies resulting from insufficient competition for both supply and demand.(242) The result is inefficiency, poor value for money, and inflated prices.

Transatlantic civil trade dwarfs transatlantic military trade.(243) At the same time, their militaries are more deeply integrated than ever before, forming a "dense

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(238) See D. FIOTT, "The 'TTIP-ing Point': How the Transatlantic Trade and Investment Partnership Could Impact European Defence", *op. cit.*, p. 18, reporting that "American firms have often rejected the idea of mergers with or acquisition of European firms because it would not translate into Europe-wide market access" and observing that "acquiring a Czech firm would not automatically translate into access to the Italian market".

(239) See K. HARTLEY, "The Arms Industry, Procurement, and Industrial Policies", *op. cit.*, p. 1151, explaining that "the United States has more duopolies and oligopolies in major weapons systems".

(240) *Ibid.*, p. 1151, saying that the EU defense market "is characterized by domestic monopolies" among Member States.

(241) For example, see W.P. ROGERSON, "Economic Incentives and the Defense Procurement Process", *J. Econ. Perspectives*, 1994, pp. 65, 67, explaining, "Government is the only possible buyer of most weapons".

(242) "[W]here a monopsonistic seller faces a monopolistic buyer" economists call this a double monopoly. See J.N. MORGAN, "Bilateral Monopoly and the Competitive Output", *Q.J. Economics*, 1949, p. 371. Several markets suffer from this condition, including professional sports, healthcare, and defense. Double monopolies are characterized by prices that are at least as high under a traditional monopoly or monopsony, perhaps even higher. See R.D. FRIEDMAN, "Antitrust Analysis and Bilateral Monopoly", *Wisc. L. Rev.*, 1986, pp. 873, 874-875.

(243) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 27.

web.”(244) Far from disintegrating at the close of the Cold War as many predicted, NATO has proven to be indispensable. Europe’s contribution to coalition forces in Afghanistan and Iraq (though not via NATO for the latter conflict) is but one manifestation of the value of this alliance. Corresponding depth in the arms trade through a version of the TTIP that includes defense may not be far off.(245)

A common trope is that the EU can hardly push for freer transatlantic defense trade when little exists even among its Member States.(246) But trade within the EU is flourishing, at least relative to where it was until a few years ago.(247) To be sure, protectionism and fragmentation persist.(248) But this market is nonetheless growing steadily. Americans worry that this brisk trade within the EU may devolve into a protectionist Fortress Europe that would exclude U.S. suppliers as European have long accused the United States of.(249)

The EU and the United States have different objectives for the transatlantic defense trade: the EU wants absolute equality in terms of volume traded; the United States wants comparable acquisition rules.(250) Yukins’s recommendation to abolish the military-civil divide in the EU,(251) is emblematic: the United States seeks not a perfect balance of trade but to replicate its own system abroad.(252) But because the two systems are in many ways asymmetric,(253) this complicates mutual understanding and calls into ques-

(244) J. BECKER, “The Future of Atlantic Defense Procurement”, *op. cit.*, pp. 10-11, 16.

(245) The longstanding transatlantic military cooperation is not the only reason for thinking that the TTIP may be on the horizon. Another is that most European defense integration has been achieved under the auspices of NATO. See gen. F. MÉRAND and K. ANGERS, “Military Integration in Europe”, in *Beyond the Regulatory Polity: The European Integration of Core State Powers* (P. GENSCHEL and M. JACHTENFUCHS eds), Oxford, Scholarship Online, 2014. Left to their own devices, Member States consider their domestic defense industries as strategic hedges against their neighbors and historic rivals. But were the larger transatlantic community included, perhaps Member States would be more open to the liberalization of their defense markets.

(246) D. FLOTT, “The ‘TTIP-ing Point’: How the Transatlantic Trade and Investment Partnership Could Impact European Defence”, *op. cit.*, p. 18, writing that “European countries can hardly push the case for reciprocity with the US when there is little reciprocity between themselves”.

(247) See J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, pp. 2, 13, describing the increased competition within the EU.

(248) See M. STAPLES (ed), *The Future of European Defence: Tackling the Productivity Challenge*, *op. cit.*, p. 24, explaining, “The European defence industry has integrated to a degree but remains fragmented”.

(249) See S.N. FERRARO, “The European Defence Agency: Facilitating Defense Reform or Forming Fortress Europe?”, *op. cit.*, pp. 234, 552, 582, 611-614, reporting there is neither a “welcome mat at Europe’s doorstep” nor any discernible “intent to exclude U.S. firms from the European market”.

(250) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, pp. 40, 51, explaining that “are two overall different views of the two way street system that transatlantic defence trade should represent: Europe sees it as a comparable traffic in volume and the U.S. sees it as comparable acquisition rules”.

(251) See above Section 2.2.3.

(252) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, pp. 40, 51.

(253) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 14.

tion how well the U.S. system can be transplanted.(254) Further, the U.S. federal procurement system is the product of improvisation;(255) as noted above, its foremost historian has observed that it is “inconceivable” that any reasonable person asked to design a public procurement system from scratch “would come up with our current system”.(256) How well a system geared to the particular circumstances in the United States would work if transplanted abroad is uncertain.

One thing seems clear. Both sides would benefit from a liberalized market because both are afflicted by the pathologies common to defense economics.(257) Consolidation and cooperation are often prescribed.(258) But perhaps the better remedy is competition, particularly the *foreign* competition that would accompany trade liberalization.(259)

#### 4.2. Mutual benefits from removing non-tariff barriers

Before tactics for carrying out liberalization are considered, the “critical issue” must be addressed. Namely, is such liberalization mutually beneficial?(260) Freeing up the transatlantic defense trade would be good policy for at least three reasons: the savings, improved military capabilities, and deeper ties within the transatlantic alliance.(261)

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(254) See gen. A. WATSON, *Legal Transplants: An Approach to Comparative Law*, 2nd ed., Athens (GEO), UGP, 1993, calling into question the transportability of legal systems.

(255) J.F. NAGLE, *History of Government Contracting*, *op. cit.*, p. 519.

(256) *Ibid.*, p. 519.

(257) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. A-2: “The defense sector can no longer prosper in a bubble and is impacted by globalization on at least two fronts: the technology front and the investment front. A quick look at the U.S. and European defense industry landscape and defense equipment shows an ever growing common technology supply and multiple transatlantic investments. Even the United States who, as a nation, enjoys the highest defense investment in the world, could not afford to sustain its technology base by relying exclusively on domestic business. Let alone the sensitive political aspect of the issue, it is simply impossible both from a financial and commercial standpoint.”

(258) See E. KLEPSCH, *Two-way Street: USA-Europe Arms Procurement*, *op. cit.*, p. 19, writing that “[q]uantities of ink have flowed on this intractable subject over many years”.

(259) See C. BALIS, “Whither the EU Internal Defense Market? Thinking Beyond ‘Pooling and Sharing’”, *Avascent*, 2014, arguing that “trading and competing” are just as important as “pooling and sharing”; Defense Science Board, *Final Report*, *op. cit.*, p. 16, arguing that competition “could yield innovative, high-quality products, and, for domicile governments, a greater return on defense investments”. “Such competition”, the authors continue, “would stimulate innovation and create the incentive to adopt the industrial and acquisition related efficiencies that generate downward pressure on cost cycle-time”.

(260) M. EDMONDS, “International Military Equipment Procurement Partnerships: The Basic Issues”, *op. cit.*, p. 15.

(261) See Defense Science Board, *Final Report*, *op. cit.*, p. 16, writing that “[c]ross-border defense industrial links can help spread the fiscal burden” and that such “transatlantic industrial links are a potential source of greater political-military cohesion” and would “amplify NATO fighting strength by enhancing U.S.-European interoperability and narrowing the U.S.-European technological gap”.

### 4.3. Economics

Defense economics is complicated and politically fraught; pursuing free trade on purely economic grounds would be overly simplistic.(262) Yet given the high cost of a modern military, affordability resonates.(263) Indeed, “The economics of defense is a powerful driver for change”.(264)

As Stephen Martin, Keith Hartley, and Andrew Cox explain, the savings from a liberal transatlantic trade would accrue in three dimensions:

“first, the static trade effect with purchasers buying from the cheapest, possibly foreign supplier; second, the competition effect which creates downward pressure on the prices of domestic firms as they attempt to compete with foreign companies entering previously protected domestic markets; and third, a restructuring effect as industry reorganises under the pressure of new competitive conditions[...]”.(265)

Though the latter two may seem too theoretical, both sides would benefit immediately from the static trade effect. The United States spends too much on gold-plated products that cost billions and are only marginally better than the next best option.(266) European vendors can offer the Pentagon savings that it cannot refuse.(267) Similarly, too often Member States waste their budgets duplicating products that are available off the shelf from U.S. vendors.(268) Such savings could be politically valuable on both sides of the Atlantic.

Less obvious but no less real would be the benefits from the competition effect and the restructuring effect. Competition from abroad “constrain[s] the behavior of domestic suppliers” and drives down cost.(269) Longer term, the

(262) K. HARTLEY, “The Future of European Defence Policy: An Economic Perspective”, *Defence and Peace Economics*, 2003, pp. 107, 112-113.

(263) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 10.

(264) *Ibid.*, p. 265.

(265) S. MARTIN, K. HARTLEY and A. COX, “Defence Procurement of Dual-use Goods: Is There a Single Market in the European Union?”, *op. cit.*, p. 58.

(266) See W.S. CURRY, “Government Abuse: Fraud, Waste, and Incompetence in Awarding Contracts in the United States”, *Transaction*, 2014, pp. 1-2.

(267) See M. SIEFF, “Europe Can Offer Defense Deals Washington Can’t Refuse”, 9:3 *Eur. Affairs*, Fall 2008, listing among the niche products that the United States has abandoned but provide far cheaper solutions the diesel-electric submarines that are built in France, Germany, and Sweden.

(268) B. MAUDAVE, “U.S. Aerial Tanker Contract Decried As Symptom of Protectionism”, [www.europeaninstitute.org/index.php/ei-blog/95-march-2010/971-aerial-tanker-contract-decried-as-symptom-of-protectionism](http://www.europeaninstitute.org/index.php/ei-blog/95-march-2010/971-aerial-tanker-contract-decried-as-symptom-of-protectionism), accessed 4 July 2019, quoting Germany’s *Die Welt* newspaper recommending that Europe “stop its common practice of senselessly developing some of its own weapons-products when it could just buy them from America”.

(269) W.B. BURNETT and W.E. KOVACIC, “Reform of United States Weapons Acquisition Policy: Competition, Teaming Agreements, and Dual Sourcing”, *op. cit.*, 298-299. See also Defense Science Board, *Final Report*, *op. cit.*, p. 16, explaining that foreign competition can “create the incentive adopt the industrial and acquisition-related efficiencies that generate downward pressure on cost”.

restructuring effect forces monopolistic domestic monopolies to reorganize in response to foreign competition.(270)

Estimates about the benefits of freeing up the transatlantic defense trade vary, but these savings are not paltry.(271) This is especially true in light of the large sums involved and the twin constraints of shrinking defense budgets and cost growth.(272) It is with good reason that efficiency is the most common argument made in favor of freeing up the transatlantic defense market.(273)

#### 4.4. Capabilities

“Equipment wins wars”.(274) In addition to the savings from freer trade, and the attendant potential for purchasing more equipment, both sides would benefit from *qualitatively* improved warfighting capabilities.(275) The United States has integrated a number of European weapon systems.(276) recognizing that European suppliers are the “world leaders in certain technologies with potentially military application”(277) and that the United States “does not have the monopoly on all key emerging military-relevant technologies”.(278) The United States sometimes struggles to design and field weapons apace

(270) K. HARTLEY, “The Arms Industry, Procurement, and Industrial Policies”, *op. cit.*, p. 1168, suggesting that governments ought to “subject their domestic monopolies to competition by allowing foreign firms to bid for national defense contracts”.

(271) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, pp. 53-54, describing vast potential for savings from foreign competition; H. KUECHLE, “The Cost of Non-Europe in the Area of Security and Defence, Study for the European Parliament”, *op. cit.*, p. 7, predicting the savings from a liberalized market in Europe; K. HARTLEY, “The Future of European Defence Policy: An Economic Perspective”, *op. cit.*, p. 112, estimating the savings at 10-20%.

(272) J. BECKER, “The Future of Atlantic Defense Procurement”, *op. cit.*, p. 13. See also S. DE VAUCORBEIL, “The Changing Transatlantic Defence Market”, in *Towards A European Defence Market*, *op. cit.*, pp. 89, 96, reporting that the cost of equipping a soldier has increased 100-fold since World War II and the price of a fighter plane increased 10,000% from 1944 to 1985.

(273) See M. EDMONDS, “International Military Equipment Procurement Partnerships: The Basic Issues”, *op. cit.*, pp. 6, 10, “The most frequent argument in favor of international weapons procurement is economic”.

(274) M. TRYBUS, *European Defence Procurement Law: International and National Procurement Systems as Models for a Liberalised Defence Procurement Market in Europe*, The Hague, Kluwer, 1998.

(275) See S. DE VAUCORBEIL, “Reforming the Transatlantic Defence Market”, *op. cit.*, p. 119.

(276) S. DE VAUCORBEIL, “The Changing Transatlantic Defence Market”, *op. cit.*, pp. 103-104, providing a table listing several European such weapons including, German canons and British armor on the M1A2 Abrams tank and the Swiss-designed Stryker armored vehicle.

(277) *Ibid.*, p. 111, quoting D. KEOHANE and T. VALASEK, *Willing and Able? EU Defence in 2020*, London, Centre for European Reform, 2008, p. 25.

(278) *Ibid.*, p. 111, quoting K. HAYWARD, *Friends and Rivals: Transatlantic Relations in Aerospace and Defence in the 21st Century*, London, Royal Aeronautical Society, 2005, p. 7. Europe’s “strategy has been to devote fewer resources to defense-specific R&T and instead leverage innovations in commercial technology for military purpose”. U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 44. European suppliers may thereby develop affordable alternatives to gold-plated U.S.-designed weapons.

with emerging threats<sup>(279)</sup> and would benefit from “alternative competitive solutions” from Europe.<sup>(280)</sup> European suppliers may offer products that are superior in absolute terms<sup>(281)</sup> and others may offer “70% solutions” at a fraction of the cost.<sup>(282)</sup> And EU capabilities would likewise benefit from a freer transatlantic trade,<sup>(283)</sup> given that the U.S. defense industry still constitutes “the main technology driver[s] in the field”.<sup>(284)</sup>

#### 4.4.1. Politico-military

Two decades ago, the European Court of Justice observed: “it is becoming increasingly less possible to look at security of the State in isolation, since it is closely linked to the security of the international community at large”.<sup>(285)</sup> The truth of that observation seems obvious today. Further, though skeptics prophesied NATO would fall apart with the end of the Cold War, the North Atlantic countries share common security threats and “are becoming more

(279) See Committee on Armed Services, U.S. House of Representative, 114th Congress, 27 October 2015, “Shortening the Acquisition Cycle”, p. 99, appending A. CARTER, “Running the Pentagon Right: How to Get the Troops What They Need”, *Foreign Affairs*, 6 December 2013, saying “the same system that excels at anticipating future needs [...] proved less capable of quickly providing technology and equipment” for the rapidly changing conditions in Afghanistan. But such problems extend beyond rapidly evolving operational needs. See National Research Council, *Optimizing U.S. Air Force and Department of Defense Review of Air Force Acquisition Programs*, Washington, National Academies Press, 2009, p. 1, writing, “Too often DoD weapons systems programs experience large cost overruns and schedule delays, contributing to a loss of confidence in the DoD acquisition system”.

(280) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 3, explaining that “Europe can offer competitive solutions to the U.S. military with technology derived from the commercial sector”. For examples see M. SIEFF, “Europe Can Offer Defense Deals Washington Can’t Refuse”, *op. cit.*, p. 269, describing BAE’s contribution to up-arming vehicles for Iraq and Afghanistan; U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 81, explaining that “European technologies were already available and suited to” the Littoral Combat Ship because this size of ship and type of mission “were more traditionally European”.

(281) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 81, noting that when European firms successfully compete in the U.S. market the general rule “is that European products do not win on price but on their technological edge”. Some examples include electric-diesel submarines, de-gauzed minesweepers, and littoral ships. See M. SIEFF, “Europe Can Offer Defense Deals Washington Can’t Refuse”, *op. cit.*, p. 269.

(282) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 3, explaining that “enhanced market access can not only result in more competition, and the innovation and affordability it can bring, but also can facilitate our war fighters’ access to existing 70 percent solutions from abroad” thereby “putting the practical ahead of the perfect”.

(283) S. DE VAUCORBEIL, “Reforming the Transatlantic Defence Market”, *op. cit.*, p. 119, arguing greater “cross-border competition across the Atlantic” would help Europe to “beef up its capabilities”.

(284) S.G. NEUMAN, “Defense Industries and Global Dependency”, *op. cit.*, p. 443, quoting an official at the Swedish Defense Material Administration.

(285) *Fritz Werner Industrie Ausrüstungen GmbH v Germany*, case C-70/94, *ECR* I-3189, 1995, p. 26; *Criminal Proceedings against Leifer*, case C-83/94, *ECR*, I-03231, 1995, p. 27.

deeply integrated than even before”.(286) Yet deep ties in political and military affairs contrast starkly with the defense trade.(287) The logic behind deepening the level of defense trade among such close allies is irresistible.(288) Rather than jeopardizing security of supply as some would suppose, procuring from allies would broaden the supply base and enhance the security of supply within the alliance.(289) Freeing up defense would also revitalize NATO at a time when America is complaining especially vociferously that Europeans are failing to pay their fair share for defense.(290) Liberalizing defense would further “entangle” members of the alliance(291) because importing weapons is not a one-off transaction but rather “implies agreement from the seller to provide technical assistance” and thus entails a long-term relationship.(292)

### **5. Strategies for Removing, Mitigating, and Avoiding Non-Tariff Barriers**

The weight of this essay has described differences of history, constitution, and law that create non-tariff barriers. The balance considers four options for removing, mitigating, or avoiding those barriers. Three are considered in this section, and the fourth is addressed in the conclusion and concerns this essay’s larger project of developing better mutual understanding. In the author’s forthcoming doctoral thesis, the latter effort extends beyond defense to cover the whole of the public procurement.

There are several strategies that this section does not consider, which may seem obvious and would likely fit under the near-term strategies discussed in Section 5.3. Namely, that firms can mitigate non-tariff barriers by establishing

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(286) J. BECKER, “The Future of Atlantic Defense Procurement”, *op. cit.*, pp. 10-11, 16, describing a “dense web of interactions” that unites NATO countries and asserting, “How both Europe and America define their security interests has become inextricably intertwined”.

(287) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 41, noting that defense trade is incommensurate with the “importance of the transatlantic defence relationship from the political standpoint”.

(288) M. EDMONDS, “International Military Equipment Procurement Partnerships: The Basic Issues”, *op. cit.*, p. 7.

(289) See D. FIOTT, “The ‘TTIP-ing Point’: How the Transatlantic Trade and Investment Partnership Could Impact European Defence”, *op. cit.*, p. 23, writing that “[o]ne method of ensuring supply security is to increase the supply base” to include transatlantic vendors; A. MAYER, “Military Procurement: Basic Principles and Recent Developments”, 21:1 *GW J. Int’l L. & Econ.*, 1987, pp. 165, 179-182, explaining multiple sourcing.

(290) S. DE VAUCORBEIL, “Reforming the Transatlantic Defence Market”, *op. cit.*, p. 128.

(291) *Ibid.*, p. 292, citing E.B. KAPSTEIN, “Allies and Armaments”, *Survival*, Summer 2002, pp. 141, 143-144, summarizing the defense economics literature and maintaining that armaments cooperation entangles allies and leads them to form deeper relationships.

(292) M.D.C. GARCÍA-ALONSO and P. LEVINE, “Arms Trade and Arms Races: A Strategic Analysis”, in *Handbook of Defense Economics*, 2007, *op. cit.*, pp. 941, 947.

local subsidiaries (either organically or through mergers and acquisitions), entering into joint ventures with domestic suppliers, or hiring local counsel. Such options were mentioned in Section 2.3.2 but are skipped over here because, while obvious, they are often costly and inefficient. They can impose transaction costs that render foreign competition cost prohibitive, especially for smaller firms.

### 5.1. The long-term strategy for removing non-tariff barriers: harmonization via reciprocal defense agreements

One policy option that has thus far gone unmentioned is the use of reciprocal defense procurement agreements (RDAs). This omission resulted in part from this essay's hypothetical under which the TTIP has come into force and overt trade barriers have been removed and only subtle non-tariff barriers remain. Now that problems with such barriers have been set forth, the balance of this essay turns to potential solutions. One such is the use of RDAs to encourage the harmonization of defense procurement.

RDAs emerged during the Cold War, seek to establish free trade in defense, and consist of mutual assurances of nondiscrimination in the form of memoranda of understanding.<sup>(293)</sup> This U.S.-led initiative sought rationalization, standardization, and interoperability of defense equipment among allies.<sup>(294)</sup> Sometimes the RDA's wording suggests that they would venture beyond strategic concerns "to facilitate the mutual flow of defense procurement"<sup>(295)</sup> and trade liberalization more broadly. These bilateral agreements are, therefore, an alluring option for freeing up a sector that various multilateral trade agreements have mostly passed by.<sup>(296)</sup>

Some advocate a more ambitious goal: the broader harmonization of procurement rules to facilitate cross-border procurement.<sup>(297)</sup> In a perfect world, that would make cross-border procurement easier, cheaper, and perhaps more common. So far TTIP negotiations seem to have ignored, or at least failed

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(293) D.B. MILLER, "Note, Is it Time to Reform Reciprocal Defense Agreements?", *Pub. Cont. L.J.*, 2009, p. 93.

(294) *Ibid.*, p. 95.

(295) Memorandum of Understanding Between the Federal Minister of Defense of the Federal Republic of Germany and the Secretary of Defense of the United States of America Concerning the Principles Governing Mutual Cooperation in the Research and Development, Production, Procurement and Logistic Support of Defense Equipment, U.S.-F.R.G., 17 October 1978, Art. I, § 1.1, [www.acq.osd.mil/dpap/Docs/mou-germany.pdf](http://www.acq.osd.mil/dpap/Docs/mou-germany.pdf), accessed 4 July 2019.

(296) See D.B. MILLER, "Note, Is it Time to Reform Reciprocal Defense Agreements?", *op. cit.*, p. 95, observing that defense procurement "has largely been excluded from the march toward liberalization".

(297) See gen. C.R. YUKINS and S.L. SCHOONER, "Incrementalism: Eroding the Impediments to a Global Public Procurement Market", *op. cit.*

to prioritize, such harmonization efforts.(298) Even the most optimistic partisans concede that harmonization is at least a generation away.(299) Meanwhile, perhaps RDAs may serve as a useful step toward such harmonization that like-minded policymakers can push for, even if their domestic politics would preclude broader reforms for the time being. Updating existing agreements with EU Member States and perhaps establishing a new RDA at the EU level may form part of that solution.(300)

Yet RDAs are not a panacea. While RDAs may succeed at addressing overt barriers to trade such as the Buy American Act or the Berry Amendment, they fail to address problems with the subtler kinds of non-tariff trade barriers discussed in this essay. The structural restrictions that discourage vendors from participating in transatlantic procurement opportunities would persist. Even if overt barriers are removed, the remaining structural restrictions would still “raise practical barriers to entry as foreign vendors run headlong into dense and alien procurement regimes”.(301)

RDAs are, therefore, helpful as far as they go. But opening up the transatlantic trade fully will require either harmonization of procurement rules, which is unlikely in the near term, or a solution that would somehow avoid the problems arising from deep dissimilarities in the two systems. As this essay has been at pains to demonstrate, simply removing overt barriers will not suffice: even if the letter of the law were the same, in practice the law would be interpreted and applied differently due to incommensurable cultural, constitutional, and political differences. In short, using RDAs to encourage harmonization mitigates the problem, but would not fully resolve it.

## 5.2. Medium-term strategies for mitigating non-tariff barriers

In addition to the political efforts to remove non-tariff barriers, there lies a parallel academic and didactic effort. This entails developing a better understanding of the differences between the EU and U.S. systems and then socializing that research to a broader audience. Butler’s book has done a great

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(298) See S. WOOLCOCK and J.H. GRIER, “TTIP and Public Procurement”, in *Rule Makers or Rule Takers? Exploring the Transatlantic Trade and Investment Partnership* (D.S. HAMILTON and J. PELKMANS eds), Brussels, Center for European Policy Studies, 2015, pp. 297, 321-323.

(299) C.R. YUKINS and S.L. SCHOONER, “Incrementalism: Eroding the Impediments to a Global Public Procurement Market”, *op. cit.*, pp. 530, 558.

(300) D.B. MILLER, “Note, Is it Time to Reform Reciprocal Defense Agreements?”, *op. cit.*, pp. 295, 102-112, advocating that RDAs should be modernized to incorporate the GPA’s transparency requirements and broader trade liberalization goals.

(301) C.R. YUKINS and S.L. SCHOONER, “Incrementalism: Eroding the Impediments to a Global Public Procurement Market”, *op. cit.*, p. 558.

service to this cause, but much work remains.<sup>(302)</sup> This essay is also primarily devoted to that effort; the conclusion (Section 6.) remarks on progress made. This section, however, considers some practical options for removing non-tariff barriers to a freer transatlantic defense trade. These medium-term policy options require neither politically challenging legal reforms nor awaiting the slow accretion of academic contributions.

### 5.2.1. Addressing public relations

If the TTIP is ever going to happen, would-be reformers must persuade both policymakers and their constituencies.<sup>(303)</sup> Not only is the public unusually skeptical about the merits of free trade at present, defense remains politically sensitive.<sup>(304)</sup> So successful persuasion will require artful statecraft. This section outlines what such statecraft may encompass.

Having missed the chance to extend an olive branch with the aerial tanker procurement a decade ago, perhaps the United States should take the first step toward reconciliation. The DoD could start by acknowledging that mistakes were made<sup>(305)</sup> and reaffirm its openness to competition in future.<sup>(306)</sup> Otherwise, the extent that the EU considers U.S. policy to be protectionist, it

(302) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, pp. 8-9, acknowledging that he is providing a “framework” for “more systematic comparative research” that may be possible in future and offering a “preliminary mapping exercise”. Given the dearth of research in comparative U.S./EU procurement, this signifies a major contribution.

(303) Even if the TTIP passes, as this essay’s hypothetical assumes, the politics of defense procurement must be considered and addressed. Even if the overt rules favor liberal trade, national preferences can still be exerted covertly – and further differences in the two procurement regimes may create non-tariff barriers unintentionally. So it is necessary to persuade the public and policymakers alike of the virtues of free trade in defense.

(304) See A. GEORGOPOULOS, “The EDA and EU Defence Procurement Integration”, *op. cit.*, p. 118, observing that defense is “linked to core functions of the notion of the Westphalian nation State”; J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defence Market and the Implications for U.S. National Security*, *op. cit.*, p. 30, describing the “close linkage” between domestic defense markets and sovereignty; J. MAWDSLEY, “The Gap Between Rhetoric and Reality: Weapons Acquisition and ESDP”, Paper 26, *BICC*, 2002, pp. 4-5, writing that defense acquisition “touches the heart of the concept of sovereignty of the nation State”, that this “rhetoric is both emotive and fundamental to the Westphalian ideas of statehood” and that “national autonomy in the armaments sector has therefore traditionally been very important for States”.

(305) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, pp. 59-60, remarking that the handling of the aerial tanker procurement evinced a protectionist atmosphere in Congress; R.F. LAIRD, “US Flap on the Aerial Tanker Could Be Self-Defeating”, *Eur. Affairs*, Fall 2008, warning that U.S. chauvinism would come “at the expense of allies and of hopes for strongly expanding the transatlantic defense-industrial base on which future force modernization depends”.

(306) Defense Science Board, *Final Report*, *op. cit.*, p. 48, recommending the DoD “publicly reaffirm [...] its willingness to consider a range of cross-border defense and industry linkages [...] that enhance U.S. security, interoperability with potential coalition partners, and competition in defense markets”.

will respond in kind.(307) By taking the lead on freer cross-border trade and articulating a public relations campaign to offset past mistakes, the United States can influence the EU's perception of U.S. protectionism.(308) Such efforts would include advocating that the longstanding imbalance in U.S.-EU the arms trade should not be a cause for concern(309) and the implementation of outreach programs to lower barriers for foreign vendors.(310) They would also include greater honesty about the limitations of the U.S. constitutional structure. That structure endows Congress with a potent role in the public procurement process and constrains aspirations to commercial efficiency. The United States would do well to exercise caution when touting its businesslike procurement system abroad since political favors to congressional constituencies play a significant role in defense procurement.(311)

The EU can also do its part to encourage friendly relations. High among its priorities ought to be dispelling lingering worries that the Defence Directive will be used to discriminate against U.S. contractors.(312) While the EU has so far "maintained a position of ostensible neutrality concerning third country participation", it should make that position explicit.(313) It should also cast aside heavy-handed tactics such as the IPI (Section 3.3.2), which only embitters trade negotiations and, if enacted, would exacerbate existing tensions. If unfamiliarity with the idiosyncrasies of 28 distinct systems discourages foreign tenders, perhaps the EU should devote resources to outreach programs to stimulate competition, especially from smaller firms.(314) Foremost, the EU should reconsider its specious

(307) See D.B. MILLER, "Is it Time to Reform Reciprocal Defense Procurement Agreements?", *Pub. Cont. L.J.*, 2009, pp. 93, 107-108, predicting that "the more Europe perceives American trade policy as protectionist, the more apt Europe is to impose retaliatory measures" and warning that "prospects for such a tit-for-tat exchange have no doubt been heightened by the circumstances surrounding cancellation of the Air Force refueling tanker".

(308) See J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 4, observing that "risks of 'fortress-like' conduct on both sides of the Atlantic are interactive" and that "policies and attitudes" trigger reciprocal responses.

(309) See below Section 5.2.2.

(310) See U.S.-Crest, "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries", *op. cit.*, p. 88.

(311) See above Section 2.2.2. See also D.I. GORDON and G.M. RACCA, "Integrity challenges in the EU and U.S. procurement systems", in *Integrity and Efficiency in Sustainable Public Contracts* (G.M. RACCA and C.R. YUKINS eds), Brussels, Bruylant, 2014, pp. 117, 142, noting that the United States tolerates political activity that is tantamount to corruption: "lobbying and contributions to political campaigns mean that large amounts of money pass between private actors and government officials".

(312) See L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 7, noting that U.S. commentators have "inevitably identified the potential for certain provisions to become disguised market barriers [...] against US contractors".

(313) *Ibid.*, pp. 447-448.

(314) See U.S.-Crest, "The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries", *op. cit.*, p. 88.

complaints about the trade imbalance, and recognize that such concerns rest on the outmoded premises of mercantilist economics. The next section elaborates on this topic.

### 5.2.2. Debunking the trade imbalance

Europeans have long decried the *imbalance* in the defense trade.<sup>(315)</sup> That imbalance is both large<sup>(316)</sup> and longstanding.<sup>(317)</sup> While this is due in part to U.S. protectionism, that is not the whole story. The very notion of a trade “imbalance” derives from the mercantilist theory that Adam Smith debunked in 1776.<sup>(318)</sup> But setting aside competing theories of international trade, there are several explanations for the trade imbalance other than U.S. protectionism.

U.S. defense contractors are often more efficient due to economies of scale.<sup>(319)</sup> Not only do EU Member States spend less than the United States, their production is divided among 28 separate markets<sup>(320)</sup> with small production runs.<sup>(321)</sup> EU competitors also have to add the cost of shipping their exports to the United States, making their wares even more expensive.<sup>(322)</sup>

Perhaps the most salient fact is that the trade imbalance closely tracks R&D spending. The trade imbalance is a ratio of roughly 5:1 or 6:1.<sup>(323)</sup> Likewise, the United States outspends the EU on R&D by a ratio of 6:1.<sup>(324)</sup> U.S. defense contractors enjoy a windfall from the federal government’s spending

(315) See W. WALKER and S. WILLETT, “Restructuring the European Defence Industrial Base”, *op. cit.*, p. 155, reporting that the “imbalance in favour of the United States in its transactions with its Western European allies has been a constant source of irritation”.

(316) See J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 27, reporting that U.S. defense exports to Europe “dwarf” the EU defense exports to the United States both in absolute and relative terms.

(317) See U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 19, reporting that the trade imbalance has been “more or less constant over the last 20 years”.

(318) Long story short, if trading were not in nations’ mutual interest, they would stop.

(319) See E. KLEPSCH, *Two-way Street: USA-Europe Arms Procurement*, *op. cit.*, pp. 26-27.

(320) M. STAPLES (ed), *The Future of European Defence: Tackling the Productivity Challenge*, *op. cit.*, pp. 14-15, reporting that although the EU spends less than half what the United States does, it funds six times as many weapon systems and if the European defense industry were as consolidated as in the United States “batch sizes would be 570 percent bigger”.

(321) See E. KLEPSCH, *Two-way Street: USA-Europe Arms Procurement*, *op. cit.*, p. 30, reporting that small production runs are Europe’s fundamental problem.

(322) U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 45, explaining that “market forces favour assembly lines in the US” because the United States buys a larger share of defense goods and services than any country in the world.

(323) J.P. BIALOS, C.E. FISHER and S.L. KOEHL, *Fortresses & Icebergs: The Evolution of the Transatlantic Defense Market and the Implications for U.S. National Security*, *op. cit.*, p. 27.

(324) U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 16.

priorities.(325) R&D spending priorities results in qualitative differences. Perhaps the United States buys more from domestic suppliers mainly because they offer products that are qualitatively better. If so, then European expectations for a strict balance of trade are misplaced.

Finally, it bears mentioning that although the United States exports more defense goods and services to Europe than it imports, overall trade flows favor the EU (to the extent that such an imbalance “favors” one side from a mercantilist perspective).(326) Overall, the EU exports far more to the United States than it imports – and this holds true not only for U.S./EU trade generally but also for public procurement.(327) So it seems strange to fixate on one sector and to demand parity. If the mercantilist trade philosophy reigns and a nation is “winning” in overall trade flows, why should it matter if the EU is “losing” in a few isolated sectors?

### 5.2.3. Reforming export control regimes

As mentioned, ITAR has “long put off” and even “actively denied [...] European firms from entering the U.S. market”.(328) Lowering this barrier would be perhaps the most promising reform to the transatlantic defense market. In the short run, the U.S. government should seek to educate foreign firms that may be intimidated by this complicated restriction on technology exports.(329) In the longer run, the United States should create a transatlantic “general license” that would waive ITAR’s strictures for members of the transatlantic alliance.(330) This would present “an historic opportunity [...] for harmonization of export control regimes across the Atlantic given the attention being paid to the issue on both sides of the Atlantic”.(331)

(325) *Ibid.*, p. 7, noting that this sector remains “grossly in favour of the United States but this imbalance in market share is not greater than the imbalance in defense spending and investment between the U.S. and Europe”.

(326) U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, p. 40.

(327) See G. GAMBINI, R. ISTATKOV and R. KERNER, “USA-EU – International Trade and Investment Statistics, EU and United States form the largest Trade and Investment Relationship in the World”, *op. cit.*, p. 4, reporting that the trade balance is “positive”, meaning that EU’s exports to the United States are greater than its imports from the United States; General Accounting Office, *International Trade: Foreign Sourcing in Government Procurement*, GAO-19-414, 2019, pp. 20-22, reporting that in 2015 the U.S. federal government bought \$2.8 billion from European contractors, whereas EU member states bought only \$300 million from American contractors.

(328) D. FLOTT, “The ‘TTIP-ing Point’: How the Transatlantic Trade and Investment Partnership Could Impact European Defence”, *op. cit.*, p. 17.

(329) U.S.-Crest, “The Nature and Impacts of Barriers to Trade with the United States for European Defence Industries”, *op. cit.*, pp. 45, 51.

(330) *Ibid.*, p. 90.

(331) *Ibid.*, p. 5.

#### 5.2.4. Consolidation versus specialization

Received opinion says that European defense contractors must consolidate to achieve the economies of scale necessary to compete with U.S. contractors. Commentators often repeat this mantra.<sup>(332)</sup> There is a logic to it. But it is strange that a country that is so paradigmatically a free trade advocate prescribes collectivism for defense acquisitions.<sup>(333)</sup> Attempts to consolidate in Europe have repeatedly foundered,<sup>(334)</sup> not least because nations treasure their independence in this area.<sup>(335)</sup> Even if there is too much product differentiation in Europe, too much consolidation is also not without costs.<sup>(336)</sup> The United States's own consolidation, for example, may have gone too far, with an industry that is now characterized by a few large firms that exercise market power.<sup>(337)</sup>

There is an alternative. Rather than consolidation, perhaps the better course would be to specialize and pursue a “core competency strategy”.<sup>(338)</sup> Some have suggested that this was the obvious strategy for post-Cold War Europe, but instead it sought consolidation.<sup>(339)</sup> The result of this consolidation has been that a few multinational firms dominate both U.S. and EU defense industries. Whereas multinational firms were once favored, they are now increasingly in disrepute.<sup>(340)</sup> It may prove unfor-

(332) For example, *see* the National Defense Authorization Act of 1976, Section 803(c), saying “It is the sense of Congress that standardization of weapons and equipment within the North Atlantic Alliance on the basis of a two-way street between Europe and North America could only work in a realistic sense of the European nations operated on a united and collective basis”.

(333) K. HARTLEY, “The Political Economy of NATO Defense Procurement Policies”, in *International Military Equipment Procurement Partnerships: The Basic Issues*, *op. cit.*, pp. 98, 112, noting the “paradox” that a free market economy like the United States would propose “socialist solutions”.

(334) *See* S.G. NEUMAN, “Defense Industries and Global Dependency”, *op. cit.*, p. 442, recounting that “attempts to create a unified market and to end costly industrial duplication have foundered on concerns about national sovereignty, the security of supply, and the conflicting strategic interests of Europe’s small and large countries”.

(335) *See* K. HARTLEY, “The Future of European Defence Policy: An Economic Perspective”, *op. cit.*, p. 112, noting that EU consolidation has failed in part because nations prefer their independence; S.G. NEUMAN, “Defense Industries and Global Dependency”, *op. cit.*, p. 438, noting that the “dark side” is “dependency” and “forgoing the production of one or more classes of weapons means the military can no longer initiate a full range of military operations”.

(336) *See* K. HARTLEY, “The Political Economy of NATO Defense Procurement Policies”, in *International Military Equipment Procurement Partnerships: The Basic Issues*, *op. cit.*, pp. 98, 99, noting that “it is possible that there is ‘too much’ and product differentiation within NATO, but reductions are not costless and complete elimination might not be worthwhile”.

(337) *See* J.S. ZUCKER, “The Boeing Suspension: Has Increased Consolidation Tied the United States Department of Defense’s Hands?”, *PPLR*, 2004, pp. 260, 262, 276, explaining that the “drastic consolidation” created an oligopoly and is “making it difficult to suspend or debar mega-defence contractors”.

(338) *See* S.G. NEUMAN, “Defense Industries and Global Dependency”, *op. cit.*, p. 443.

(339) *See* W. WALKER and P. GUMMETT, “Nationalism, Internationalism, and the European Defence Market”, *op. cit.*, p. 18, observing that specialization was an “obvious solution” but that “[b]y and large, this did not happen”.

(340) *See* gen. Briefing, “The Retreat of the Global Company”, *Economist*, 3 February 2017, pp. 18-22.

tunate if Europe finishes its defense industry consolidation project just as scholars and business leaders begin to question the efficiency of sprawling organizations.(341)

### 5.3. A near-term strategy for avoiding non-tariff barriers: the U.S. foreign military sales program as a model for collaborative procurement

The United States's Foreign Military Sales (FMS) program presents an alluring model for furthering transatlantic defense collaboration and perhaps beyond. This section describes the FMS program, defines collaborative procurement under the EU procurement directives, and then explains how FMS is compatible with collaborative procurement, how it may further the transatlantic defense trade, and how it could serve as a model for wider procurement policy.

#### 5.3.1. The U.S. foreign military sales program

Among the United States's primary foreign policy tools is foreign military assistance, whereby America transfers defense equipment to friends and allies.(342) FMS is species of U.S. security assistance, which traces its lineage to 1941 assistance to the British during World War II through the Lend-Lease Program.(343) For three decades, the United States transferred defense gear to Cold-War allies under precursors to FMS.(344) Congress established FMS in its current form in the late 1970s.(345)

Under the auspices of the FMS program, the U.S. government either sells from its own stockpiles or serves as middleman between U.S. defense contractors and foreign governments.(346) It is the latter that is of most interest because FMS allows U.S. defense contractors to avoid the complications that arise from selling abroad, such as securing export licenses(347) and domestic requirements such as full and open competition.(348) Governments have the

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(341) *Ibid.*

(342) A.B. GREEN, *International Government Contract Law*, New York, West, 2011, pp. 109-110.

(343) *Ibid.*, p. 110.

(344) *Ibid.*, pp. 110-111.

(345) *Ibid.*, pp. 111-112, citing 22 U.S.C. §§ 2751-2799, originally known as the Foreign Military Sales Act and now known as the Arms Export Control Act. See A.J. PERFILO, *Foreign Military Sales Handbook*, Toronto, Thomson, 2016, §§ 1.4 and 1.5 for a description of the deep differences in President Carter's and Reagan's FMS policies.

(346) Security Assistance Management Manual, § C4.4.1, [www.samm.dsca.mil/](http://www.samm.dsca.mil/), accessed 4 July 2019, "Defense articles or services may be sold from DoD stocks, or the DoD may enter into contracts to procure defense articles or services on behalf of eligible foreign countries or international organizations".

(347) A.B. GREEN, *International Government Contract Law*, *op. cit.*, p. 113, noting that FMS alleviates the need for contractors to secure export licenses.

(348) For example, one of the cornerstones of the U.S. federal procurement system is the Competition in Contracting Act (CICA), but foreign governments may waive full and open competition when purchasing via the FMS program. A.J. PERFILO, *Foreign Military Sales Handbook*, *op. cit.*, § 4.12, citing

option of buying most defense products directly from U.S. contractors,(349) but they vote with their feet: fully 90% of U.S. defense exports are consummated through the FMS program.(350)

The U.S. is the world's largest defense exporter(351) in part because it sells superior wares, but perhaps the FMS program also explains its dominance. FMS is much more than clever marketing. It reduces uncertainties and transaction costs for buyers and sellers.(352) This intermediary service isn't free. The United States demands a surcharge.(353) Rapid growth in FMS in the past two decades, however, suggests this is a price that foreign buyers willingly pay.(354)

Perhaps the secret to FMS's success lies in the nature of the contractual relationship. Entering into an FMS agreement entails paying the U.S. government to buy from contractors on their behalf.(355) Privity of contract lies not with the manufacturer but with the middleman. The buyer thereby benefits from the same terms and conditions that would apply if the United States were buying on its own behalf. Such benefits would include economies of scale, contract management expertise, and a predictable legal system.(356)

### 5.3.2. Collaborative procurement in the EU

Collaborative procurement in a defense context is a term of art. It refers to a practice whereby Member States "agree to procure defence equipment and fund its development and/or production in common".(357) Many hope it can solve the EU's defense procurement problems.(358) Thus far such hopes seem to have been misplaced.(359) One commentator went so far as to say that the

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FAR, § 6.302-4; 10 U.S.C. § 2304(e)(4).

(349) A.B. GREEN, *International Government Contract Law*, *op. cit.*, p. 113, explaining that in 2011 about 40 defense articles were available only through the FMS program and could not be purchased through direct commercial sale.

(350) A.J. PERILLO, *Foreign Military Sales Handbook*, *op. cit.*, § 1.2.

(351) *Ibid.*, § 1.1.

(352) *Ibid.*, p. 113.

(353) *Ibid.*, § 3.19, explaining that by statute FMS must be managed at no cost to the United States, citing SAMM C.9.3.1.

(354) *Ibid.*, § 1.2, reporting that annual FMS sales averages \$10 billion in the 1990s, climbed to \$20 billion in the aughts, and is hovering around \$30 billion the in the past decade.

(355) *Ibid.*, § 3.3, explaining that the DoD "uses the same procedures and mechanisms when conducting procurements for its own use" and the same federal acquisition law applies – the FAR, DFARS etc.

(356) A.B. GREEN, *International Government Contract Law*, *op. cit.*, p. 113.

(357) B. HEUNINCKX, "A Primer to Collaborative Defence Procurement in Europe: Trouble, Achievements, and Prospects", *PPLR*, 2008, p. 123.

(358) *Ibid.*, pp. 124-125, listing economies of scale, greater interoperability, stable funding for defense R&D, stronger ties among participating States, and technology transfer among the benefits that Member States hope for.

(359) *Ibid.*, pp. 131-139, demonstrating collaborative procurement undermines interoperability, delays development, and increases costs.

only thing worse than Member States' fragmentation in defense procurement is their collaboration.(360)

Collaborative procurement is indisputably exempted from the Defence Directive and does not apply to contracts awarded in the framework of a cooperative programme based on research and development, conducted jointly by at least two Member States for the development of a new product and, where applicable, the later phases of all or part of the life-cycle of this product.(361)

A closer question, however, is whether the Directive would cover government-to-government purchases from third countries (that is, non-EU Member States).(362) EU defense procurement experts are divided on this point.(363) Whatever the academic answer maybe, as a practical matter most EU countries are FMS purchasers.(364) This essay proceeds on the assumption that FMS is not covered by the Defence Directive and, thus, that FMS purchases remain permissible.(365)

### 5.3.3. FMS as a model for collaborative procurement

Thus far the FMS program has been described mainly as a vehicle for increasing the United States's already favorable balance of trade in defense exports. But it is more than that. The aims of the FMS program's enabling statute are surprisingly compatible with the aims of collaborative procurement under the EU Defence Directives. Four decades ago, the opening section of the Arms Export Control Act recognized that "[b]ecause of the growing cost and complexity of defense equipment, it is increasingly difficult and uneconomic

(360) B. SCHMITT, "The European Union and Armaments: Getting a Bigger Bang for the Euro", in *Chaillot Papers*, Pretoria, ISS, 2003, pp. 10-11, "Ironically, armaments cooperation has often made things even worse" because "cooperative projects have implied complex institutional and industrial settings, creating delays and extra costs".

(361) Dir. 2009/81/EC, Art. 13(c).

(362) A.E. IPPOLITO, *Government to Government Contracts*, in *EU Defence Procurement*, 2014, Cambridge, CUP, pp. 249-250, 261, arguing that the "prevailing view" is that the public procurement directives would not cover FMS purchases, but noting Martin Trybus's disagreement.

(363) Cf. *ibid.*, pp. 250, 261 (not covered). B. HEUNINCKX, "Lurking at the Boundaries: Applicability of EU Law to Defence and Security Procurement", *PPLR*, 2010, p. 91 (not covered). And E. ANDRESEN, "The New EU Defense and Security Procurement Directive", *Colum. J. Eur. L.*, 2011, p. 22 (not covered); with M. TRYBUS, "The Tailor-made EU Defence and Security Procurement Directive: Limitation, Flexibility, Descriptiveness, and Substitution", *ELR*, 2013, p. 3, arguing FMS is covered because otherwise such purchases would violate Art. 11's anti-circumvention provision and citing three compatriots who agree with him.

(364) Accurately calculating FMS spending is hard. For estimates based on historical purchases over the previous 10 years, see FY 2010 Congressional Budget Justification, Foreign Assistance, Title IV Supporting Information, 2009, accessed 4 July 2019 at <https://2009-2017.state.gov/f/releases/iab/fy2010cbj/pdf/index.htm>, pp. 2-6, listing most EU Member States.

(365) Even if the Defence Directive applies to third-country transactions such as FMS purchases, it remains unclear what effect the Directive would have. See L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 412. Practically speaking, most Member States regularly employ FMS purchases, and theoretical arguments that would forbid FMS seem futile. See *ibid.*, p. 367.

for any country [...] to fill all of its legitimate defense requirements from its own design and production base”.(366)

“Accordingly,” the preamble to the statute continues,

“it remains the policy of the United States to facilitate the common defense by entering into international arrangements with friendly countries which further the objective of applying agreed resources of each country to programs and projects of *cooperative exchange of data, research, development, production, procurement, and logistics support* to achieve specific national defense requirements and objectives of mutual concern”.(367)

This “cooperative exchange” resonates with the Defence Directive’s exception for cooperative R&D among Member States.(368) Perhaps FMS would be more regularly used if the United States saw it as an opportunity to enter what would be effectively collaborative research, development, and procurement projects with its European allies.

If the FMS program is imperfectly implemented, two features may deserve emulation and definitely merit further study. First, FMS lowers the transactions costs for both buyers and sellers and thereby encourages cross-border procurement on a massive scale, no small feat given how much the EU has struggled to stimulate cross-border procurement among Member States. Just how it does this is not a simple matter and would be an essay unto itself, but perhaps the answer lies partly in the second feature.

Unlike most collaborative procurement, which is purely government-to-government or at least orchestrated by and among governments, FMS crucially involves a private party that can freely walk away from uneconomic deals. This may introduce an element of market rigor that is often missing. FMS may function as a *simulacrum* of a free market – not as good as the real thing, but less dysfunctional than how public procurement “markets” usually work.

As noted, the FMS model is imperfect. The premium for having the U.S. government contract on another country’s behalf is not insignificant.(369) FMS is subject to the whims of U.S. foreign policy, which are sometimes unpredictable.(370) Buyers have been disappointed to learn that without privity of

(366) 22 U.S.C. § 2751.

(367) *Ibid.* (emphasis added).

(368) Dir. 2009/81/EC, Art. 13(c).

(369) The surcharge totals 4.7%, the sum of the Contract Administration Services rate (1.2%) and the Administrative Surcharge rate (3.5%). Defense Security Cooperation Agency, News Release, 3 November 2013, [www.dsca.mil/news-media/news-archive/cost-foreign-military-sales-reduced](http://www.dsca.mil/news-media/news-archive/cost-foreign-military-sales-reduced).

(370) A. J. PERILLO, *Foreign Military Sales Handbook*, *op. cit.*, § 1.1, describing the political tension arising from FMS given that it implicates sensitive questions about foreign and trade policy, domestic employment, and national security; *ibid.*, §§ 1.4 and 1.5, describing the massive swings in FMS policy from the Carter to the Reagan administrations.

contract they lack standing and cannot sue in U.S. federal court.(371) This list is hardly exhaustive. Yet despite such shortcomings, FMS may serve as an innovative model not just for collaborative defense procurement but for collaborative procurement generally.

## 6. Conclusion

Perhaps more questions have been raised in this essay than answers have provided; many loose ends remain. It has attempted to introduce some problems of mutual understanding that have created non-tariff barriers and to provide some options for addressing those barriers.

Because the comparative discussion across the Atlantic has been limited thus far,(372) scholars now have an opportunity to make a practical contribution to defense procurement:

“unlike in the context of public procurement in which comparative legal analysis has largely grown in response to regional and international initiatives, there is now a real opportunity for comparative legal analysis to directly inform rather than simply respond to regional and international initiatives. Ultimately, a clearer legal and empirical understanding which may result from comparative analysis could improve the quality of the decision-making of policy-makers and legislators tasked with ensuring not only that defence procurement regulation is effective to meet national objectives but also, increasingly, objectives of regional and international trade”.(373)

To this end, this essay has sketched out the historical, constitutional, and legal underpinnings of the public procurement systems in the United States and the EU. The goal has been to directly inform the free trade initiatives that are on the horizon for the transatlantic defense market.(374)

Cross-border defense procurement within the EU remains limited. If the past is any guide, Europe’s prospects for achieving further liberalization of its own accord seem dim.(375) Paradoxically, hope for freeing up European defense lies farther afield – given that most of the integration within Europe

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(371) See *Secretary of State for Defence v. Trimble Navigation Limited*, 484 F.3d 700, 707-09 (4th Cir. 2007), holding that the purchasing government under an FMS government is not granted third-party beneficiary status and therefore cannot bring direct legal action against the defense contractor.

(372) L.R.A. BUTLER, *Transatlantic Defence Procurement: EU and US Defence Procurement Regulation in the Transatlantic Defence Market*, *op. cit.*, p. 438.

(373) *Ibid.*, p. 374.

(374) *Ibid.*

(375) See C. CRANE, “Dealing with Reality: the Difficulties of European Consolidation”, in G. ADAMS, *et al.*, *Europe’s Defence Industry: A Transatlantic Future?*, *op. cit.*, p. 22, observing that “[t]he obstacles to pan-European consolidation remain immense – namely the political, philosophical, psychological and cultural differences, not to mention the many vested interests, which divide the European nations”.

has happened in cooperation with the United States.(376) Interest in a defense industry that “straddles the Atlantic” has been longstanding.(377) Perhaps a TTIP that includes defense could serve as a catalyst to rationalize the European arms industry.(378) Problems would remain. Even if the TTIP were enacted, surmounting the barriers described in this essay would be challenging.(379) Nonetheless, given the mounting costs of cosseted defense industries, freeing up the arms trade among NATO countries (of whom there is a substantial overlap with EU Member States) is an idea whose time has come. Such a program would entail more than removing or mitigating overt barriers; it would require further scholarship to deepen mutual understanding and thereby identify and remove the disguised barriers to trade.

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(376) See F. MÉRAND and K. ANGERS, “Military Integration in Europe”, *op. cit.*, p. 2, reporting that although post-war Europe has achieved some military integration, “Most of this integration has taken place in the context of the Atlantic Alliance”.

(377) M. EDMONDS, *International Military Equipment Procurement Partnerships: The Basic Issues*, *op. cit.*, p. 13.

(378) See D. FIOTT, “The ‘TTIP-ing Point’: How the Transatlantic Trade and Investment Partnership Could Impact European Defence”, *op. cit.*, p. 15, arguing that the TTIP could “shift the terms of reference for European defence markets and defence policy completely”; *ibid.*, p. 25, “could provide the push that European defence-industrial integration needs”.

(379) See also G. ADAMS, “The Necessity of Transatlantic Defence Co-operation”, in *Europe’s Defence Industry: A Transatlantic Future?*, *op. cit.*, pp. 42, 48, predicting that the “transatlantic route is not an easy one; it will doubtless suffer many setbacks”, but “[o]ver time [...] it promises a more competitive future for the defence industry; more cost-effective acquisitions for allied governments; and greater efficiency of coalition operations, inside or outside Europe”.



## CHAPTER 17

### Electronic Means as an Approach to Public Purchasing

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#### *1. Introduction: Electronic Tools for the Public Procurement Cycle Management*

Inefficiencies caused by maladministration in public contracts (passive waste) and/or corruption (active waste) in public procurement(1) can affect the entire public procurement cycle from the needs assessment through the contract execution.(2)

Information and Communication Technologies (ICT) play a major role in addressing inefficiencies in public procurement. ICT can innovate the public procurement cycle management (innovation in the process – how to buy) and provide the means to innovate public services and public entities' activities through the subject matter of the contract (innovation in the works / goods / services – what to buy).(3)

According to relevant EU Commission policies, the switch from traditional and paper-based processes to electronic processes may be an end-to-end process, or a limited process involving only some of the phases in the

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(1) O. BANDIERA, A. PRAT and T. VALLETTI, "Active and passive waste in government spending: Evidence from a policy experiment", *Am. Econ. Rev.*, 2009, pp. 1278-1308. See also R. DI TELLA and E. SCHARGRODSKY, "The role of wages and auditing during a crack down on corruption in the city of Buenos Aires", *J. L. & Econ.*, 2003, pp. 269-292.

(2) EU Comm., "Single Market Scoreboard", ed. July 2017. The indicators used are: awarding procedure with "One Bidder"; "No Calls for Bids", "Publication Rate", "Cooperative Procurement", "Award Criteria", "Decision Speed", "Missing Values", "Missing Calls for Bids", "Missing Registration Numbers". The different levels of performance in the efficiency of contracting activities in the EU Member States shows how a complete efficiency of the Internal Market may be achieved by reducing waste through the strategic use of techniques and instruments to favor competition in the relevant markets to reduce "waste in government spending".

(3) PwC, *The Strategic Use of Public Procurement for Innovation in the Digital Economy*, Report for EU Comm., DG Communication Network, November 2018, pp. 17-20. The distinction between "what to buy" and "how to buy" was made in the EU Comm., "Green Paper on the modernisation of EU public procurement policy Towards a more efficient European Procurement Market", 2011, pp. 35 and ff.; OECD, "Recommendation on Public Procurement", 2015.

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procurement cycle.(4) At the EU level, the introduction of e-procurement has been a part of the ambitious e-government program for years,(5) an approach that intends fundamentally to transform the delivery and performance of public administration.(6) Despite the indisputable benefits and ambitious political targets, the 2010/2012 data highlighted that only 5-10% of procurement procedures that were carried out across the EU had actually used e-procurement.(7) Denmark, Sweden, Finland, and Netherlands were identified by the 2018 Digital Economy and Society Index (DESI) as the most advanced digital economies in the EU, followed by Luxembourg, Ireland, the UK, Belgium and Estonia. Romania, Greece and Italy had the lowest DESI scores.(8)

The use of electronic means is conditioned by a number of factors, including legislation, acceptance of stakeholders, available technology, and suitability of an electronic process (some of which are technically complex) to a particular stage or subject matter of the procurement process.(9)

This chapter aims to review key resources on the public procurement cycle, more particularly, on how the use of e-procurement can improve the implementation of a demand-driven project in public administration (e.g. the dissemination of information directly through only one national public procurement

(4) EU Comm., “Communication on End-to-End Procurement”, July 2013. See C.H. BOVIS, “The Efficiency Drive to Deliver Savings for the European Public Sector: Full E-Procurement for All Public Purchases by 2016”, *EPPPLR*, 2012, p. 85.

(5) See IDC, *Study on e-Procurement Measurement and Benchmarking – D2 e-Procurement State of Play Report*, 17 June 2013, p. 14.

(6) See EU Comm., “International Digital Economy and Society Index 2018,” SMART 2017/0052, pp. 27 and ff.; EU Comm., “EU e-Government Action Plan 2016-2020. Accelerating the digital transformation of government”, COM(2016) 179 final, 19 April 2016.

(7) By comparison, a full online procurement market place has already been achieved in Korea, which generated savings for US\$4.5 billion (about 8% of total annual procurement expenditure) annually by 2007; in Brazil 80% of public procurement is carried out electronically. EU Comm., “e-Procurement”. According to EU data, given the size of the total public procurement market in the EU, each 5% saved could return around €100 billion to the public purse. Contracting authorities and entities that have already made the transition to e-procurement commonly report savings between 5 and 20% and a rapid recovery of the related investment costs. See also *e-Procurement Uptake Final Report*, Prepared for DG GROW, 23 April 2015, available at [ec.europa.eu/docsroom/documents/10050/attachments/1/translations/en/renditions/native](http://ec.europa.eu/docsroom/documents/10050/attachments/1/translations/en/renditions/native).

(8) EU Comm., “International Digital Economy and Society Index 2018”, aforesaid. In 2017, all Member States improved in the DESI. Ireland and Spain progressed the most (close to 5 points as opposed to an EU average of 3.2). On the other hand, there was a small increase in Denmark and Portugal (below 2 points).

(9) OECD, “e-Procurement”, *SIGMA Public Procurement Briefs*, No. 17, 2011. B. JULLIEN, “Pricing and other business strategies for e-procurement platforms”, in *Handbook of Procurement* (N. DIMITRI, G. PIKA and G. SPAGNOLO eds), Cambridge, CUP, 2006, pp. 249-266. E-Procurement platforms are often not user-friendly, and trying to access and learn how to use them is often considered by economic operators particularly time-consuming and inefficient. R. BICKERSTAFF, “E-procurement under the new EU procurement Directives”, *PPLR*, 2014, No. 3, pp. 134-147. See also P. FERK, “Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?”, *EPPPLR*, 2016, p. 327; PwC, *e-Procurement Golden Book of good practices*, report prepared for EU Comm., 11 March 2013, p. 8.

platform – in some national legal frameworks, it is mandatory to publish the information in the Web profile of the contracting authority),(10) and to highlight the importance of political commitment at the national level for an effective use of e-procurement tools.(11)

## ***2. Innovation through e-Procurement in the ‘Pre-Awarding Phase’***

The correct definition of needs, including the collection of relevant information from the market, is essential in designing the best public procurement strategy.(12) In every public procurement procedure, the proper management of the pre-award phase should result in a procurement strategy that is designed to favor best value for money during the execution phase. The use of electronic means promotes efficiency in this phase by allowing the use of data from previous award procedures. It can also promote a wider participation of stakeholders (not only prospective bidders) during the preliminary activities. The accessibility of available data through interoperable electronic means can help contracting authorities use these data in defining the best procurement strategy according to their needs and the characteristics of the relevant market.(13) In addition, these data may mitigate some of the procurement risks, such as a failure of the procurement procedure due to a lack of interested economic operators, or because none of the submitted tenders are acceptable.

Moreover, the use of electronic means in this phase can enhance market engagement activities (e.g., market research, ‘preliminary market consultation’,(14) market soundings, the publication of Prior Information Notice – PIN, and industry/info days to explain the project to potential tenderers), and thereby encourage interest from economic operators, which can later

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(10) E.g. Italy. *See* the Italian Public Contracts Code, Legislative Decree, No. 50 of 2016, Art. 73(4), and the Ministerial Decree (Italian Ministry of Infrastructure and Transport), 2 December 2016, on the Definition of the general addresses for publication of contract notices.

(11) EU Comm., “Benchmarking of national policy frameworks for innovation procurement across the 28 European Member States”.

(12) In this book, *see* the chapter of J.M. GIMENO FELIU, “Public Procurement as a Strategy for the Development of Innovation Policy”. *See also* PwC, Study for the EU Comm., “Strategic use of public procurement in promoting green, social and innovation policies”, December 2015, available at [ec.europa.eu/docsroom/documents/17261](http://ec.europa.eu/docsroom/documents/17261).

(13) Gathering information about conditions that affect a marketplace can be useful in defining the most appropriate award procedure, the criteria for the tenders’ evaluation, the number and characteristics of lots, the terms of the procurement documents (overcoming e.g. the risk of collusion between economic operators, subcontracting arrangements and anticompetitive behavior). P. ALEXIA GIOSA, “Division of Public Contracts into Lots and Bid Rigging: Can Economic Theory Provide an Answer?”, *EPPPLR*, 2018, pp. 30-38.

(14) EU Dir. 2014/24, Art. 40.

stimulate their participation. It also ensures accountability and compliance with EU principles on transparency, equal treatment and prior involvement of economic operators through traceability of the provided information.

A technical e-dialogue with stakeholders (not only with economic operators, but also with trade associations, end-users, academia, and experts) helps in defining efficient solutions, and in generating wide interest and response while ensuring that sound and uniform information are provided to all interested parties.<sup>(15)</sup> A digital platform can enhance participation and ensures more transparency and traceability in the exchange of communications, which contributes to stimulating their interest in participating in the subsequent awarding procedure. Electronic tools can provide fast and structured information to economic operators on potential business opportunities, existing possibilities for innovation, and contract notices, as well as information on the specific needs of the contracting authorities and the characteristics of the relevant market.<sup>(16)</sup>

Electronic means offer many opportunities, but they must be used correctly.<sup>(17)</sup> In all communication, exchange and storage of information, contracting authorities must ensure that the integrity of data and the confidentiality of tenders and requests to participate are preserved.

### ***3. Innovation through e-Procurement in the ‘Awarding Phase’***

According to EU rules on public contracts, ‘electronic means’ refers to the “electronic equipment for processing, storing, digitally compressing, and transmitting/receiving information via wires, radio waves, optical means or other electromagnetic transmissions”.<sup>(18)</sup> In the award procedure, this equipment plays an important role not only in spreading, collecting and processing information, but also in reducing transaction and communication costs. In fact, the EU rules require that information in relation thereto, including any expression consisting of words or figures which can be read, reproduced and subsequently communicated, including information that is transmitted and

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(15) This is particularly relevant for the demand of innovative solutions in which the prior engagement of the private sector can stimulate innovation in it. O.S. PANTILIMON VODA, “Innovative and sustainable procurement: framework, constraints and policies”, in *Research Handbook on EU Public Procurement Law* (C.H. BOVIS ed.), Cheltenham, Edward Elgar, 2016, p. 220.

(16) EU Comm., “Guide on dealing with innovative solutions in public procurement. 10 elements of good practice”, SEC(2007) 280, 2007, pp. 17-18.

(17) EU Comm., “Commission notice. Guidance on Innovation Procurement”, 15 May 2018, C(2018) 3051 final, p. 31.

(18) EU Dir. 2014/24, Art. 2, par. 1 (19).

stored by electronic means, must be ‘written’ or ‘in writing’.(19) The correct use of electronic tools can generate a wider interest in the awarding procedure, standardize information given to all the interested economic operators, and enhance participation especially in cross-border and transnational transactions. Moreover, electronic means of communications assure traceability of information and communication to the economic operators, which will eventually prevent possible criticism.

An incorrect application of communication rules may result in an infringement of EU principles on transparency and non-discrimination.(20)

In addition, the EU provisions require that all electronic means of communications, including various devices for communication by electronic means as well as their technical characteristics, shall be non-discriminatory, generally available and interoperable with the ICT products in general use, and accessible (*i.e.*, must not restrict the economic operators’ access to the procurement procedure).(21)

The use of e-communication(22) in all stages of procurement was introduced only in 2012,(23) and this paved the way to the gradual introduction of e-procurement in contractual activity. While the 2014 EU Procurement Directives provide mandatory e-communication requirements, Member States were, however, allowed to postpone their application, more particularly the provision on e-submission, until 18 October 2018.(24) The Directive also includes a special provision for central purchasing bodies (CPBs), which limits the allowed period for deferment of implementation of the e-communication requirements to only 36 months, instead of 54. Member States could only postpone the mandatory e-communication requirements for CPBs until

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(19) *Ibid.*, par. 1 (18).

(20) For instance, a contracting authority which does not inform all participants of specific decisions in the course of the procedure violates the requirement of non-discrimination, while the failure to publish an addendum to a contract notice (e.g. in case the contracting authority extends the time period for receipt of applications or tenders but does not publish a notice concerning the change) compromises the requirement for transparency in public procurement.

(21) EU Dir., 2014/24, Art. 22 (1).

(22) The concept of oral communications would seem to cover communication by telephone, video-link and other means from a distance, as well as face-to-face communication. See S. ARROWSMITH, *The Law of Public and Utilities Procurement. Regulation in the EU and UK*, London, Sweet & Maxwell, 2014, p. 639. Moreover, EU rules allow “oral communication” in respect of communication other than the essential elements of the awarding procedure (EU Dir. 2014/24, Art. 22 [12]).

(23) EU Comm., “E-Procurement Strategy”, 20 April 2012, COM (2012), p. 179.

(24) EU Dir. 2014/24, aforesaid, for dynamic purchasing systems, electronic auctions (e-auctions), e-catalogues, procurement procedures conducted by central purchasing bodies, drafting and transmission of notices, and electronic availability of procurement documents, the normal transposition period of 24 months applies, *i.e.* until 18 April 2016. See EU Comm., “Public Procurement guidance for practitioners”, 2018, pp. 14 and ff. For an analysis of Member States’ legal framework, see OECD-SIGMA, “Support for Improvement in Governance and Management Implementing the EU Directives on the selection of economic operators in public procurement procedures”, 6 September 2018.

18 April 2017.(25) One possible reason for this provision was that CPBs were the most suitable contracting authorities to benefit from the use of electronic means.(26)

The transition to electronic procurement, which means re-designing procurement processes in a way that considers the changes induced through information technology,(27) is the minimum requirement that the Directive imposes upon EU Member States. In fact, Member States and contracting authorities remain free to go further in the use of electronic means to favour policies on end-to-end procurement.(28)

As of April 2016, prior information notices, contract notices and contract award notices for contracts above the EU thresholds are electronically available. The electronic submission to the Commission of standardised notices for publication is made through the Tenders Electronic Daily (TED).(29)

TED, the online version of the *Supplement to the Official Journal* of the EU, is a single, accepted and well-used system for the publication of notices for projects above the EU thresholds across the EU, and is supported by compatible infrastructures at the national level.(30) From the demand side, TED allows the publication of relevant notices of a procurement procedure (pre-information notice, contract notice, contract award notice) in 24 official EU languages. This is possible through the standardization of forms for communications(31) and the use of common identification codes at the European level.(32) The use

(25) Where a Member State chooses to postpone the application of e-communication requirements, it must nevertheless provide that contracting authorities may, in the interim period, choose between the following means of communication for all communication and information exchanges: (1) electronic means, (2) post or other suitable carrier, (3) fax, or (4) a combination of any of those means.

(26) G.L. ALBANO and M. SPARRO, "Flexible Strategies for Centralized Public Procurement", 2010, available at [www.rei.unipg.it/rei/article/viewFile/17/23](http://www.rei.unipg.it/rei/article/viewFile/17/23), p. 6.

(27) K. VAIDYA, A.S.M. SAJEEV and G. CALLENDER, "Critical Factors That Influence EProcurement Implementation Success in the Public Sector", *J. Publ. Procur.*, 2006, pp. 70-99, according to which, three steps are usually considered: first, unnecessary process elements should be discarded; second, simplifying the process as much as possible. Only then, in a concluding third step, the process should be automated with a suitable IT system.

(28) EU Comm., "End-to-End E-Procurement to Modernise Public Administration", 2013. The provision of the mandatory use of further electronic means / tools can generate significant savings, facilitate structural re-thinking of certain areas of public administration, and constitute a growth enabler by opening up the Internal Market and by fostering innovation and simplification.

(29) EU Dir. 2014/24, Art. 51 (2).

(30) EU Comm., "Green Paper on expanding the use of e-Procurement in the EU", *op. cit.*, p. 8, where it is reported that "in 2009 just over 90% of forms sent to TED (Tenders Electronic Daily) were received electronically and in a structured format. The electronic publication of notices for below threshold procurement has also advanced at the national or regional level".

(31) EU Comm. implementing Regul. (EU) No. 2015/1986 of 11 November 2015 establishing standard forms for the publication of notices in the field of public procurement and repealing implementing Regul. (EU) No. 842/2011.

(32) E.g. the Common Procurement Vocabulary – CPV and the NUTS classification (Nomenclature of territorial units for statistics). Differently from many national official journals (where the publication often involves a cost charged to the contracting authority or to the future awardee), the EU publication

of IT solutions can simplify the standard forms for the publication of notices, as provided by EU rules.<sup>(33)</sup> The Publications Office takes responsibility for the translations and summaries of the notices received.<sup>(34)</sup>

Notices are published in *OJEU* through the TED Web site within five days from the receipt by the Publications Office.<sup>(35)</sup> There are three ways to submit public contracts notices in structured electronic format: using the eNotices application, contacting an official TED eSender, and becoming an official TED eSender.<sup>(36)</sup>

eNotices is an on-line tool for preparing public contract notices and publishing them in the *OJEU*. It provides access to all the standard forms used in EU public contracts procedure, since eNotices is allowed to standardize notices at the EU level.<sup>(37)</sup>

eSenders is a tool that is used by contracting authorities for a large number of awarding procedures, including notices by central purchasing bodies. National contracting authorities may use this tool if they submit substantial numbers of electronic notices; so, too, may e-procurement software developers use the eSenders tool.<sup>(38)</sup>

The eTendering system integrates and synchronizes TED eNotices within the TED Web site. This e-tool allows free electronic access to call for tenders' documents such as procurement documents, technical specifications, annexes, questions and answers. The contracting authorities can also use this system in managing the preparation of their notices through reports, statistics on documents downloaded, subscribers, etc. The Publications Office of the European

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is free of charge. In this context, in Italy, procurement documents commonly provide that the cost related to the publication of the notices in the *National Official Journal* are to be charged to the awardee. See EU Dir. 2014/24, Art. 51 and 52.

(33) Regul. (EU) No. 842/2011 of 19 August 2011 establishing standard forms for the publication of notices in the field of public procurement and repealing Regul. (EC) No. 1564/2005. L. VALADARES TAVARES (ed.), "Why e-Public Procurement?", in *E-Public Procurement in Europe: Public Management, Technologies and Processes of Change*, p. 18.

(34) C.H. BOVIS, *EU Public Procurement Law*, Cheltenham, Edward Elgar, 2007 p. 66. EU Dir. 2014/24, Art. 51 (3).

(35) Notices submitted by EU institutions are fully translated into all official EU languages and thereafter published within 7 or 12 days depending on their length according to Article 103(1) of the Financial Regulation.

(36) The use of services provided by TED requires registration in the European Commission Authentication Service (ECAS).

(37) EU Regul. No. 2015/1986, establishing standard forms for the publication of notices in the field of public procurement and repealing implementing Regul. (EU) No. 842/2011. ENotices is a free service, which provides an opportunity to check the possible errors in notices, including their compliance with the EU 2014 directives on public contracts.

(38) TED provides free access to business opportunities in the European Union and other States that are in relationship with the EU. A subset of TED data cover public procurement for the European Economic Area, Switzerland, and the former Yugoslav Republic of Macedonia from 1 January 2006 to 31 December 2017. Economic operators from these States can search for procurement notices made by a country, region and business sector (CPV code), and other relevant criteria.

Union produces timely and insightful reports on the transactions within the TED Web site.(39) TED e-Tendering is an added-value extension to TED.(40)

On 20 April 2015, the European Commission launched a pilot project on the use of the *Internal Market Information* (IMI) system to help public authorities check the information provided by tenderers/candidates from other European countries. The IMI system helps public entities from EU countries to verify information and documentation by economic operators in other EU Member States. The exchange of data among public entities can refer to different areas, including public procurement. In fact, this tool is used to check information and documentation provided by companies from other European countries. Although the data show that the tool is increasingly used by public entities in the EU, its use is still very limited if we consider that EU data indicating that there were only 7859 registered authorities as of December 2017. The use of the IMI system can be very useful in enhancing cross-border procurement because it simplifies the exchange of data among public entities in different Member States.(41)

Contracting authorities that opt to do so can likewise send their notices by electronic means to the Publications Office of the European Union.(42) The absence of an automatic translation in all languages, however, can limit the citizens and other stakeholders' access to information in public procurement. The issue on the use of EU languages in public procurement poses risks of undermining opportunities for more participation, including the growth, of European economic operators.

In addition, EU contracting authorities are obliged to offer by electronic means "unrestricted and full direct access free of charge to the procurement documents" from the date of publication of a contract notice or the date on which an invitation to confirm interest is sent.(43) The contract notice or the

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(39) The data is grouped by different parameters, such as: original language of the notices, issuing country, file format and reception channels.

(40) TED e-Tendering is the EU institutions' e-Procurement platform based on EU Directives on public procurement. It provides free electronic access to calls for tenders published by EU institutions, agencies and other bodies. It is integrated and synchronized with TED e-Notices and the TED Web site, where public procurement notices are published.

(41) Contracting authorities may also publish notices for public contracts that are not subject to the publication requirements laid down in the EU Directives. For example, contracts which are below the EU threshold may still be published at the EU level not only to promote the EU principles on public contracts, but also to encourage more cross-border procedures.

(42) EU Dir. 2014/24, Art. 51 (6). The electronic transmission must be made in accordance with the format and procedures for transmission indicated in Annex VIII of the 2014/24 EU Dir. The use of a common database promotes accessibility of information, it does not ensure that all the content of the notices are translated in a common language, most probably because translation of a summary in all languages seems insufficient to assure a wider participation.

(43) EU Dir. 2014/24, Art. 22 (5). R. BICKERSTAFF, "E-procurement under the new EU procurement Directives", *op. cit.*, pp. 134-147.

invitation must specify the internet address at which the procurement documents are accessible. The 2014 EU Directives on public contracts include an exhaustive list of circumstances when contracting authorities may indicate in the notice or in the invitation to confirm interest that the procurement documents will be transmitted by another means rather than by electronic means. It is thus possible to overcome the obligation to communicate electronically.(44)

Many Member States have national databases that are generated by their official journals, public procurement registries or public procurement observatories. These databases represent sources of information that can be used for monitoring national contracting activity. These national databases include contracts which are above and below the EU thresholds, and the data included represent the national procurement systems. However, national databases have several limitations.(45) Some of these databases do not exist in all Member States or their availability or legal use is limited at national or local levels. Interoperability through different national electronic platforms does not allow cross-border data exchange and can be an obstacle for cross-border procurement and/or cooperation between contracting authorities.(46) For example, some of these limitations include the use of Nomenclature of Territorial Units for Statistics code (NUTS). NUTS is a geocode standard for referencing the subdivisions of countries for statistical purposes and for locating an area where goods and services subject to European public procurement legislation are to be delivered. For each EU member country, a hierarchy of three NUTS levels is established by Eurostat in agreement with each Member State.(47) For instance in the case of the Austrian national platform, it has restrictions on the use of NUTS codes.(48) The Austrian publication portal does not allow the use of more than one NUTS code, making it impossible to include both the Austrian and others NUTS codes.(49)

Moreover, the information contained in national databases varies not only regarding the scope of the contracts covered, but also regarding the level of

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(44) There may be exceptional situations when the contracting authorities should be allowed to waive the mandatory use of e-Communication. Such circumstances may be: seeking more security information; technical considerations, such as offered items or documents requiring specific tools that are not available or supported by public applications.

(45) *E-Procurement Uptake Final Report*, prepared for DG GROW, 23 April 2015.

(46) EU Comm., “Interoperability between e-procurement systems and other government databases”.

(47) The subdivisions at some levels do not necessarily correspond to administrative divisions within the country. See [ec.europa.eu/eurostat/web/nuts/background](http://ec.europa.eu/eurostat/web/nuts/background).

(48) See [lieferanzeiger.at](http://lieferanzeiger.at).

(49) See the BBG-SKI report for the EU Comm., “Feasibility study concerning the actual implementation of a joint cross-border procurement procedure by public buyers from different Member States”, 2017.

detail made available to the public.(50) To prevent the duplication of activities (*i.e.*, at the national and EU levels), the EU Parliament suggests “the possibility of interlinking national contract registers with Tenders Electronic Daily (TED) to remove the obligation on contracting authorities to publish the same information in two systems”.(51)

For more interoperability and traceability across the Internal Market, the 2014 EU Directives delegated to the EU Commission the authority to amend(52) the requirements relating to tools and devices for electronic receipt of tenders and requests for participation as well as plans and projects in design contests,(53) the four exceptions from the use of electronic means of communications,(54) and the interoperability of technical formats as well as of process and messaging standards, especially in a cross-border context;(55) that authority was limited only with regard to the procedures to be adopted.(56) The Directive likewise requires the conduct of prerequisite activities such as stakeholder consultation and cost/benefit analysis prior to exercising the authority, thereby, making it difficult to exercise; hence, that authority remains unused.(57) Member States, however, may take an active and coordinated role in enforcing an EU interoperable and transparent eProcurement package.

Nonetheless, a push may be necessary to enforce the use of electronic means, including its inoperability, by Member States. The EU Commission may start by coordinating the activities from its previous and current funded projects on these topics. Moreover, contracting authorities from Member States should be encouraged to apply the process for e-Notice and e-Communication to contracts below the EU thresholds.

Using e-Notifications for contracts with values below the EU thresholds may encourage a wider dissemination of the procurement procedures by contracting authorities. Being the first step towards broader e-procurement, e-Notification in contracts with lower thresholds has a positive impact on e-Procurement as a whole. In addition, countries where the involvement of small and medium-sized enterprises (SMEs) in public procurement is particularly high (e.g. Estonia)(58) can use low thresholds to facilitate the participation of SMEs in public procurement. In this case, SMEs that have limited

(50) PwC, Study for the EU Comm., “Strategic use of public procurement in promoting green, social and innovation policies”, December 2015.

(51) European Parliament Resol. on the public procurement strategy package, *op. cit.*, p. 30.

(52) EU Dir. 2014/24, Art. 22 (7).

(53) Contained in Annex IV of EU Dir. 2014/24.

(54) EU Dir. 2014/24, Art. 22 (1), subpar. II (a)(b)(c)(d).

(55) EU Dir. 2014/24, Art. 22 (7), subpar. III.

(56) EU Dir. 2014/24, Art. 87.

(57) See the chapter of I. LOCATELLI in this book, par. 4.4.

(58) See the chapter of M.A. SIMOVART and M. BORODINA in this book.

capacity must be guided in the use of electronic means, e-procurement tools and platforms.(59)

### 3.1. The electronic platform in public procurement

Three models can be used to implement an e-procurement platform: (1) Private driven (where all electronic tools/e-platforms are developed and maintained, on a commercial basis, by the private sector, whereas the contracting authorities pay for their use); (2) Public driven (where only one, mandatory, central electronic tool/e-platform, developed and maintained by the public sector, exists – usually for free); and (3) a mixed model (e.g., private-fee based with public authorities having free electronic tools/e-platforms).(60)

One possible issue in the use of an e-procurement platform has to do with the nature of its activities, that is, whether it is economic or non-economic in nature. The case of mandatory use of a single platform can decrease business opportunities for other providers, and, in the case of a mixed model, the financial support of the State can be considered as State aid. In a recent case, the national Dutch platform known as ‘TenderNed’,(61) an e-procurement platform set up by a sub-department of the Netherlands Ministry of Economic Affairs, Agriculture and Innovation, was declared as a platform for “non-economic” activities since it was related to the exercise of public powers,(62) and the case is pending on appeal.(63)

The electronic access to information may be free of charge to contracting authorities.(64) Otherwise, this may cause complications such as difficulty in searching for information related to a particular procurement procedure. Some e-procurement platforms provide functionalities and information only

(59) *e-Procurement Uptake Final Report*, prepared for DG GROW, 23 April 2015, pp. 49 and ff. Therefore, low e-Notification thresholds can be considered as a good practice promoting the uptake of e-Procurement and SME inclusion.

(60) Z. RACZKIEWICZ, “It Is Possible for the State to Develop and Impose Technical Solutions for e-Procurement”, *EPPPLR*, 2018, p. 229.

(61) TenderNed, [www.tenderned.nl/](http://www.tenderned.nl/).

(62) EU Gen. Ct, VII, 28 September 2017, *Aanbestedingskalender BV and others v EU Commission*, case T-138/15, par. 60. *See*, to that effect, EUCJ, 10 January 2006, *Cassa di Risparmio di Firenze and Others*, case C-222/04, par. 31; EUCJ, 12 July 2012, *Compass-Datenbank*, case C-138/11, par. 36. On the fact that TenderNed is non-profit-making is not a sufficient factor for the purpose of determining whether or not an activity is of an economic nature, *see* EUCJ, 26 March 2009, *SELEX Sistemi Integrati v Commission*, aff. C-113/07 P, par. 116.

(63) EUCJ, *Aanbestedingskalender BV and others v EU Commission*, case C-687/17 P.

(64) EU Dir. 2014/24, Art. 53, according to which access to public procurement documents should be free of charge. *See also e-Procurement Uptake Final Report*, prepared for DG GROW, 23 April 2015. The report points out that access to information is free of charge in 23 Member States, and for the economic operators in 26 Member States.

to their users. There is also an on-going concern regarding the dissemination of information when using multiple platforms since different platforms are not usually interconnected. The access to information becomes a real issue to economic operators that are (sometimes) required to pay for information on contract notices published on local platforms. One possible solution in addressing these concerns is the use of a single national platform or “One-stop shop procurement portal” because it can limit the costs and it favours interoperability of the information (as in Netherlands and Poland).(65) Besides, the EU principle on transparency calls for ‘connecting’ procurement information and data generated and published on different platforms within one country.

### 3.2. The European Single Procurement Document – ESPD

The 2014 Directives on public contracts simplify the administrative burdens in the tenderers’ requirements (e.g., the need to produce attestations, certificates or other documents evidencing tenderer’s suitability)(66) through the use of the European Single Procurement Document (ESPD).(67) ESPD is a self-declaration, available in all EU languages, that is used as preliminary evidence, replacing the certificates issued by public authorities or third parties, and confirming that the tenderer fulfils the required (non-) exclusion grounds and selection criteria.(68) Moreover, ESPD can be used despite the different implementation of the rules on exclusion grounds in EU Member States. Although most of the grounds for exclusion are mandatory in all EU Member States, there are still some grounds which are discretionary on the part of EU Member States.(69)

(65) EU Comm., “One-stop shop procurement portal”, in which are highlighted the best practices of Poland’s Public Procurement Office portal and of the Dutch Public Procurement Expertise Centre (PIANOo) of the Ministry of Economic Affairs.

(66) See the Chapter of I. LOCATELLI in this book. 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 *Outside the EU Procurement Directives – inside the Treaty?* (D. DRAGOS and R. CARANTA eds), Copenhagen, Djøf Publ., 2012, pp. 382-383.

(67) EU Dir. 2014/24/EU, Art. 59.

(68) G.M. RACCA, “Electronic Qualitative Selection of Economic Operators: the challenge of the European Single Procurement Document (ESPD)”, in *Qualification, Selection and Exclusion in EU Procurement* (M. BURGI, M. TRYBUS and S. TREUMER eds), Copenhagen, Djøf Publ., 2016, pp. 303-325; S. ARROWSMITH, *The Law of Public and Utilities procurement. Regulation in the EU and UK*, *op. cit.*, pp. 1307 and ff.; A. SEMPLE, *A practical guide to public procurement*, Oxford, OUP, 2015. See also EU Comm. implementing Regul. (EU) 2016/7 of 5 January 2016 establishing the standard form for the European Single Procurement Document; EU Comm., “Legal framework for the European Single Procurement Document (ESPD) as set out in the Directive 2014/24/EU”, 11 February 2015.

(69) G.M. RACCA, “Electronic Qualitative Selection of Economic Operators: the Challenge of European Single Procurement Document (ESPD)”, *op. cit.*, pp. 314 and ff.

ESPD was already mandatory as of April 2016. It can be used either in paper form,(70) or as an electronic service (e-ESPD). The electronic version of ESPD was developed by the EU Commission and is already available to Member States in five different implementing modes, allowing different levels of customisation for Member States.(71) The five ways to use the ESPD are: (1) the ESPD services in EU countries through the National contact points, (2) the Free ESPD service provided by the European Commission,(72) (3) the ESPD Exchange data model, which enables integration of the eESPD service into national e-procurement solutions/pre-qualification services, the open source eESPD service,(73) (4) the Virtual Company Dossier (VCD), which allows the contracting authority to handle the eESPDs; and (5) the tenderers are to benefit from an automated filling-in of the eESPD. These activities have been funded by the ISA<sup>2</sup> programme (*Interoperability Solutions for Public Administrations, Businesses and citizens*).

As of 18 April 2018, ESPD was exclusively provided in electronic form. The ESPD Web service allows economic operators and contracting authorities to create, edit and export the electronic ESPD. As a simplification tool for economic operators, contracting authorities are obliged to accept the ESPD submitted by tenderers, though its use is not mandatory.(74)

Tenders in open procedures and requests for participation in restricted procedures, competitive procedures with negotiations, competitive dialogues or innovation partnerships must be accompanied by ESPD, which economic operators have completed in order to deliver the required information. The situation is more complex in cases of negotiated procedures without prior publication.(75) In some circumstances in which this procedure is allowed, ESPD may become an unnecessary administrative burden, or, otherwise inappropriate (e.g. where only one predetermined participant is possible, because of the urgency involved or the particular characteristics of the transaction for supplies quoted and purchased on a commodity market). In the other cases in which competitive procedures with negotiations are allowed (characterised by the possible participation of more than one participant and the absence of

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(70) See EU Comm. implementing Regul. (EU) No. 2016/7 establishing the standard form for the European Single Procurement Document, 5 January 2016.

(71) The ISA<sup>2</sup> programme supports the development of tools, services and frameworks in the area of e-Government.

(72) The use of ESPD can be met by using national ESPD services until April 2019. The role of the European Commission's ESPD service was to support the uptake of this tool during the initial phase.

(73) Managed by EU Comm., the open source version is compatible with the ESPD data model and some elements can be adjusted to take into account of national needs, and it is available at [joinup.ec.europa.eu/solution/european-single-procurement-document](http://joinup.ec.europa.eu/solution/european-single-procurement-document).

(74) EU Comm. implementing Regul. (EU) No. 2016/7 of 5 January 2016 establishing the standard form for the European Single Procurement Document, recital No. 3.

(75) Dir. 2014/24/EU, Art. 32; and Dir. 2014/25/EU, Art. 50.

urgency or particular characteristics linked to the transaction), ESPD's role becomes significant.

The e-ESPD service of the EU Commission aims to support only a transitional phase in Member States,(76) "since the full potential of the ESPD should be exploited with the integration of a 'national' ESPD with the procurement system and registers or databases of certificates/evidences of each Member State".(77)

For example, in Italy, the implementation of a national database of economic operators is provided to allow contracting authorities to verify exclusion grounds and selection criteria.(78) Nonetheless, the system is not completely implemented.(79) Such limitation results in the failure to simplify the process as the contracting authorities still need to evaluate a number of requirements.(80)

The simplification of the procedure from participation to awarding procedure is a goal in the French implementation of the 2014 Public Procurement directives,(81) though, not completely reached since the French Senate suggested a further simplification of the qualification stage and the ESPD standard form in order to reduce the cost of the award procedure.(82) In France, it is provided that tenderers cannot be required to provide documents and information that contracting authorities can already obtain from an official electronic system subject to "two conditions: (1) candidates must provide the relevant information regarding the said system; and (2) it must be in free access. The contracting authority can exempt a candidate from providing relevant documents that are already in the authority's possession provided that these documents are still valid and non-submission thereof is announced in the contract notice or the contract documents".(83) Moreover, it is highlighted

(76) According to the transitional nature of the service, the EU Commission will not undertake further developments of the e-ESPD after 18 April 2019. It is planned that the e-ESPD will be ceased after that date.

(77) EU Comm., "Report from the Commission to the European Parliament and the Council on the review of the practical application of the European Single Procurement Document (ESPD)", 17 May 2017, COM(2017)242 final, p. 3.

(78) Legisl. Decr., No. 50 of 2016, Italian Public Contracts Code, Art. 81. In Italy, the self-declaration (from 1 July 2014) has been provided by law and the certificate proving the absence of exclusion grounds and the respect of the selection criteria should be acquired only through the Public Contract National Database.

(79) Italian Anti-Corruption Authority, *2014 Annual Report*, 2 July 2015, pp. 80 and ff. Other limits are indicated by the Italian Anti-Corruption Authority which noted the lack of the information reported and an implementation of the system that, until now, it is not fully operative.

(80) Italian Anti-Corruption Authority, *2014 Annual Report, op. cit.*, p. 7.

(81) Ord. No. 2015-899 of 23 July 2015 on public procurements.

(82) Sen. fr., "Passer de la défiance à la confiance : pour une commande publique plus favorable aux PME", available at [www.senat.fr/rap/r15-082-1/r15-082-122.html](http://www.senat.fr/rap/r15-082-1/r15-082-122.html).

(83) F. LICHERE, "Qualification, Selection and Exclusion of Economic Operators under French Public Procurement Law", in *Qualification, Selection and Exclusion of Economic Operators*, Copenhagen, Djøf Publ., 2016, pp. 41 and ff. See also the French Decree of 26 September 2014 that implemented some provisions of Dir. 2014/24/EU.

that the use of e-certificates is allowed in order to reduce “administrative costs by 35% and the awarding process by 10 days”.(84)

In Germany, a contracting authority can “view the means of proofs submitted by the economic operator in the electronic database with the aid of the certification code”. However, the procedure adopted in the German legal system “does not replace the entire procedure of the verification of the selection criteria, but does replace the verification of certain means of proofs”.(85)

In UK, the Public Contract Regulations 2015 implemented the ESPD with the ‘copy-out’ method,(86) requiring contracting authorities to obtain the information needed for the qualification of the economic operators from national databases without providing any postponement (from 26 January 2016).(87) Contracting authorities “shall have recourse to e-Certis and shall require primarily such types of certificates or forms of documentary evidence as are covered by e-Certis” without postponing the use of such tools.(88) Moreover, specific websites for pre-qualification of tenderers have been created.(89) The ESPD was available in an online format only, nonetheless the ‘online only’ requirement was delayed until April 2017.(90) However these provisions in UK appear “of less importance (both for UK economic operators and for UK contracting authorities), since the UK does not operate many of the kinds of official certifications that are operated in some other Member States”.(91) Moreover, to ensure a simpler and more consistent approach to selection and to remove red tape and barriers which make difficult for businesses to access to public contracts, the standard Selection Questionnaire(92)

(84) By a French Central Purchasing Body (UGAP), *see* EU Comm., “End-to-end e-procurement to modernise public administration”, COM(2013) 453 final, p. 4.

(85) *See* M. BURGI and L.K. WITTSCHURKY, “The Qualification, Selection and Exclusion of Economic Operators (Tenderers and Candidates) form a German Perspective”, in *Qualification, Selection and Exclusion of Economic Operators* (M. BURGI, M. TRYBUS and S. TREUMER eds), Copenhagen, Djøf Publ., pp. 63 and ff.

(86) UK Public Contracts regulations 2015, Art. 59. *See* also UK Cabinet Office – consultation document “UK Transposition of new EU Procurement Directives. Public Contracts Regulations 2015”, 30 January 2015, p. 9, where it was noted that the use of the copy-out method “limit the extent to which we can deviate from the wording of the Directives when casting the national UK implementing regulations”.

(87) Dir. 24/2014/EU, Art. 59 (5), as implemented in UK Public Contracts regulations 2015, Art. 59(11).

(88) UK Public Contracts Regulation 2015, Art. 61, where ‘e-Certis’ is defined as “the online repository established by the Commission”.

(89) *See* L.R.A. BUTLER, “Exclusion, Qualification and Selection in the UK under the Public Contracts Regulation 2015”, in *Qualification, Selection and Exclusion of Economic Operators* (M. BURGI, M. TRYBUS and S. TREUMER eds), Copenhagen, Djøf, p. 189.

(90) UK Public Contracts regulations 2015, Art. 1 (4).

(91) *See* L.R.A. BUTLER, “Exclusion, Qualification and Selection in the UK under the Public Contracts Regulation 2015”, *op. cit.*

(92) Crown Commercial Services, “Procurement Policy Note: Standard Selection Questionnaire (SQ)”, 2016, available at [www.gov.uk/government/publications/procurement-policy-note-816-standard-selection-questionnaire-sq-template](http://www.gov.uk/government/publications/procurement-policy-note-816-standard-selection-questionnaire-sq-template).

has been developed to make the national questionnaire compliant with ESPD.(93)

Despite the national provisions, the EU integration allows a greater customisation and adaptation to national conditions, thus favouring the digitalisation of public administration and creating the basis for simplification of procedures (especially at cross-border level) via the implementation of the Once-Only Principle ('OOP').(94) The main idea of the 'once-only principle' is that economic operators should provide the information only once to the public entities and that the latter should share this information internally. This requires a database for the archiving of information from previous award procedures by each contracting authority.

Moreover, Member States, especially the ones with more sophisticated rules (and not based on the copy-out method) need an effective commitment to pursue a real simplification of the qualitative selection of tenderers (and of the entire awarding procedure). Leadership at the EU level seems essential. For example, in some Member States in which all the exclusion grounds(95) foreseen by the 2014 European Directives have been implemented (as in Italy), contracting authorities ask for integration of a self-declaration provided by ESPD. In Italy, contracting authorities ask for an autonomous self-declaration for the regularity of payment for social security of the employees (and the competent territorial authority), the mandatory respect (by the employees of the tenderer) of the national public entities ethic code,(96) and acceptance of the processing of personal data. The request for these additional self-declarations from each tenderer is an administrative burden to be overcome by tenderers.

At the European level, e-Certis is the information system that helps in identifying the different certificates requested in procurement procedures across the EU.(97) It helps interested parties to understand what information is being requested or provided, and to identify what are mutually acceptable as equivalents. It is accessible to any economic operator, and contracting authorities use e-Certis primarily to ask for certificates and other documents. The e-Certis system is a sort of repository for these documents, which is regularly updated by Member States.(98) In fact, Member States are obliged to ensure

(93) See UK Crown Commercial Services, "Public Contracts Regulations 2015: New requirements relating to Pre-Qualification Questionnaires to help businesses access Public Sector contracts", 27 February 2015.

(94) The ESPD allows the advancement of the 'once-only principle'. National solutions of the ESPD are already available in Denmark, Finland, Netherlands, and Slovenia.

(95) EU Dir. 2014/24, Art. 57. G.M. RACCA, "Electronic Qualitative Selection of Economic Operators: the challenge of the European Single Procurement Document (ESPD)", *op. cit.*, 2016.

(96) Italian D.P.R. No. 62 of 2013.

(97) EU Comm., "Information system e-Certis", 2016.

(98) EU Dir. 2014/24, Art. 61, Online repository of certificates (e-Certis).

that the information concerning certificates and other forms of documentary evidence introduced in e-Certis is constantly up-to-date. Contracting authorities use e-Certis and require primarily the types of certificates or forms of documentary evidence that are covered by e-Certis, since the use of e-Certis is already mandatory as of 18 October 2018. Moreover, the use e-Certis is now closely connected to the improvement of ESPD.(99)

Further developments of ESPD (and e-Certis) will also have to take into account developments in the systems interconnecting Member States' registries (such as *Business Registers Interconnection System (BRIS)*, *Interconnection of Insolvency Registries*, or the *European Criminal Records Information System – ECRIS*), which include documents and certificates relevant for awarding procedures which facilitate interoperability.(100)

### 3.3. E-Submission

E-submission became mandatory for all contracting authorities and all procurement procedures beginning in October 2018.(101) CPBs were, however, required to adopt full electronic means of communication including electronic bid submission as of April 2017.

E-Submission tools allow economic operators to participate in calls for tenders by preparing their tenders electronically. The submission of requests to participate and tenders must be done using electronic means of communication.(102) This phase is usually through the use of structured online forms and/or the submission of digital documents such as XML or PDF files.

Contracting authorities are not obliged to require electronic submission where the use of other means of communication is necessary to avoid a breach of security or for the protection of the particularly sensitive information requiring such a high level of protection, which cannot be properly ensured by using electronic tools and devices.(103)

(99) EU Dir. 2014/24, Art. 59, “European Single Procurement Document”, and Art. 60, “Means of proof”.

(100) EU Comm., “Report from the Commission to the European Parliament and the Council on the review of the practical application of the European Single Procurement Document (ESPD)”, *ibid.*, pp. 11-12. Standardisation is often seen as a contradiction to innovation, though its use can in fact serve as a catalyst for innovation, especially in defining test standards, methods and quality certificates.

(101) Two years after the expected transposition of the 2014 EU Dir. See EU Dir. 2014/24, Art. 22. See V. EIRÓ, “E-procurement: the Portuguese experience”, *PPLR*, 2016, NA5-NA16.

(102) R. BICKERSTAFF, “E-procurement under the new EU procurement Directives”, *op. cit.*, p. 141. P. FERK, “E-Procurement between EU Objectives and the Implementation Procedures in the Member States – Article 22(1)” in *Reformation or Deformation of the EU Public Procurement Rules in 2014* (G.S. OLYKKE and A. SANCHEZ-GRAELLS eds), Cheltenham, Edward Elgar, 2016; EU Dir. 2014/24, Art. 22(1) (a) (b) (c) and (d).

(103) EU Dir. 2014/24/EU, Art. 22 (1), subpar. IV. In these circumstances, communication must be carried out by post or another suitable carrier or by a combination of those means and electronic means, and, the contracting authority has to provide reasons for not using electronic submissions in the

To ensure the correct use of electronic means, tools and devices for electronic receipt of tenders, requests to participate, plans and projects in design contents must determine the exact time and date of tender receipt, requests to participate, and the submission of plans and projects. Moreover, data management must carefully safeguard the tenders' confidentiality and data integrity. No access to transmitted data must be made before the deadline provided for the tenders' submission and only authorised persons may set or change the dates for the opening of the data that is received throughout the procurement procedure. Only after a specified date may authorised personnel grant access to the data. Any data received or accessed is accessible only to those with granted permission.(104)

If the aforementioned security rules are breached, the contracting authority has to ensure that the infringements or attempts are clearly detectable. If the procurement documents require the use of technology or tools that are not publicly available, the contracting authority must provide an alternative means of access.(105) Free and unlimited access via electronic means to these tools and devices must be provided. This may occur in an e-Data modeling or equivalent.(106) These tools allow a digital representation with all the information of the works to be realized (also pointing out maintenance costs).(107) The availability of e-Data on the project makes it possible to evaluate it according its life-cycle cost (during the award phase), and simplify the monitoring activity in the execution phase and the maintenance of the work.

Most of the concerns encountered in the submission of tenders relate to the means used for authentication, such as electronic signatures and recognition of electronic identification. Such issues are not specific to e-Procurement but arise in any situation where authentication/signatures are required. The 2004 EU Directives on public procurement provided the possibility for Member States to regulate the level of electronic signature required and restrict the choice of contracting authorities to qualified signatures.(108) The level of secu-

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individual report on the contract award procedure. See S. ARROWSMITH, *The Law of Public and Utilities procurement. Regulation in the EU and UK*, *op. cit.*, pp. 639 and ff.; P. FERK, "Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?", *op. cit.*, pp. 327 and ff.

(104) EU Dir. 2014/24/EU, Annex IV.

(105) EU Dir. 2014/24/EU, Art. 22 (5).

(106) EU Dir. 2014/24/EU, Art. 22 (4). For example, Building Information Modeling may be requested in the procurement documents for the planning of a work. See the Chapter of G. DI GIUDA and G.M. RACCA in this book.

(107) A.L.C. CIRIBINI, M. BOLPAGNI and E. OLIVERI, "An Innovative Approach to e-public Tendering Based on Model Checking", in *Procedia Economics and Finance*, 2015, pp. 32-39, in which is provided an analysis of an electronic Model Checking in order to control the compliance between the client's requirements and bidders' offers within a digital environment.

(108) Dir. 2004/18/EC, Art. 42(5)(b) and Annex X. For the utilities sector, see Dir. 2004/17/EC, Art. 48(5)(b) and Annex XXIV. The device for the electronic receipt of tenders and requests to participate must guarantee that the electronic signatures used are in conformity with the national provisions adopted pursuant to Dir. 1999/93/EC.

rity required for the use of e-communications in the various stages of procurement procedure is left to the Member States. Also, in this case, a coordination among them seems essential in order to overcome the differences in national levels.(109)

The 2004 EU Commission's evaluation of the e-Procurement Action Plan revealed that the preference for qualified electronic signatures constituted an unnecessary entry barrier to e-Procurement – particularly for partner country suppliers in cases where there is an absence of operational tools for the recognition of different electronic signatures.(110) In 2008 a specific action plan was adopted with the aim of offering a comprehensive and pragmatic framework to achieve interoperable e-signatures and e-identification to simplify access to cross-border electronic public services.(111) The Digital Agenda for Europe had foreseen a review of e-signatures legislation and a stepping up of work in the area of e-identification.(112)

In 2010, 18 countries expressly required the use of e-signatures in e-Procurement procedures, “while 13 countries did not explicitly require them. In terms of the type of signature required, 13 out of the 27 Member States have introduced a legal requirement specifying the use of advanced e-Signatures”.(113) With the mandatory introduction of e-Procurement in the EU, e-signatures became a tool for identifying the persons in electronic transaction and all Member States adopted this requirement in their national provisions. The 1993 EC Directive(114) for a common legal framework was amended in 2014 with the aim of promoting “comprehensive cross-border and cross-sector framework for secure, trustworthy and easy-to-use electronic transactions”.(115)

The above-mentioned analysis on the legal framework highlighted how “e-Signature can be both a facilitator and a barrier”.(116) It makes public procurement simpler and reduces the length of the procedure and related costs for contracting authorities, though, with limitations as to when each

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(109) See the Chapter of I. LOCATELLI in this book, par. 4.5.

(110) EU Comm., “Action plan for the implementation of the legal framework for electronic public procurement”, 13 December 2004.

(111) EU Comm., “Action Plan on e-signatures and e-identification to facilitate the provision of cross-border public services in the Single Market”, COM(2008) 798 final, 28 November 2008.

(112) EU Comm., “A Digital Agenda for Europe”, COM(2010)245, 19 May 2010.

(113) EU Comm., “Evaluation of the 2004 Action Plan for Electronic Public Procurement Accompanying document to the Green Paper on expanding the use of e-Procurement in the EU”, aforesaid, p. 35. The regulatory choices of Member States in regard to e-Signatures may indicate their preferences in relation to security and trust but also need to be considered from a cross-border and interoperability perspective.

(114) Dir. 1999/93/EC of the European Parliament and of the Council of 13 December 1999 on a Community framework for electronic signatures.

(115) EU Regul., No. 910/2014 of 23 July 2014, on electronic identification and trust services for electronic transactions in the internal market and repealing Dir. 1999/93/EC, Recital No. 3.

(116) *e-Procurement Uptake Final Report*, Prepared for DG GROW, 23 April 2015, p. 134.

Member State requires different certificate or characteristics. In fact, digital certificates for authentication in the system and for document signing can also be burdensome, especially for SMEs and foreign companies, which may outweigh the benefits of an e-Signature. In addition, one of the main focuses of the e-Signature initiatives in the EU Commission is harmonization. An open source software was developed for e-Signature creation and validation that Member States can use at the national level under the ISA programme.(117) As the process of acquiring a digital certificate can be a costly, lengthy and in general bureaucratic procedure (e.g. in Germany and Portugal), the European legislation provides for mutual recognition of electronic signatures with a qualified certificate, based on a similar approach as the one defined in the Services Directive (Trusted List).

Electronic signatures were first recognised in the 1999 Directive on a Community framework for electronic signature (eSignature Directive).(118) The EU rules on electronic identification were completely revised to enhance “trust in electronic transactions in the internal market by providing a common foundation for secure electronic interaction among citizens, businesses and public authorities, thereby increasing the effectiveness of public and private online services, electronic business and electronic commerce” in the EU.(119) The eIDAS Regulation defines three levels of electronic signature: 'simple' electronic signature,(120) advanced electronic signature;(121) and qualified electronic signature.(122)

A digital signature placed on a document ensures that the document has been signed by the holder of the digital certificate accompanying the document (*i.e.* authenticity), and has not been altered from the time the digital signature was placed on the document (*i.e.* integrity), and that the signatory cannot deny having signed the document (*i.e.* non-repudiation).

Depending on national policies and rules, platforms use digital signatures to achieve authenticity and non-repudiation in a range of different ways, creating interoperability problems across borders.

Frequently, to submit a digitally signed tender on a platform, foreign companies need to acquire a digital signature certificate in the country of the platform. To remove barriers to SMEs, improve cross-border trading and reduce technical/operational complexity for contracting authorities, the Commission encourages Member States to re-evaluate, via risk analysis, if

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(117) Action 1.9 for the interoperability of public services in Europe.

(118) EC Dir. 1999/93.

(119) Regul. (EU) No. 910/2014 of 23 July 2014.

(120) Regul. (EU) No. 910/2014, Art. 3 (10).

(121) Regul. (EU) No. 910/2014, Art. 3 (11).

(122) Regul. (EU) No. 910/2014, Art. 3 (12).

digital signatures are strictly necessary at the tendering stage for authentication and non-repudiation, and to shift the signature to the stage of signing the contracts if the national legal framework or policies allow authorities to do so. For purely integrity-assurance purposes, platforms should use solutions not requiring personal digital signature certificates, such as hash-codes. Where digital signing of bids is deemed unavoidable to ensure authenticity and non-repudiation, contracting authorities are invited to enforce an e-submission model accepting all Qualified Electronic Signatures (QES) using certificates included in the EU Trusted Lists of Certification Service Providers.(123) These should be seen as a ‘passport’ signature across borders.(124)

‘E-signatures’ are supported by the eSignature building block of the European Commission’s Connecting Europe Facility (CEF), ‘CEF eSignature’ for short. Through the CEF eSignature building block, the European Commission supports the use of electronic signatures across European countries. This Web site is dedicated to the CEF eSignature building block, as well as the other building blocks of CEF.

The EU e-Procurement *Digital Service Infrastructure* allows full cross-border interoperability for electronic public procurement. Connecting Europe Facility – Digital Service Infrastructures has a budget of 1.14 billion euros, out of which 170 million euros are for broadband activities, while 970 million euros are dedicated to Digital Service Infrastructures (DSIs) delivering networked cross-border services for citizens, businesses and public administrations. Building block DSIs concern: eID & eSignature (services enabling cross-border recognition and validation of eIdentification and eSignature), eDelivery (services for the secured, traceable cross-border transmission of electronic documents), Automated Translation (services allowing pan-European digital services to operate in a multilingual environment), cybersecurity (services to enhance the EU-wide capability for preparedness, information sharing, coordination and response to cyber threats) and eInvoicing (services enabling secure electronic exchange of invoices).(125)

The EU Commission has adopted other measures to allow contracting authorities to identify the origin/certification of partner countries’ signatures

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(123) European Union Agency For Network And Information Security, “Security guidelines on the appropriate use of qualified electronic signatures – Guidance for users”, December 2016.

(124) Every e-submission platform in the EU supporting digitally signed tenders should accept this type of signature whatever the country of origin of the certificate. Verification of the electronic signature on the tenders is greatly simplified: once the verification tools available on the platform verifies the validity of the certificate (*i.e.* not expired nor revoked) and its nature as a qualified certificate listed in the EU trusted list, the tender should be accepted without any further consideration regarding security levels.

(125) EU Comm., “Connecting Europe Facility in Telecom”.

and to overcome EU barriers.(126) The Electronic Signature Service satisfies the security and legal requirements of typical European Commission eSignature applications including cross-border interoperability. The ESSI application platform supports the generation, verification, and extension of interoperable electronic signatures(127) and can validate existing electronic signatures on received documents, provided that these signatures comply with recognized standards.

### 3.4. E-Award

The EU Public Procurement Directives provide for tools and systems on the use of electronic means during the award procedure. The evaluation of tenders can be made through electronic means as in the case of an electronic auction process (e-Auction). The use of electronic means or e-auction does not mean that the award is automatized through an e-award. Sometimes paper documents are also required (e.g. concerning the selection requirement) or tender evaluations are made in a traditional way. Only the evaluation of the jury is included in a software or in an eDocument.(128)

An e-award can be used in any award procedure under the EU Directives, including the award criteria. Contracting authorities may select the award procedure and award criteria in the design procurement procedure strategy based on the result in the pre-awarding phase. The e-award seems to be one of the most challenging procedures, especially when applying the criteria for the most economically advantageous tender.(129) It requires a clear indication (in the procurement documents) of the evaluation criteria using measurable parameters and a proportional distribution of the achievable scores to a given value in the adopted measurement scale (e.g. meters, time, inch, weight). There are math formulas that can be used to evaluate different tenders. These formulas can be ‘independent’ or ‘interdependent’. ‘Independent’ formulas contain values independent from the others included in submitted tenders. ‘Interdependent’ formulas can include data of other submitted tenders (e.g. the best price submitted, the minimum value of a data parameter submitted).(130)

(126) The PEPPOL project developed solutions to provide on-line tools permitting automatic recognition of electronic signatures from other Member States to be used in a procurement context.

(127) It handles Advanced Electronic Signatures on XML, PDF, or any binary documents, according to Regul. (EU) No. 910/2014 of 23 July 2014.

(128) EU Dir. 2014/24, Art. 35 (5). J. PAVEL and E. SÍLÁKOVÁ-BEBLAVÁ, *Do e-Auctions Really Improve the Efficiency of Public Procurement? The Case of the Slovak Municipalities*.

(129) O.S. PANTILIMON VODA, *Innovative and sustainable procurement: framework, constraints and policies*, *op. cit.*, pp. 222 and ff.

(130) F. DINI, R. PACINI and T. VALLETTI, “Scoring rules”, in *Handbook of Procurement* (N. DIMITRI, G. PIGA, G. SPAGNOLO eds), Cambridge, CUP, 2006, pp. 304 and ff.

The choice of a math formula for the evaluation of the tenders is a key aspect of the procurement strategy and the design of procurement documents. It should not be treated as a separate element from the subject matter of the contract as it interacts in a crucial way with many other elements of the tender design (such as the starting price of the auction).(131)

The use of measurable parameters with ‘independent’ formulas allows the predetermination of scores in the tender evaluation, while the use of ‘interdependent’ formulas mitigates the risk that tenders are submitted (e.g. by subsidiary company) with the sole purpose of altering the regular development of the procurement procedure and its competitive equilibrium.

The inclusion of a formula in the procurement document can be made according to the characteristics of the relevant market (e.g. the number of economic operators, the level of competition among economic operators) and the need of the contracting authority.

Moreover, the optimal formula for all relevant criteria and their optimal weight (for the contracting authority) is generally very complex,(132) which makes it operationally complex to handle.(133) For example, a multi-criteria decision analysis is a decision-making method that requires knowledge of the criteria used in order to verify if the effect that is produced corresponds with the *desiderata* of the contracting authority.(134) There are numerous decision making methods and each one is created to respond to specific needs (often untied from procurement procedures). Their use, which is to bring true benefits in terms of efficiency and best value for money, must be done in a conscious way and with the necessary technical knowledge. Otherwise, the outcome of the tender procedure poses risks of being randomly produced.

In fact, the use of simple purchasing formulas is usually suggested as the optimal choice subject to certain conditions.(135) Sometimes a math formula is used solely to translate the scores given by the evaluation committee (jury) into a ranking. The problem is often not in the formula itself but in the subjectivity of the scores. In such cases, the assessment of the jury continues to have a discretionary impact and the mathematical formulae are used only to give a semblance of objectivity to a subjective evaluation.

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(131) F. DINI, N. DIMITRI, R. PACINI and T. VALLETTI, “Formule di Aggiudicazione nelle Gare per gli Acquisti Pubblici”, *Quaderni Consip*, 2007.

(132) P.S. STILGER, “Formulas for Choosing the Most Economically Advantageous Tender – a Comparative Study”, 2011, available at [dspace.library.uu.nl/bitstream/handle/1874/235924/StilgerPS-MA2011Part%20I.pdf?sequence=1](https://dspace.library.uu.nl/bitstream/handle/1874/235924/StilgerPS-MA2011Part%20I.pdf?sequence=1).

(133) J. ASKER and E. CANTILLON, “Optimal Procurement when both Price and Quality Matter”, CEPR Discussion Paper No. 5276, 2005.

(134) P. MIMOVIC and A. KRSTIC, “Application of Multi-Criteria Analysis in the Public Procurement Process Optimization”, *Economic Themes*, 2016, pp. 103-128.

(135) F. DINI, N. DIMITRI, R. PACINI and T. VALLETTI, “Formule di Aggiudicazione nelle Gare per gli Acquisti Pubblici”, *op. cit.*

E-award seems particularly apt for the activities of CPBs, allowing the electronic evaluation of tenders/request for participation and the award of contracts (e.g. with a correct use of eAuctions) or the conclusion of framework agreements. In this case, the professionalism of CPBs and their resources can facilitate the end-to-end e-procurement process through the use of electronic processes and tools provided by the EU Directives. The CPBs can conclude framework agreements electronically with the use of an eCatalogue for the submission of tenders. In that case, the possible call-off can be realized through the eCatalogue tool. An electronic signature can identify the tenderer in the phase for the conclusion of the framework agreement, and, for the signature of the contract in case of reopening the competition. E-Communication tools allow easy notifications of information to tenderers and candidates during the award procedure.

### 3.5. Electronic Auctions

The electronic auction (electronic reverse auction or eAuction) is not an autonomous awarding procedure but it is a procurement tool that emerged as a result of progress in electronic technology.<sup>(136)</sup> The e-auction is allowed in open or restricted procedures or competitive procedures with negotiation, as well as in the reopening of competition among the parties to a framework agreement<sup>(137)</sup> and on the opening for competition under a dynamic purchasing system.<sup>(138)</sup>

The e-auction is an electronic process<sup>(139)</sup> that allows the submission of new prices (revised downwards) and/or new elements of tenders after an initial full evaluation of tenders has been undertaken. It involves a process that is usually forbidden in an open or restricted procedure, *i.e.*, negotiation with the tenderers during the evaluation stage;<sup>(140)</sup> though, allowed in an e-auction process. In fact, e-auctions often lead to a modification of the initial conditions set out in the contract notice and procurement documents. If the contracting authority has concerns about the clarity of the procurement documents, it can consider re-launching the procedure with revised specifications. The use of electronic means avoids risks of error in the tender data submitted (e.g.

<sup>(136)</sup> G.M. RACCA, “The Electronic Award and Execution of Public Procurement”, *Ius Publicum Network Rev.*, 2012, p. 38.

<sup>(137)</sup> As provided in EU Dir. 2014/24, Art. 33(4) pts (b) or (c).

<sup>(138)</sup> EU Dir. 2014/24, Art. 34.

<sup>(139)</sup> EU Dir. 2014/24, Art. 35, par. I(2).

<sup>(140)</sup> The electronic evaluation of the tender, whatever the award criteria, is provided through the instrument defined as e-Auctions to be applied in open or restricted procedures or in different kinds of framework agreements and dynamic purchasing systems, as already provided by the 2004 Directive on public procurement. L. FOLLIOT-LALLIOT, “The French Approach to Regulating Frameworks under the New EC Directives”, in *Reform of the UNCITRAL model law on procurement* (S. ARROWSMITH ed.), Danvers, Thomas Reuters/West, 2009, pp. 198 and ff. on French rules on framework agreements.

providing a measurable range – meter, time, weight – without the possibility of inserting data outside the provided gap) and allows traceability of information, including the monitoring of activities in the execution phase of the contract.

An interesting issue concerns the ability (for the tenderers/candidates) to contest or point out anomalies in the rebates made during the eAuction online through the same eNotification tools used by the contracting authority. When the lowest price is the award criterion, contracting authorities will not refer to any other qualitative element in the award of the contract. The lowest price is the sole quantitative benchmark that can differentiate the offers submitted by the tenderers.(141) When rebates affect that outcome, however, it may be necessary to ensure open communications throughout the electronic procedure.

When the contracting authority fails to precisely define the object of the contract performance, the only criterion for the award of the contract is the most economically advantageous tender. Specific concerns may arise in the electronic evaluation of the scored criteria. In such cases, different elements linked to the subject-matter of the contract must be evaluated.(142) As is well-known, the above-listed criteria are not exhaustive. The technical specifications of the required quality of services, goods or works (*i.e.*, the quality of the bid)(143) must be distinguished from the criteria for the qualitative selection of participants (quality of bidder) for further electronic evaluation.

The contracting authority must specify in the contract notice or in the contract documents the relative weight given to each criterion in determining the most economically advantageous tender. The contracting authority may express the appropriate relative weight for evaluation using a range from minimum and maximum scores(144) or by providing a range with an appropriate maximum range. When it is not possible to demonstrate the weighted scores, a contracting authority can provide the criteria in descending order of importance in the contract documents. The implementation of such criteria in

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(141) Dir. 2004/18/EC, Art. 53(1)(b).

(142) E.g. 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. Dir. 2004/18/EC, Art. 53(1), and Dir. 2004/17/EC, Art. 55(1). Concerning the scoring rules provided from the contracting authority, see F. DINI, R. PACINI and T. VALLETTI, “Scoring rules”, *op. cit.*, pp. 294 and ff.

(143) ECJ, *Emm G. Lianakis AE v. Alexandroupolis*, case C-532/06, 2008, *E.C.R.*, I-251; on this ECJ case law see “Application and Implications of the ECJ’s Decision in Lianakis on the Separation of Selection and Award Criteria in EC Procurement Law”, *PPLR* (sp. iss.), 2009, p. 103. For a general EU perspective, see S. TREUMER, “The Distinction Between Selection and Award Criteria in EC Public Procurement Law: A Rule Without Exception?”, *PPLR*, 2009, p. 103.

(144) Dir. 2004/18/EC, Art. 53(2), and Dir. 2004/17/EC, Art. 55(2). For example, an authority could perhaps assign in the documents a weighting of 80% to price and 20% to quality; or state in the documents that the weighting will be 80-85% for price and 15-20% for quality, and later decide on the more precise weighting.

an electronic system of evaluation only requires the definition of objectively measurable qualitative elements that can accommodate an automatic score in case of relevant changes or improvements to proposals.

One of the main challenges in implementing e-auction systems lies in making them interoperable with electronic tendering platforms.<sup>(145)</sup> In this way, the entire award procedure and related procedure can be traceable. These characteristics make e-auctions particularly well-suited as components for dynamic purchasing systems.

### 3.6. Electronic catalogues

Electronic catalogues (e-catalogues) provide a “format for the presentation and organisation of information in a manner that is common to all of the participating bidders and that lends itself to electronic treatment”.<sup>(146)</sup> They constitute tools (not procedure) to facilitate public procurement, specifically (but not exclusively) as a means for participating in procurement through framework agreements or within a dynamic purchasing system.<sup>(147)</sup>

E-catalogues have to be fulfilled (by economic operators) in accordance with the technical specifications and format established by the contracting authority.<sup>(148)</sup> Moreover, the requirements for electronic communication tools have to be respected.<sup>(149)</sup> The procurement documents should indicate the necessary information on the format, the electronic equipment used, and technical connection arrangements and specifications for the e-catalogue. E-catalogues may be used for the whole tender or just for a part thereof. They may be updated at the request of the contracting authority.<sup>(150)</sup> Contracting authorities can define specific time periods, during which suppliers may update their e-catalogues. This ensures equal treatment and transparency for all suppliers.<sup>(151)</sup> Tenders must remain confidential until the deadline for submission.

At their simplest, e-catalogues are merely electronic versions of traditional paper-based catalogues that show the details of an economic operator’s goods

<sup>(145)</sup> EU Comm., “Use e-auction for small, standardised purchases”.

<sup>(146)</sup> EU Dir. 2014/24, recital No. 68. *See also* recital No. 55 on interoperability.

<sup>(147)</sup> I. GALLEGO CÓRCOLES, “Electronic catalogues under Directive 2014/24: simplifying procedures and increasing efficiency”, *PPLR*, 2018, pp. 109-119.

<sup>(148)</sup> E-catalogues must be custom-made for each award. *See* EU Dir. 2014/24, Art. 36(2). On interoperability, *see also* EU Dir. 2014/24, Art. 22(7).

<sup>(149)</sup> EU Dir. 2014/24, Art. 22. Where the presentation of tenders in the form of e-catalogues is accepted or required, contracting authorities have to state this information in the contract notice or in the invitation to confirm interest.

<sup>(150)</sup> R. BICKERSTAFF, “E-procurement under the new EU procurement Directives”, *op. cit.*, p. 141.

<sup>(151)</sup> European Dynamics, “Functional Requirements”, *Electronic Catalogues in Electronic Public Procurement*, 2007, p. 39.

or services.(152) An example is where a contracting authority sets up a single-provider framework agreement, which is then operated using an e-catalogue set up by the provider, describing the products and prices in a pre-agreed and structured manner. In this case, the e-Catalogue was established during the award procedure and its contents based on the submitted tender. Unlike other e-catalogues, this example does not require the awardee and the contracting authority to perform other activities for the establishment of an e-catalogue.

In a multi-supplier framework agreement, the 2014 EU Directives provide two alternative methods for reopening the competition: either by inviting resubmitted catalogues, or by collecting information from previously-submitted catalogues, provided suppliers are given the chance to refuse that collection.(153) The same possibilities are provided for using updated catalogues in the context of dynamic purchasing systems.(154)

Where a framework agreement has been concluded with more than one economic operator, the submission of tenders can be made in the form of electronic catalogues. Moreover, contracting authorities may provide that the reopening of competition for specific contracts takes place based on updated catalogues.(155) In such a case, contracting authorities shall invite tenderers to resubmit their electronic catalogues (according to the requirements of the contract in question). The economic operators can notify tenderers that already submitted in the electronic catalogues (in another call-off) or adapt the original tender for the single call-off.

Regardless of the type of award procedure used by a contracting authority, the use of e-catalogues per se does not seem to create significant scope for distortions of competition, other than the eventual imposition of the use of exceedingly demanding or non-compatible IT solutions. However, that risk can be mitigated per the requirement that e-catalogues shall comply with the requirements for electronic communication tools which requires that tools and devices as well as their technical characteristics, “shall be non-discriminatory, generally available and interoperable with the ICT products in general use and shall not restrict economic operators’ access to the procurement procedure”.(156)

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(152) From a technical perspective, they could take virtually any form, ranging from general text documents (e.g. in PDF or MS Word format).

(153) EU Dir. 2014/24, Art. 36(4).

(154) EU Dir. 2014/24, Art. 36(6).

(155) On framework agreements see G.L. ALBANO and C. NICHOLAS, *The Law and Economics of Framework Agreements*, Cambridge, CUP, 2016; R. CANAVAN, “Public Procurement and frameworks”, in *Research Handbook on EU Public Procurement Law* (C.H. BOVIS ed.), Cheltenham, Edward Elgar, 2016, pp. 119 and ff.; M. BOWSER and L.E. JOHN, “The use (and abuse?) of framework agreements in the United Kingdom”, in *International Public Procurement. A guide to best practice* (R. HERNANDEZ GARCIA ed.), London, Globe Law & Business, 2009, p. 349.

(156) EU Dir. 2014/24, Art. 22, par. I.

### 3.7. The Dynamic Purchasing System: future perspective on their use

The use of e-procurement tools favours the monitoring of procurement procedures, thus ensuring greater transparency and improved monitoring power. From the public administration standpoint, IT represents both a way to promote accountability and integrity of public officials and an opportunity to realise intra- and cross-border administrative co-operation through the exchange of relevant information. The characteristics of the ‘Dynamic Purchasing System’ – DPS seem to adapt to these needs. In fact, DPS constitutes (in the future) a tool capable of balancing efficiency and integrity in public contracts favouring a progressive use of electronic means in public procurement.

The 2004 directives on public procurement introduced a mechanism for repetitive standard purchases, the DPS.<sup>(157)</sup> This system authorized public entities to establish, using electronic means, a list of suppliers that were interested in supplying certain standard supplies or services. However, the uncertainty on the use of electronic means (especially at the cross-border level) and the complexity of the process discouraged its use at the European level.<sup>(158)</sup> The Crown Commercial Service (UK), in response to the European Commission Green paper on the modernisation of EU public procurement policy for the 2014 procurement directives, concluded that “flawed and unnecessarily onerous procedural rules” deterred many practitioners from deploying DPS.<sup>(159)</sup>

Some of these procedural restrictions were addressed in the 2014 EU Directive in order to encourage its use.<sup>(160)</sup> DPS<sup>(161)</sup> operates rather like a live, online, internet-based framework agreement,<sup>(162)</sup> which economic operators can join at any time. The openness of DPS makes it possible to overcome the problems related to possible collusion among economic operators who are part of the framework agreement and leaves open the possibility for new companies

(157) EC Dir. 2004/18, Public Sector Directive, Art. 33; EC Dir. 2004/17, Utilities Directive, Art. 15. See S. ARROWSMITH, “Dynamic Purchasing Systems Under the New EC Procurement Directives – A Not So Dynamic Concept?”, *PPLR*, 2006, p. 16.

(158) S. ARROWSMITH, “The past and future evolution of EC procurement law: from framework to common code?”, *Publ. Contr. L.J.*, 2006, pp. 337 and ff. See also PWC/Ecorys, “Public procurement in Europe Cost and effectiveness”, p. 53.

(159) UK response to the EC Green paper on the modernisation of EU public procurement policy, COM (2011) 15 final.

(160) EU Dir. 2014/24, Art. 34, par. I. C. RISVIG HAMER, “Regular purchases and aggregated procurement: the changes in the new Public Procurement Directive regarding framework agreements, dynamic purchasing systems and central purchasing bodies”, *PPLR*, 2014, pp. 201-210.

(161) This purchasing technique allows the contracting authority to have a particularly broad range of tenders and hence to ensure optimum use of public funds through broad competition in respect of commonly used or off-the-shelf goods, works or services which are generally available on the market.

(162) G.L. ALBANO and C. NICHOLAS, *The Law and Economics of Framework Agreements*, Cambridge, CUP, 2016.

to enter the DPS while it is established. The requirement of IT tools favours transparency of the conclusion of framework agreement and of the call-off procedure.

The period of its validity is indicated in the contract notice of a DPS. The possibility (for the economic operators) to be admitted and to ask to participate throughout the entire period of validity of a DPS is the reason why the EU directives do not provide for a maximum duration. The contract notice for a DPS also is to indicate the electronic equipment for the DPS, including the technical connection arrangements.

A DPS is managed in two different steps. According to the restricted procedure,<sup>(163)</sup> the first step is the evaluation of the selection criteria (required in the contract notice) for admission to the DPS, which includes the requirement for Member States to “make available and up-to-date” in eCertis a complete list of databases containing DGUE relevant information regarding economic operators.<sup>(164)</sup>

The second step concerns the award of a specific procurement under the DPS. In this phase, a contracting authority considers all economic operators that are already admitted to a DPS (however a contracting authority may ask tenderers and candidates at any time during the procedure to submit all or part of the supporting documents) as qualified, and, thereafter, may evaluate the submitted tenders according to the criteria set out in the contract notice.<sup>(165)</sup> Alternatively, the contracting authority can specify the selection and award criteria that are already set out in the contract notice for the DPS. In this case, the specification of the award criteria allows the tenders to be adapted to the needs of the contracting authority. The specification of the selection criteria reduces the benefits derived from having already qualified economic operators in the first step.

A concern relates to the fact that the rules do not provide any obligation to notify the providers of a decision to award a contract under a DPS. However, also considering that publication is no longer required in a simplified notice where the contract is above the EU threshold, there is a risk that it can be declared ineffective on the ground of breach of contract. A voluntary standstill period can be observed to avoid ineffectiveness, and as part of good procurement practice, it seems better that contracting authorities should provide feedbacks to tenderers.<sup>(166)</sup>

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(163) EU Dir. 2014/24, Art. 34, par. II.

(164) EU Dir. 2014/24, Art. 59(6).

(165) Moreover, contracting authorities may require that tenders were presented in the form of an electronic catalogue in accordance with the relevant technical specifications provided.

(166) A. EYO, “Evidence on use of dynamic purchasing systems in the United Kingdom”, *PPLR*, 2017, pp. 6, 23-248.

DPS is best suited in markets with large numbers of suppliers combined with a large volume of transactions, such as the purchase of different goods under the same category (e.g. drugs). For example, in Italy, there were several DPSs that operated for the procurement of drugs. A DPS was used in that case to simplify the award procedure that commonly would require separate and numerous lots by developing (as the first step) the qualitative selection of tenderers. In fact, the use of this tool has increased in Italy, particularly by the National CPB (Consip S.p.A.), which used DPS's for several categories of goods (furniture, computer, electromedical equipment) and services (insurance services, cleaning services, maintenance of electrical installations).

A DPS may be divided into categories of goods, works or services based on the characteristics of the procurement to be undertaken.<sup>(167)</sup> The total anticipated cost is also a key factor to ensure that the effort involved in developing a DPS results in the expected benefits. Alternatively, when the cost in implementing a DPS is smaller, its benefits stay similarly small on balance.

The similarity of DPS and framework agreements does not exclude the possibility of using a DPS for the conclusion of a framework agreement. This can happen especially in situations where there is uncertainty in the quantity to be purchased. In this case, the efficiency of electronic means and the flexibility of the framework agreements are considered in the establishment of the DPS. The UK dynamic purchasing system that is managed by the UK Crown Commercial Service (CCS) is an example of this type of the DPS. Here, buyers can access framework agreements that meet common purchasing requirements across government.

Another UK experience on the use of DPS is provided by the Health and Social Care Network (HSCN),<sup>(168)</sup> which enables a competitive marketplace on social care through the use of a dynamic purchasing system tailored to HSCN requirements, initially with nine suppliers including SMEs. The DPS is provided by the UK Crown Commercial Service (CCS) that launched the HSCN Access Services dynamic purchasing system. DPS can also be used to procure connectivity, closely related services, and support with transition and implementation.

The use of electronic means must be balanced with the need to favour participation, especially of SMEs. In many cases, economic operators are

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<sup>(167)</sup> EU Dir. 2014/24, Art. 34, par. I. Such characteristics may include reference to the maximum allowable size of the subsequent specific contracts or to a specific geographic area in which subsequent specific contracts will be performed.

<sup>(168)</sup> The Health and Social Care Network (HSCN) is a new data network for health and care organisations which replaced N3. It provides the underlying network arrangements to help integrate and transform health and social care services by enabling them to access and share information more reliably, flexibly and efficiently.

unable to understand or to use the authority's e-tendering system. Nonetheless, it is still necessary to enhance DPS practice and secure the efficiencies that the mechanism offers to contracting authorities and suppliers. In this respect, it is suggested that contracting authorities must prepare for DPS implementation by adopting initiatives that address organisational, personnel-related and technological challenges to DPS deployment, while also encouraging training activity for SMEs.

There are other factors that need to be considered in establishing a DPS such as the characteristics of the relevant market (e.g. the competition among supplier, regular new entrants/suppliers exiting the market, the adaptability to local SMEs, the volume of transactions). Moreover, "no charges may be billed prior to or during the period of validity of the dynamic purchasing system to the economic operators interested in or party to the dynamic purchasing system".<sup>(169)</sup> This provision becomes relevant in Member States that have established a fee or other form of economic contributions for the participation in an award procedure.<sup>(170)</sup>

To enhance the use of DPS, a prototype that demonstrates this electronic process was created at the European level.<sup>(171)</sup> This tool provides several scenarios, from the establishment of DPS, to the creation of a specific contract, the submission of indicative tenderers, and the submission of tenders and their evaluations.

#### ***4. The Management of Public Contracts through Electronic Means and the e-Invoice***

E-procurement plays a significant role in managing public contracts. The use of integrated and interoperable electronic means allows the management of the entire public procurement cycle. The contracting authority (or a National Authority and other third parties) can also monitor the execution of public contracts.<sup>(172)</sup>

Two main goals can be pursued. First, it is possible to easily compare the performances of the economic operators to whom contracts have been awarded

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(169) EU Dir. 2014/24, Art. 34, par. IX.

(170) This is for example the case of Italy where sometimes the cost of the award procedure is charged to the successful tenderer. See Italian Anticorruption Authority, dossier No. 2788 of 2016. Moreover, the Italian Law (Art. 1, par. 65 and 67, law of 23 December 2005, No. 266) establish the payment of a contribution (for the contracting authority and the economic operator) for any single award procedure. See the Italian Anticorruption Authority, Resol. No. 1300 of 2017.

(171) IDABC Public e-Procurement, "Static demonstrator for dynamic purchasing systems".

(172) G. M. RACCA, *The role of third parties in the execution of public contracts*, in L. FOLLIOT-LALLIOT – S. TORRICELLI (eds), *Contrôle et contentieux des contrats publics – Oversight and remedies in public contracts*, Brussels, Bruylant, 2017, 415 e s.

for similar services. From a second point of view, it is, at least in principle, possible to verify in a simple manner the deviations from what the awardee promised during the awarding procedure. Some examples are provided by the ‘modifications of the contract during its execution’, the ‘subcontracting’ and possible situations of conflict of interest, the monitoring of the delay in the payment of the contracting authorities.

In this way, accessible online data can simplify the process, provided that the ‘quality’ data of all contracting authorities are compiled in an archive of knowledge regarding public administration, which has reusable information. To pursue these goals at the European level, the standardization of data in the required documents is essential. In the execution of public contracts, an example is provided by e-invoice. Until a few years ago many e-invoice formats were used across the EU. These varied formats caused unnecessary complexity and high costs for economic operators and contracting authorities.

To simplify the EU context, the EU Commission introduced a European standard for e-invoicing.<sup>(173)</sup> The e-invoicing directive provides information to be shared between EU countries. The EU rules do not include obligations related to electronic invoicing (e-invoicing), apart from a requirement to include information on the acceptance of e-invoices in the contract notice, when appropriate. However, Directive 2014/55/EU on electronic invoicing in public procurement provides that Member States must ensure that contracting authorities and entities receive and process electronic invoices that comply with the EU standards on e-invoicing.<sup>(174)</sup>

The EU Commission realized several initiatives to promote the correct use of e-invoicing in public procurement. With the aim “to help pave the way for a broad-scale adoption of e-invoicing at the national and EU-level”, the EU Commission established the European Multi-Stakeholder Forum on Electronic Invoicing (EMSFEI) that brings together stakeholders from national e-invoicing forums and from the user-side of the market. The EMSFEI allows the exchange of experiences and best practices across borders through EU Member States. It also may issue recommendations to the Commission.

An interesting tool that is realized at the EU level is the *e-Invoicing readiness checker* that allows users to check their level of readiness to exchange e-Invoices in compliance with Directive 2014/55/EU. This is a ‘public entity repository’ that allows users to find and consult Public Administrations.

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(173) EU Directive 2014/55/EU, on electronic invoicing in public procurement.

(174) R. WILLIAMS, *Commission proposes draft Directive on e-invoicing*, in *PPLR*, 2013, 6, NA154-NA157. For an example on the potential benefit, see *Electronic Invoicing – The next steps towards digital government*, 2014; A. GROZNIK and A. MANFREDA, *e-invoicing and e-government – impact on business processes*.

The main goal is the correct use of information and data to favour transparency and efficiency of contracting authority through an effective management of contract execution and monitoring.(175) The availability of clear, complete and comparable information (quality of information) ensures an efficient and effective management throughout the public procurement cycle, to the full benefit of integrity, understood as “the use of funds, resources, assets and authority, according to the intended official purposes and in line with public interest”.(176) This directly affects the efficiency of the public administration activity.

The slowness of the process of standardization at the European level due to divergent interests of the individual Member States is a critical issue that needs to be overcome with a deeper political commitment.

## 5. Conclusions

Electronic means can significantly favour better procurement outcomes, and high-quality public services, while stimulating greater competition (including cross-border procurement) across the EU Internal Market.(177) A greater availability of information can be an incentive for economic operators to boost the access to the public procurement sector.(178)

Enabling a unified approach to public procurement policy and ensuring the production of uniform and structured data are certainly two of the main concerns in Europe.(179) Greater access to information must be accompanied by a calibrated strategy for the implementation of electronic tools (e.g. creation and management of electronic platforms) that ensures data interoperability and quality.(180) The Directives provisions on “electronic and aggregated procurement”(181) and the policies on professionalization of public procure-

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(175) Transparency is commonly considered the basis for good governance. See A. CERRILLO-I-MARTINEZ, *Public transparency as a tool to prevent corruption in public administration*, in A. Cerrillo-I-Martinez and J. Ponce (eds by), *Preventing Corruption and Promoting good Government and Public Integrity*, Brussels, Bruylant, 2017, 2-3; J.M. ACKERMAN and I.E. SANDOVAL-BALLESTEROS, *The global explosion of freedom of information acts*, in *American Law Review*, 2006, 58.

(176) G.M. RACCA and C.R. YUKINS (eds), *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally*, coll. Droit Administratif / Administrative Law, Brussels, Bruylant, 2014. M. PIGNATTI, “The use of e-procurement and contractual terms and conditions for the risk assessment and risk management in the public procurement cycle”, in *Risk management: perspectives and open issues. A multi-disciplinary approach* (V. CANTINO, P. DE VINCENTIS and G.M. RACCA eds), Londron, Mc Graw Hill, 2016, pp. 927 and ff.

(177) OECD, “Public Procurement for Innovation. Good Practices and Strategies”, *op. cit.*, p. 67.

(178) EU Comm., “Green Paper on expanding the use of e-Procurement in the EU”, COM(2010) 571 final, 18 October 2010.

(179) Multi-Stakeholder Expert Group on e-procurement (EXEP), “Certification of E-tendering Platforms”, 12 September 2017.

(180) EU Comm., “Harmonised standards: Enhancing transparency and legal certainty for a fully functioning Single Market”, 22 November 2018, COM(2018) 764 final.

(181) EU Dir. 2014/24, Art. 33-39.

ment practitioners to prevent anticompetitive conduct and collusive practices must be taken into account.(182)

Currently, Member States “are not using to their full extent the possibilities of public procurement as a strategic tool” to support EU policies.(183) To support a change of the public procurement culture in EU Member States, the EU Commission has recently identified six priority areas,(184) where clear and concrete action can transform public procurement into a powerful instrument in each Member State’s economic policy toolbox. ‘Increasing transparency, integrity and better data’ and ‘boosting the digital transformation of procurement’ are two of these priorities aimed at making digital transformation effective throughout the public procurement process, rethinking the way public procurement and public administrations are organised.

The availability of data and the sharing with other interested parties make it possible “to assess better the performance of procurement policies, optimise the interaction between public procurement systems and shape future strategic decisions”.(185) This should enable the dialogue with and through civil society and third parties to encourage monitoring activity.(186)

E-Procurement requires re-thinking the organisation of public procurement and the activities of contracting authorities to improve overall efficiency and overcome barriers to the full development of electronic means.(187) Many EU studies emphasize several approaches adopted by EU Member States, highlighting possible barriers for the development of the Internal Market and cross-border procurement, such as language barriers, the national orientation of

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(182) These activities are considered as essential “to attract, develop and retain skills, focus on performance and strategic outcomes and make the most out of the available tools and techniques”. EU Comm., “Recommendation on the professionalisation of public procurement Building an architecture for the professionalisation of public procurement”, 3 October 2017, C(2017) 6654 final.

(183) EU Comm., “Making Public Procurement work in and for Europe”, 3 October 2017, COM(2017) 572 final, p. 3.

(184) The Commission’s six policy priorities for public procurement are: Ensuring wider uptake of innovative, green, and social procurement; Professionalising public buyers; Increasing access to procurement markets; Improving transparency, integrity and data; Boosting the digital transformation of procurement; Cooperating to procure together.

(185) EU Comm., “Making Public Procurement work in and for Europe”, 3 October 2017, COM(2017) 572 final, p. 11. This publication also pointed out the relevance of training on innovation and e-procurement tools.

(186) G.M. RACCA, “The role of third parties in the execution of public contracts”, in *Contrôle et contentieux des contrats publics – Oversight and remedies in public contracts* (L. FOLLIOU-LALLIOT and S. TORRICELLI eds), Brussels, Bruylant, 2017, pp. 415 and ff. On the concept of ‘collaborative transparency’, see A. FUNG, M. GRAHAM and D. WEIL, *Full disclosure. The perils and promise of transparency*, Cambridge, CUP, 2007. See also M. ROGALSKA, “Leverage technologies – preparing for a data driven and automated culture in public procurement”, at the “Digital Transformation of Public Procurement”, Lisbon, 18 October 2018.

(187) G.M. RACCA, “The Electronic Award and Execution of Public Procurement”, *Ius Publicum Network Rev.*, available at [www.ius-publicum.com/pagina.php?lang=it&pag=articoli&n=2,2012](http://www.ius-publicum.com/pagina.php?lang=it&pag=articoli&n=2,2012), pp. 1-63.

e-procurement platforms and the lack of interoperability between them.(188) Proper training can maximize the benefit from e-procurement. Moreover, recommendations, guidelines and best practices tools for the transition to e-procurement have been drafted by the Multi-Stakeholder Expert Group on e-procurement (EXEP) set up by the EU Commission in October 2014.(189) E-Competence Centers have been created to provide tools and information to help public buyers get value for money and better policy outcomes for citizens who are also using electronic means.

The EU Commission proposed new standard e-forms to improve the collection of data enhancing transnational interoperability.(190) The Single Digital Gateway(191) and the European services e-card(192) are some of the tools that have been implemented in complementary areas. The data and information acquired are the most important elements, and this requires taking into account data security issues and access concerns.

A single portal related to tenders allows monitoring on the selection of contractor and on the execution by third parties (universities, companies, associations, citizens, social witnesses and civic engagement actions), with a control that promotes respect of ethical principles by public officials and facilitates obedience to constitutional obligations on the fulfillment of the assigned public functions.(193)

Moreover, if not properly created/used, e-procurement will not address real challenges of the EU public procurement in the long term. Language translation and interoperability (also through EU standards) are perhaps two of the possible means that help in addressing real challenges of EU public procurement, more particularly, those challenges that result in higher direct

(188) A. BUYSE, N. DEWYNGAERT, N. LOOZEN, M. LOPEZ POTES, G. SIMONS and A. ZIEMYTE, *e-Procurement Uptake – Final Report*, report prepared for DG GROWTH by PwC EU Services, 2015.

(189) See the key policy documents implemented by the Multi-Stakeholder Expert Group on e-procurement (EXEP). On 19 September 2017: “Contract Registers”, “Electronic Catalogues” and “Certification of e-Tendering Platforms”. On 24 October 2016: “Solutions and Interoperability”, “Governance and capacity building” and “Regulatory Aspects and Interpretation”.

(190) Multi-Stakeholder Expert Group on e-procurement (EXEP), “Solutions & interoperability”, 24 October 2016. See also European Parliament resolution “on the public procurement strategy package”, aforesaid, p. 27.

(191) EU Comm., “Proposal for a Regulation of the European Parliament and of the Council on establishing a single digital gateway to provide information, procedures, assistance and problem solving services and amending Regul. (EU) No. 1024/2012”, COM/2017/0256.

(192) EU Comm., “Regulation proposal on the legal and operational framework of the European services e-card”, COM 2016 (823) and COM 2016 (824), adopted by the Commission in January 2017 and currently being discussed by the European Parliament and Council, introducing a harmonised EU-level procedure for cross-border expansion of construction and business services in the internal market which includes the approval of economic operators entered into the official lists referred to in Art. 64 of Dir. 2014/24/EU.

(193) G.M. RACCA, “Disciplina e onore nell’attuazione dei codici di comportamento”, in *Al servizio della nazione. Etica e statuto dei funzionari pubblici* (R. CAVALLO PERIN and F. MERLONI eds), Milan, Franco Angeli, 2009, pp. 250-265. *e-Procurement Uptake Final Report*, Prepared for DG GROW, 23 April 2015.

cross-border trade<sup>(194)</sup> and diminish the efficiency of public contracting activities.

Other relevant issues can be identified. The ‘quality’ with which information is given assumes autonomous relevance in the notion of transparency. The 2017 Public Procurement Strategy of the EU Commission pointed out that public administrations are in dire need of larger quantities of data exhibiting a higher quality to enable a better assessment of procurement practices. Furthermore, traditional procurement often suffers from erroneous or missing data due to media breaks (e.g., entering data from paper-based submissions into a computer system).<sup>(195)</sup>

Through the establishment of an end-to-end electronic procurement process, media breaks can be prevented, since all procurement data are always available in digital format. This will help guarantee the availability of higher quantities of data, since all created data artifacts will be logged automatically and will no longer be lost by not being transferred from paper into a digital system.<sup>(196)</sup>

A political commitment of Member States seems essential in order to support the transition to an innovative way of buying for public administration, making effective the correct use of electronic means in the public procurement cycle.<sup>(197)</sup>

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(194) P. FERK, “Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?”, *EPPPLR*, 2016, p. 327.

(195) EU Parliament, “Systems and e-procurement – Improving Access and Transparency of Public Procurement”, Briefing requested by the IMCO committee, April 2018. P. P. STOLL, *Procurement – Grundlagen, Standards Und Situation Am Markt*, Wiesbaden, Germany: Springer Science + Business Media, 2007.

(196) Avoiding media breaks is also an essential first step into increasing the quality of procurement data, as it avoids conversion errors such as typos and overlooking parts of the given information.

(197) Multi-Stakeholder Expert Group on e-procurement (EXEP), “Governance and capacity building. Effective Transition to e-Procurement: Useful Tips”, 24 October 2016.

**CHAPTER 18**  
**A Qualitative Step from e-Communication**  
**to e-Procurement:**  
**the Estonian e-Procurement Model**

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**1. Introduction**

In recent years, the topic of electronic public procurement has been in the centre of attention, mostly in the light of the duty to transfer to fully electronic procurement procedures that were introduced under the 2014 public procurement directives.(1) While the inherent positive notions accompanying such transfer are evident,(2) the potential benefits and purposes that are usually credited to an electronic mode of procurement had been subject to some critical approach as well.(3) Nonetheless, resorting to electronic communication, publication and record keeping cannot be avoided in this day and age in most areas of life, including in the field of public procurement.

However, as several Member States are still reported to show insufficient progress in this area,(4) estimation of the possibilities as well as the challenges associated with different systems of e-procurement is an equally logical step. The Estonian model of e-procurement might hopefully serve as one possible example.

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(1) Dir. 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts, Art. 34; Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC, Art. 22, 90; Dir. 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 Dir. 2004/17/EC, Art 40, 73, 106. A prior version of this piece was published through the Ius Publicum Network Review ([www.ius-publicum.com](http://www.ius-publicum.com)), issue 2, 2017.

(2) See, e.g. R. BICKERSTAFF, “E-procurement under the new EU procurement Directives”, *PPLR*, 2014, 3, pp. 134-147; V. EIRO, “E-Procurement: the Portuguese experience”, *PPLR*, 2016, NA1 – NA16.

(3) P. FERK, “Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?”, *EPPLR*, 2016, pp. 327-339, *passim*.

(4) *Ibid.*, p. 329.

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Estonia has been moving towards a fully electronic public procurement environment since the year 2001, with 92% of procurement procedures conducted electronically in 2016.<sup>(5)</sup> The following is a short overview of the Estonian electronic procurement system, with attention to some legal issues that have been associated with e-procurement.

We submit that while single steps in electronic communication in public procurement do not constitute a jump to a new level, the fully electronic procurement as required pursuant to the 2014 directives can be associated with the added quality expected to support the drive for more cross-border competition, transparency and non-discrimination. Further, resorting to *e-procurement* as a system itself is a way of supporting innovation that can be viewed as a “cornerstone”<sup>(6)</sup> of EU public procurement policy.

## 2. Background and Recent Developments

### 2.1. Time-line of developing e-procurement in Estonia

A web-based electronic public procurement register of Estonia commenced in April 2001, at that time merely facilitating electronic submission and publication of contract notices. In 2009, the function of sharing electronic procurement documents was added to the register. For instance, the new function provided the public access to contract documents – contracting authorities (entities) could now publish contract documents on the register’s web site instead of sending them to tenderers via e-mail.

In 2011, an innovative e-Procurement environment was launched. The environment consists of two parts: the e-Procurement Register (hereinafter ‘the ePR’ or ‘the Register’<sup>(7)</sup>) and an information portal of public procurement.<sup>(8)</sup> The database for processing public procurement data, the Register, currently performs the following functions: publication of contract notices and forwarding them to the Publications Office of the EU; provision of information on results of complaints procedures; electronic processing of public procurement procedures, gathering of statistical data and publishing any other

<sup>(5)</sup> *Rahandusministeerium*, 2016, *aasta riigihangete kokkuvõte*, *Avaldatud* 17 March 2017, available at [www.rahandusministeerium.ee/et/system/files\\_force/document\\_files/riigihankemaastiku\\_esmane\\_kokkuvote\\_2016\\_1.pdf?download=1](http://www.rahandusministeerium.ee/et/system/files_force/document_files/riigihankemaastiku_esmane_kokkuvote_2016_1.pdf?download=1), lk 1 (last visit 5 December 2017).

<sup>(6)</sup> L. BUTLER, “Innovation in Public Procurement: towards the ‘Innovation Union’”, in *Modernising Public Procurement: the New Directive* (F. LICHÈRE, R. CARANTA and S. TREUMER eds), Copenhagen, Djøf Publ., 2014, p. 337.

<sup>(7)</sup> Available at [riigihanked.riik.ee/rhr-web/#/](http://riigihanked.riik.ee/rhr-web/#/) (last visit 1 March 2019).

<sup>(8)</sup> Available at [www.rahandusministeerium.ee/et/riigihangete-poliitika](http://www.rahandusministeerium.ee/et/riigihangete-poliitika) (last visit 1 March 2019).

procurement related information.(9) The Register thus provides the workspace for conducting an actual fully electronic procurement, *i.e.* submission of tenders and performance of all the steps within a procurement procedure electronically. The information portal on the other hand gathers all the relevant public procurement-related information.

In 2013, the law made e-procurement (including e-submission) partially mandatory in Estonia, requiring all contracting authorities (entities) to accept electronic submission of offers or electronic requests to participate in the procurement in at least 50% of all the procurement procedures planned for acquiring supplies, works and/or services in a fiscal year.(10) This requirement applied to any and all public (utilities) procurement procedures that were subject to the duty of publication, including procurement procedures for contracts below the national thresholds that were conducted as “simplified procedures.”(11) The Ministry of Finance (the body liable for overseeing the field of public procurement in Estonia) performed regular and systematic supervision over contracting authorities following the 50% e-procurement duty.(12)

This partially mandatory e-procurement practice seems to have been rather successful as by 2016, electronic procurement procedures made up slightly over 90% of all published public (utilities) procurement procedures,(13) in comparison to 80% of e-procurements in 2015.(14)

With a view to the above figures, transfer to 100% electronic procurement is not expected to pose considerable difficulties. In fact, many contracting authorities in Estonia have already been in the habit of practicing 100% electronic procurement for years. The entire electronic procurement practice has been credited with leading to a reduction of costs related to conducting procurements for both contracting authorities (entities) and tenderers; a

(9) Riigihangete seadus (RHS) RT I, 1 July 2017, 1, in force since 1 September 2017, hereinafter RHS, § 181 lg 1, §§ 183-184.

(10) Riigihangete seadus (RHS 2007) RT I 2007, 15, 76 ... RT I, 25.10.2016, 20, § 55 lg 7.

(11) At the time, the duty to publish a contract notice in the ePR generally began from the estimated value of €10,000 for a supply or service contract and €30,000 for a works contract. – RHS 2007 § 15 lg 3, § 18<sup>2</sup>. The current Act on Public Procurement (RHS § 125 lg 1) requires contracting authorities to publish a contract notice if the value of the procurement equals or exceeds that of a threshold for a ‘simplified procedure’ (§ 14 lg 1): €30,000 in the case of supplies or services, 60 000 euros for works and certain concessions.

(12) *Rahandusministeerium, 2015, aasta riigihangete plaanilise järelevalve kokkuvõte, Struktuursed probleemid riigihanke-eeskirjade kohaldamisel*, May 2016, available at [www.rahandusministeerium.ee/system/files\\_force/document\\_files/2015\\_plaaniline\\_jv\\_31.05.2016.pdf?download=1](http://www.rahandusministeerium.ee/system/files_force/document_files/2015_plaaniline_jv_31.05.2016.pdf?download=1), lk 29 (last visit 1 March 2019).

(13) *Rahandusministeerium, 2016, aasta riigihangete kokkuvõte*, lk 1.

(14) *Rahandusministeerium, 2015, a riigihankemaastiku kokkuvõte, Poliitika kujundamine, nõustamis- ja koolitustegevus, riiklik ja haldusjärelevalve, riigihangete register ja statistiline ülevaade*, September 2016, available at [www.rahandusministeerium.ee/et/system/files\\_force/document\\_files/riigihankemaastikukokkuvote2015\\_4.pdf?download=1](http://www.rahandusministeerium.ee/et/system/files_force/document_files/riigihankemaastikukokkuvote2015_4.pdf?download=1), lk 32-33 (last visit 3 January 2019).

reduction of administrative and labour costs as well as an increase in the quality of conducting procurement procedures that in turn can lessen the number of complaints and court cases.(15)

The new Act on Public Procurement, in force since 1 September 2017, raised the proportion of mandatory electronic procurement: at least 70% of all procurement procedures published in the Register by any one contracting authority (entity) must now be conducted electronically, including electronic publication of contract documents, submission of requests, tenders or explanations.(16) Any electronic means employed in a procurement procedure are subject to strict technical criteria in order to allow unrestricted and nondiscriminatory access of tenderers as well as interoperability with generally used IT products.(17)

From 18 October 2018, public procurement is to be 100% electronic as a rule.(18) Exceptions apply for technical (e.g. due to specific file formats or sizes), physical (e.g. samples must be enclosed to tenders) or security reasons or in the case of negotiations or dialogue that form a part of a particular award procedure – these do not have to take place in the electronic format.(19) Any exchange of information related to a public procurement must take place electronically,(20) except for information concerning unsubstantial elements of a procurement procedure that can be communicated orally, provided that the content of such information is sufficiently documented. Some parts of a procurement procedure – namely contract documents, tenders or requests – are always regarded as substantial elements of the procedure that can never be subject to an oral exchange of information.(21)

With the view to the above transition period and the actual high percentage of e-procurements, the transfer to a 100% electronic procurement is not expected to pose considerable difficulties.

## 2.2. Characteristics of the Estonian e-Procurement Register

The Estonian Electronic Procurement Register is a centralised national platform designated for the mandatory use in procurement procedures

(15) *Rahandusministeerium*, 2015, *aasta riigihangete plaanilise järelevalve kokkuvõte*, lk 27; *Selektuskiri riigihangete seaduse eelnõu juurde*, available at [www.riigikogu.ee/tegevus/eelnoud/eelnou/d8709d7d-cf5c-45c6-8576-1b7e86c80a8a](http://www.riigikogu.ee/tegevus/eelnoud/eelnou/d8709d7d-cf5c-45c6-8576-1b7e86c80a8a), lk 7.

(16) RHS § 220 lg 1. As a rule, this concerns procurements from the estimated value of €30,000 for a supply or service contract and €60,000 for a works contract. RHS § 14 lg 1, pp. 2-3, § 125, lg 1.

(17) Following RHS § 45, lg 8, criteria as to electronic means of communications in public procurement are introduced by the ministerial decree: *Riigihalduse ministri määrus, Nõuded elektroonilisei teabevahetuse seadmele, Vastu võetud 9 August 2017, No. 61, RT I, 15 August 2017, 3.*

(18) RHS § 45, lg 1, § 238, lg 3.

(19) RHS § 45, lg 2, pp. 1-5.

(20) RHS § 45, lg 1, § 238, lg 3.

(21) RHS § 45, lg 5.

conducted by all contracting authorities and entities. The central platform solution is one of the globally established good practice examples, even though it is not very common in the EU.(22) (On the other hand, it is probably the only reasonable solution for a tiny nation such as Estonia). While the current ePR was introduced in 2011, a new version of the ePR is currently in the final stages of development. Parts of the new platform opened for use in September 2017, and the entire new platform is to be launched in two parts by 2018 and 2019.(23) The main improvements of the new ePR include the faster and more automatic options for both tenderers and contracting authorities (entities), better search options, more flexibility in the sequence and the conduct of steps of a procurement procedure as well as certain innovative tools featuring the changes brought about by the 2014 directives.(24) The new version is expected to provide more efficiency and lower the costs of conducting or participating in a public (utilities) procurement. The users of the current Register can now separate the different parts of the same procurement and have the ability to change the sequence or time-line of such parts.(25)

The ePR is financed and developed by the State and is free for use by any contracting authority or entity when conducting public or utilities procurement procedures. As such, it can be classified as a mandatory one-platform solution supported by a government office.

As an exception to the mandatory use of the ePR, contracting authorities (entities) can either develop their own individual platforms for conducting electronic auctions, dynamic purchasing systems or electronic catalogues or use such platforms as offered on the market(26) – a possibility that has found some use in practice.(27)

In the ePR, contracting authorities (entities) can prepare public procurement procedures, draft notices and contract documents (information) to be published in the ePR, choose the members (officials) for the contracting authority's team in that particular procurement, keep lists of tenderers, correspond with tenderers, including responding to any requests for information by tenderers or sending any other procurement related notices to the tenderers. Tenders are accepted, opened and evaluated within the e-environment, requests for

(22) P. FERK, "Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?", *op. cit.*, pp. 335.

(23) [www.rahandusministeerium.ee/et/eesmargidtegevused/riigihangete-poliitika/riigihangete-register/registrite-arendamine](http://www.rahandusministeerium.ee/et/eesmargidtegevused/riigihangete-poliitika/riigihangete-register/registrite-arendamine).

(24) *Rahandusministeerium*, 2016, *aaasta riigihangete kokkuvõte*, lk 9.

(25) *Täieliku e-hangete võimekuse loomine, Eelanalüüs*, AS Datel 2016, available at [www.rahandusministeerium.ee/sites/default/files/Riigihangete\\_poliitika/register/rhr\\_eelanaluus\\_1.0.pdf](http://www.rahandusministeerium.ee/sites/default/files/Riigihangete_poliitika/register/rhr_eelanaluus_1.0.pdf), lk 9-10 (last visit 1 March 2019).

(26) *Seletuskiri riigihangete seaduse eelnõu juurde*, lk 58.

(27) E.g. [www.mercell.com/en/67127880/leading-e-tender-system-and-tender-offer-provider.aspx](http://www.mercell.com/en/67127880/leading-e-tender-system-and-tender-offer-provider.aspx).

additional explanations can be sent to tenderers (e.g. in the case of mistakes discovered in a tender if these can legally be made good), requests for information can be sent to other registries to cross-check the information submitted by tenderers – e.g. to check on tax debts of tenderers, to verify the rights of an agent to represent a tenderer, to look at an annual report of a company etc.

Any potential tenderer, on the other hand, has access to all published contract notices, contract documents and the contracting authorities' replies to any requests for information or clarification. A tenderer also has an option to order specific information packages from the electronic environment. When interested in a particular procurement, a tenderer must register with the contracting authority in order to be able to submit questions or to submit an electronically-signed tender. Via the ePR, tenderers will receive notifications of decisions made in the course of the procurement procedure.(28)

Thus, the ePR fulfils all requirements established under the Directive 2014/24(29) for the scope of a full e-procurement, namely that it must cover all activities in the pre-award phase of public procurement: publication of notices, access to tender documents, submission of tenders and the award of contracts.(30) Also, it corresponds to the requirement that potential tenderers must have *unrestricted and free direct access* to documents – a criterion that has been interpreted to mean accessibility through the internet as opposed to sending the documents via e-mail.(31)

At the end of a procedure, the ePR offers the option to automatically submit the public contract to the successful tenderer for signing and to transfer the contract data into the report following the signing.(32) In this stage of procurement, it is however not mandatory under the Directive 2014/24(33) or the law to use electronic means of communication to carry out electronic processing of tenders or use electronic evaluation or automatic processing. Similarly, electronic communication is not mandatory during the phase of negotiations or dialogue where applicable, or in the post-award (contract performance) phase.(34)

(28) *Seletuskiri riigihangete seaduse eelnõu juurde*, lk 37-38.

(29) "Preambula", p. 52, Art 22.

(30) See also S. ARROWSMITH, *The Law of Public and Utilities Procurement: Regulation in the EU and UK*, London, Sweet and Maxwell, 2014, p. 639; R. BICKERSTAFF, "E-procurement under the new EU procurement Directives", *op. cit.*, p. 138; V. EIRO, "E-Procurement: the Portugese experience", *op. cit.*, NAs.

(31) R. BICKERSTAFF, "E-procurement under the new EU procurement Directives", *op. cit.*, p. 144.

(32) *E-hanke läbiviimine riigihangete registris, Abimaterjal hankijale, Koostatud 31 August 2017*, available at [rshkoolitused.publicon.ee/userfiles/E-hange%20RHRis\\_abimaterjal%20hankijale\\_II%20poolaasta.pdf](http://rshkoolitused.publicon.ee/userfiles/E-hange%20RHRis_abimaterjal%20hankijale_II%20poolaasta.pdf), lk 4, 7 (last visit 3 January 2019).

(33) Dir. 2014/24 whereas No. 52 and Art. 22.

(34) Also S. ARROWSMITH, *The Law of Public and Utilities Procurement: Regulation in the EU and UK*, *op. cit.*, pp. 639-640.

### 2.3. Comprehensive e-procurement environment

While resorting to e-procurement is expected to simplify the conduct of award procedures, reduce the impact on the environment through cutting costs on paper and transportation, and achieve a better price-quality ratio (different numbers have been published on the EU level, referring to a 5-20% reduction of costs<sup>(35)</sup>), it still is vital that e-procurement should mean more than a simple change from paper-based to electronic communication systems. Only as such can an e-procurement system enhance the efficiency of public procurement in general and benefit the functioning of public procurement markets as a whole.<sup>(36)</sup>

Perhaps it is the comprehensive nature of the whole electronic procurement environment that has been the crucial factor in the hitherto development of the Estonian electronic procurement system. Besides the electronic Procurement Register for conducting (fully) electronic award procedures, the same web page contains the electronic register of complaints<sup>(37)</sup> as well as access to user help and the information portal.

The electronic register of complaints provides references to all complaints submitted to the Complaints Board (the review body in public procurement matters<sup>(38)</sup>) and the decisions made in these matters. Submission of complaints is however not conducted within the ePR. In the course of preparing the latest update to the electronic procurement environment, the possibility of integrating the Complaints Board cases more closely with the ePR has been discussed but has not been decided as of present.<sup>(39)</sup>

The presence of user help facilitates direct and immediate assistance in case of facing any problems with the ePR. Equally vital are trainings offered by the Ministry of Finance, regularly offered to both contracting authorities and entities.<sup>(40)</sup> As a part of user preparation, the ePR provides a training environment<sup>(41)</sup> that offers video instructions for conducting different actions in the register and allows trying out various scenarios (different award procedures) in the role of either a tenderer or a contracting authority. Both parties can thus exercise their skills or acquire an experience similar to that of the other side,

(35) EU Comm., “A Strategy For E-Procurement”, COM/2012/0179 final, eur-lex.europa.eu/legal-content/ET/ALL/?uri=CELEX:52012DC0179, p. 2.

(36) EU Comm., “Green Paper on expanding the use of e-Procurement in the EU”, COM (2010) 571 final, pp. 2-3, available at eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52010DC0571 (last visit 3 January 2019).

(37) *Vaidlustuste register, riigihanked.riik.ee/rhr-web/#/search-links* (last visit 3 January 2019).

(38) RHS, § 117, lg 4; *Riigihangete vaidlustuskomisjoni põhimäärus, Rahandusministri määrus*, RTL 2007, 34, 599 ... RT I, 15 September 2015, 12.

(39) *Täieliku e-hangete võimekuse loomine*, 2016, lk 96.

(40) *rhskoolitused.publicon.ee/kasutajatoe-koolitus/*.

(41) *E-riigihangete koolituskeskond on leitav aadressil: rhrkoolitus.fin.ee/rhr-web/#/*.

possibly helping to avoid some of the problems that might happen in the course of actual award procedures.

The information portal focuses on all things related to public procurement and contains information on legal regulation on both the EU and national levels, references to court cases and summaries of case law of both the CJEU and Estonian Supreme Court, research conducted on the request or by the Ministry of Finance as well as recommendations by the Ministry, information on trainings and seminars, FAQs, news etc.(42)

We submit that collecting a comprehensive body of procurement-related information in one information portal can be a part of boosting user-friendliness and thus supporting the popularity of e-procurement solutions.

### ***3. Legal Challenges and Possibilities Attributed to Electronic Procurement***

#### **3.1. Does the e-procurement system support the primary goals of the EU public procurement policy?**

The importance of transferring to electronic public procurement has been emphasised by the European Commission since 2010.(43) Electronic procurement is expected to assist in advancing the primary goals of the EU public procurement law – competition, transparency and non-discrimination. Presumably, any e-procurement system should be launched with these primary values in mind.

Technical functions of the Estonian ePR are created with a view to increasing transparency and accountability: in order to participate in an e-procurement procedure, all users – including tenderers and well as contracting authorities' agents – must authenticate themselves. Authentication of Estonian citizens or e-residents(44) takes place via the ID card while foreign users are identified with the help of a specifically created username and password.

All steps made in the ePR are logged and, as such, can later be verified. For instance, members of the Complaints Board can verify if and when a challenged decision is delivered to tenderers. When a complaint about a procurement procedure is on-going in the Complaints Board, members of the Board are vested with special rights with regard to that particular procurement

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(42) [www.rahandusministeerium.ee/et/riigihangete-poliitika](http://www.rahandusministeerium.ee/et/riigihangete-poliitika).

(43) *Euroopa Digitaalne tegevuskava, Euroopa Komisjoni teatis*, 26 August 2010, pp. 33-34, available at [eur-lex.europa.eu/legal-content/ET/TXT/PDF/?uri=CELEX:52010DC0245R\(01\)&from=ET](http://eur-lex.europa.eu/legal-content/ET/TXT/PDF/?uri=CELEX:52010DC0245R(01)&from=ET) (last visit 3 January 2019).

(44) Information about the Estonian e-residency program can be found here: [e-resident.gov.ee/](http://e-resident.gov.ee/) (last visit 5 December 2017).

procedure. These rights differ from those of the public or the tenderers: for instance, unlike the tenderers, the Complaints Board members have access to the content and price of the tenders.<sup>(45)</sup> On the other hand, these rights are specifically tied to the on-going case and cease with regard to the concerned procedure once the Complaints Board makes its decision.<sup>(46)</sup>

In the course of the proceeding, the Complaints Board can routinely access any document or information that exists within the challenged procurement procedure in the ePR and is relevant to the on-going review. As a result, the actual burden of submitting proof in public procurement cases is significantly reduced, both in terms of reducing the emerging paper trail and making the review proceedings more efficient. Evidence must be submitted only if it is not available in the Register and not accessible via other public records.<sup>(47)</sup> For instance, a tenderer naturally still has to submit proof of damages as well as evidence that the value of the tender is not abnormally low.

Tenders are submitted through safe HTTPS channels and saved in the ePR. In addition, the persons authorised by the Ministry of Finance guarantee the safekeeping of tenders. Authorized persons representing the contracting authority have access to the tenders only after the deadline for tender submission. Security related to submitting tenders is naturally critical for creating trust and thus increasing competition.<sup>(48)</sup>

A challenge referred to by Ferk concerns the need to establish national e-procurement systems in such a way that instead of straying away from the primary objectives of the EU public procurement policy and serving the interests of local purchasing, the systems would in fact increase cross-border procurement. Without such increase, the e-procurement reform cannot be considered to fulfil its objectives.<sup>(49)</sup> For instance, an overly restrictive approach to e-procurement can be a technical solution that is not easily available to the nationals of the other States.

The Directive 2014/24, Article 22 (1) second sentence addresses this concern as follows: “The tools and devices to be used for communicating by electronic means, as well as their technical characteristics, shall be non-discriminatory, generally available and interoperable with the ICT products in general use and shall not restrict economic operators’ access to the procurement procedure”. An example of a discriminatory requirement, fulfillment of which is not

(45) RHS § 181, lg 6, Riigihangete registri põhimäärus RT I, 1 September 2017, 13, § 21, lg 18.

(46) *Täieliku e-hangete võimekuse loomine*, 2016, lk 20.

(47) RHS § 190, lg 7.

(48) More information with regard to the security protocol of the updated ePR can be found here: *Täieliku e-hangete võimekuse loomine*, 2016, lk 12-15, 16.

(49) P. FERK, “Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?”, *op. cit.*, pp. 327-328, 332 -333.

generally possible, would be the request to sign a tender electronically with a digital signature. While digital signing via the national ID-card is a routine practice in Estonia in private as well as in business affairs,(50) it would not be possible without an Estonian ID-card. Therefore, this requirement is never applied to foreign companies.

While the share of public contracts awarded to tenderers from other Member States in public and utilities procurements in Estonia in 2015 is not a particularly high at 2.6% of the total number of awarded contracts or ca 7.3% in terms of total contract values,(51) the share of cross-border procurement cannot be criticized too much either. It must be taken into account that this share is based on all the conducted procurement procedures of which only 17.3% are for contracts above the EU threshold(52) – those are the contracts that presumably have any cross-border interest and that the EU public procurement rules of cross-border competition are aimed at.(53)

In 2015, tenderers from other Member States participated significantly more in e-procurement procedures (63%) than in other, non-electronic procedures (37%).(54) In general, the average number of tenderers in e-procurement procedures is higher (3.7) than that in award procedures that are not conducted electronically (2.6).(55) That can be attributed to the fact that through a central ePR platform, information simply reaches potential tenderers better.(56) The above seems to be in harmony with the global experience where transparency and added participation of tenderers have been noted,(57) and the overall high indicators describing procurement ‘performance’ in Estonia in 2016.(58) In view of the above, the Estonian model of e-procurement cannot be heading in the wrong direction.

(50) Information and assistance on application of digital signing is available here: [www.id.ee/?lang=en&id=](http://www.id.ee/?lang=en&id=) (last visit 3 January 2019).

(51) *Rahandusministeerium*, 2015, *a riigihankemaastiku kokkuvõte*, lk 49. In the EU, the share of direct cross-border activities was indicated as 1.3% in 2012, in terms of total contract value the share was 3.5% in 2012. Z. KUTLINA-DIMITROV and C. LAKATOS, “Determinants of direct cross-border public procurement in EU Member States”, *Trade*, Iss. 2, July 2014, available at [trade.ec.europa.eu/doclib/docs/2014/july/tradoc\\_152700.pdf](http://trade.ec.europa.eu/doclib/docs/2014/july/tradoc_152700.pdf), p. 5 (last visit 3 January 2019).

(52) *Rahandusministeerium*, 2015, *a riigihankemaastiku kokkuvõte*, lk 48.

(53) Furthermore, the number includes a fair amount of so-called ‘simplified’ award procedures for public contract with a relatively minor financial value, see *Rahandusministeerium*, 2016, *aasta riigihangete kokkuvõte*, lk 1.

(54) *Rahandusministeerium*, 2015, *a riigihankemaastiku kokkuvõte*, lk 47.

(55) *Rahandusministeerium*, 2016, *aasta riigihangete kokkuvõte*, lk 1.

(56) *Ibid.*

(57) P. FERK, “Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?”, *op. cit.*, p. 331.

(58) EU Comm., “Single Market Scoreboard, Performance per Policy Area”, Public Procurement (Reporting Period January 2016-December 2016), available at [ec.europa.eu/internal\\_market/scoreboard/\\_docs/2017/public-procurement/2017-scoreboard-public-procurement\\_en.pdf](http://ec.europa.eu/internal_market/scoreboard/_docs/2017/public-procurement/2017-scoreboard-public-procurement_en.pdf), pp. 3-4.

### 3.2. Does the e-procurement system support secondary EU public procurement policy goals?

Besides the primary objectives, electronic procurement can as well benefit the secondary policy goals, e.g. green and socially responsible procurement, as well as boost innovation.<sup>(59)</sup> With regard to secondary objectives, an interesting feature of the new e-procurement environment to be launched in Estonia in 2018 is a function offering default green public procurement criteria as grounds for exclusion, selection and award.<sup>(60)</sup> Developed to facilitate the inclusion of green requirements in public contract documents, the default green public procurement criteria were drafted by the Ministry of Environment based on criteria offered by the European Commission for certain groups of products or services.<sup>(61)</sup> It should be mentioned that currently, green public procurement can generally be described as rather underexploited in Estonia. The default inclusion of suitable green procurement criteria can perhaps bring about some increase of such practice.

Another policy goal emphasised in the 2014 directives is the purpose of better engagement of SMEs in public procurement. The question of suitability of electronic procurement systems for an efficient SME participation has been subject to some conflicting arguments.<sup>(62)</sup> We submit that *per se*, the presence of e-procurement cannot be said to have negatively influenced SME tenderers in Estonia as in 2016, 87% of all public contracts were awarded to SMEs. (As referred to above, 92% of all procurement was e-procurement.) However, an e-procurement might in fact create obstacles for SME participation in certain instances, e.g. when the e-platforms are not user-friendly enough, i.e., no assistance or training is available or when multiple platforms are creating confusion as to the potentially available award procedures.

Identified as a 'cornerstone' of EU policy, the importance of pursuing innovation in general for EU public procurement law should not be underestimated although it has not yet gained the deserved recognition in public procurement systems.<sup>(63)</sup> When developing and launching an improved electronic public procurement system (an updated platform), the process itself is regarded as a form of direct procurement of innovation: all the end users (contracting

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(59) EU Comm., "Single Market Scoreboard, Performance per Policy Area", *op. cit.*, p. 329.

(60) *Täieliku e-hangete võimekuse loomine*, 2916, lk 50-51.

(61) [ec.europa.eu/environment/gpp/eu\\_gpp\\_criteria\\_en.htm](http://ec.europa.eu/environment/gpp/eu_gpp_criteria_en.htm).

(62) See, e.g., R. BICKERSTAFF, "E-procurement under the new EU procurement Directives", *op. cit.*, p. 136; P. FERK, "Can the Implementation of Full E-Procurement into Real Life Address the Real Challenges of EU Public Procurement?", *op. cit.*, p. 332.

(63) L. BUTLER, "Innovation in Public Procurement: towards the 'Innovation Union'", *op. cit.*, pp. 337, 343, 346.

authorities as well as tenderers) can directly or indirectly benefit from that innovation. In addition, any state or office that is engaged in establishing or ordering a state-of-the-art e-procurement system can serve as a catalyst that actively promotes and introduces innovative electronic systems, creating an example possibly to be followed.(64)

### 3.3. Does the e-procurement system support the objective of effective review proceedings?

Even though in general, e-procurement systems have not been shown to cause special circumstances or specific obstacles with regard to review procedures in public procurement, an issue can be highlighted that concerns electronic procurement in particular. A procedural issue related to e-procurement concerns calculating the moment when a limitation period for review starts to run when the review concerns a contract document. Here, the national legislator might face the question, if the limitation period should be calculated to start to run exactly from the moment of *publishing* the concerned contract document that contains an allegedly unlawful (e.g. discriminatory) term as is referred to in the Remedies Directives,(65) or from the moment when that document was *actually accessed* by the person initiating the review procedure, provided that the period remains in harmony with the 10-day period prescribed by the Remedies Directives.

In public procurement matters, Member States may establish limitation periods for review procedures, and the triggers and lengths of those limitations periods are, as a rule, subject to the procedural autonomy of Member States.(66) However, the Remedies Directives as well as the case law of the CJEU provide some guidelines in this respect. In view of the principle of effectiveness, for instance, *the detailed methods for the application of national limitation periods must not render impossible or excessively difficult the exercise of any rights which the person concerned derives from Community law.*(67) According to the EU public procurement law, therefore, the limitation period may not

(64) On innovation taxonomy, incl. direct and catalytic procurement, see L. BUTLER, "Innovation in Public Procurement: towards the 'Innovation Union'", *op. cit.*, pp. 348-349.

(65) Art. 2c of Council Dir. 89/665/EEC of 21 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts; Art. 2c of Council Dir. 92/13/EEC of 25 February 1992 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors.

(66) S.-J. OTTO, "The Starting Point of Limitation Periods for Remedies in Public Procurement Procedures. Annotation on the Judgements of the European Court of Justice of 28 January 214 in Case C-161/13, *Idrodinamica Spurgo Velox and Others v Acquedotto Pugliese SpA*", *EPPPLR*, 2014, p. 209.

(67) ECJ, *Uniplex (UK) Ltd v NHS Business Services Authority*, case C-406/08, ECLI:EU:C:2010:45, par. 40.

start until the concerned party *knows or ought to know* of the alleged breach of procurement law.(68)

When the contracting authority publishes contract documents in the electronic public procurement register, such actual or presumed knowledge can be determined in two ways. First, one can presume that the time of limitation starts to run at the moment the contract documents are published. Second, one can start counting the time from the moment it can be established that a particular concerned party actually downloaded these documents or registered to participate in a particular procurement procedure.

In the first case, the length of the limitation period ends earlier, making the option of contesting the contract documents (e.g. based on discriminatory award conditions) somewhat shorter. However this option provides the concerned parties with somewhat more legal certainty, as after a certain date all the concerned parties can be sure that review of contract award conditions is no longer possible, as a rule. (An exception could be a situation where the concerned clause is so ambiguous as to allow different interpretations. In such cases, it is possible that, having relied on one possible version of interpreting the clause, a concerned party later learns of a different interpretation given to the clause by the contracting authority. Even when a limitation period for requesting review of the clause has already ended, the complaint should be accepted by the review body when the delay was caused by a mistake or difference in understanding in good-faith by the complainant.) The first alternative can be criticized for failing to provide adequate protection to the rights of interested parties as well as for failing the essential purpose of providing effective review options in public procurement matters. As such, the harmony of the solution with the remedies directives is questionable. Making the deadline depend on the date of publishing the contract documents can also put a disproportionate burden upon the concerned parties, particularly in the case of complex award procedures.(69)

In the second case, the opposite is true: tenderers' rights can be said to receive somewhat more protection, while reducing the legal certainty.

Until now, the case law of the Estonian Complaints Board has favoured the second option: as a rule, the Board established the exact moment when the particular tenderer learned or had the opportunity to learn that certain terms of contract documents violated its rights on a case-by-case basis. Often, either

(68) S.-J. ORTO, "The Starting Point of Limitation Periods for Remedies in Public Procurement Procedures. Annotation on the Judgements of the European Court of Justice of 28 January 214 in Case C-161/13, *Idrodinamica Spurgo Velox and Others v Acquadotto Pugliese SpA*", *op. cit.*, pp. 211-212.

(69) *Seletuskiri riigihangete seaduse eelnõu juurde*, lk 128.

the moment of downloading the contract documents or registering with the particular procurement was considered to be the moment of learning that these documents violated the tenderer's rights.(70)

However, the Act on Public Procurement now provides a new, 'compromise' version, tying the limitation period for review of contract documents to the term for submitting tenders. Depending on the value of the contract, a complaint must be submitted no later than two or five working days prior to the deadline for submitting tenders for 'simplified' (under national threshold) or ordinary procedures and not after the deadline for submitting tenders in procedures with shortened tender submission deadlines.(71) The explanatory letter accompanying the draft for the new Act refers to the fact that published contract documents can mostly be freely accessed without logging into the ePR, making it futile to connect the time limit for submitting complaints to the fact of the interested party actually learning about the alleged breach. Taking into account that under the new regulation, the limitation period for submitting a complaint on a contract document in a cross-border procurement is always at least ten days from the moment of publishing the documents, the regulation must be considered to be in harmony with the Remedies Directives.

#### 4. Conclusions

In the case of Estonia, a centralised e-procurement platform has succeeded in bringing the share of electronic procurement to 92% by 2016, and hopefully will facilitate a smooth transfer to 100% e-procurement very soon. The percentage of public contracts awarded to tenderers of other Member States as well as the relatively large average number of participants in e-procurements can be seen as a positive indicator of the benefits attributable to the Estonian ePR. One of the reasons for the success of the Estonian e-procurement system may be the comprehensive nature of the whole electronic procurement environment: in addition to the procurement register, the same webpage contains the register of the review decisions, a training site and an information portal. As a next step, further modernisation of the public procurement review system and the introduction of additional e-review functions should be considered.

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(70) This is established for instance in the following cases of the Complaints Board: *Vaidlustuskomisjoni otsus*, 8 July 2016, No. 153-16/174535, pp. 7-8; *Vaidlustuskomisjoni otsus*, 13 May 2016, No. 99-16/172874, pp. 4-5; *Vaidlustuskomisjoni otsus*, 10 February 2016, No. 23-16/170047, p. 5; *Vaidlustuskomisjoni otsus*, 11 April 2014, No. 82-14 /150647, p. 5; *Vaidlustuskomisjoni otsus*, 11 July 2014, No. 161 /152349, pp. 4.2-4.3.

(71) RHS § 189, lg 2, pp. 1-3.

# CHAPTER 19

## An Overview of Innovative Procurement in Eastern Europe

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### *1. Introduction*

Recent publications on public procurement by the Organization for Economic Co-operation and Development (OECD) and the European Union confirm the growing consensus on the role of public procurement in addressing social challenges, improving productivity, creating job opportunities and ensuring value for money.(1) Public procurers are becoming more concerned not only with ‘how to buy’ but also with ‘what to buy’.(2) They have started to spend taxpayers’ money beyond the mere satisfaction of their primary needs.(3) As a result, innovation becomes fundamental in ensuring that the procured solutions provide an added value in terms of quality, cost-efficiency, and environmental and social impact.(4)

The Oslo Manual (OECD, 2005) defines innovation as “the implementation of a new or significantly improved product or process; a new marketing method; a new organizational method in business practices, in workplace organization and/or external relations. As such, innovation can occur in any sector of the economy, including government services”.(5) To be innovative, any work, product, service or process must either have a significant

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(1) OECD, “Public Procurement for Innovation: Good Practices and Strategies”, *OECD Publ. Gov. Rev.*, Paris, OECD Publ., 2017, available at [read.oecd-ilibrary.org/governance/public-procurement-for-innovation\\_9789264265820-en#](http://read.oecd-ilibrary.org/governance/public-procurement-for-innovation_9789264265820-en#), 1.

(2) P. VALCARCEL FERNANDEZ, “The relevance of promoting collaborative and joint cross border public procurement for buying innovative solutions”, *Ius Publicum Network Rev.*, 1/2017, pp. 1 and ff.; S. PONZIO, “Joint Procurement and Innovation in the new EU Directive and in some EU-funded projects”, *Ius Publicum Network Rev.*, 1/2014, pp. 1 and ff. G.M. RACCA and S. PONZIO, “Nuovi modelli organizzativi per il joint procurement e l’innovazione dei contratti pubblici in Europa”, in *Compra Pubblica Agregada* (R.F. ACEVEDO and P. VALCARCEL FERNANDEZ eds), 2016, pp. 373-406.

(3) EU Comm., “Guidance on Innovation Procurement”, Brussels, 15 May 2018.

(4) *Ibid.*

(5) OECD, “Oslo Manual”, 2005, available at [www.oecd.org/sti/inno/2367580.pdf](http://www.oecd.org/sti/inno/2367580.pdf). See also *infra*, par. 3, Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC, Art. 2 (22).

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added value (in terms of increased social wellbeing or value for money); must be present on the market for less than two years and in small commercial volumes; or have used old technologies in new or novel ways.(6) This chapter presents innovation procurement in the European Union with particular reference to the role of public procurers in providing new solutions through a *demand-side* approach using pre-commercial procurement (PCP) and public procurement of innovative solutions (PPI). In doing so, this chapter is divided into four parts. The first part looks at public expenditure in the EU and the role of innovation in public procurement in ensuring more effective public services to citizens and/or achieving economies of scale and other important policy goals. Thereafter, this chapter analyses the increasing importance of a *demand-driven* approach to public procurement by using the main documents that support them at the EU level. It also provides a synthesis on the main distinctions between buying standard products and/or services and purchasing innovation (both in terms of product or process) through either PCP or PPI. The policy and legal framework of innovation procurement in the EU are analyzed thoroughly by giving particular attention to the most significant provisions in the 2014 EU public procurement directives on innovation procurement. The last two parts of this chapter discuss the results of a case study on the transposition of the 2014 EU public procurement directives in the national legal frameworks in certain Central European countries.(7)

## ***2. The Role of Public Procurement as a Driver of Innovation***

The overall expenditures by local and national governmental authorities for works, goods, and services represent 13.1% of European GDP, amounting to €3 billion in 2015.(8) The massive buying power in public procurement has significant impact on economic growth, jobs creation, competitiveness and the overall social well-being. In order to make this impact more effective, public authorities should cease to see procurement as a mere administrative and financial task. They must start to look at it as a strategic tool for purchasing

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(6) OECD, “The Innovation Imperative”, 2015, available at [www.oecd.org/publications/the-innovation-imperative-9789264239814-en.htm](http://www.oecd.org/publications/the-innovation-imperative-9789264239814-en.htm).

(7) In particular, the countries that participated in PPI2Innovate (*Capacity Building to Boost the usage of PPI in Central Europe*) project, a project funded by INTERREG covering six Member States from Central Europe, and namely Croatia, the Czech Republic, Hungary, Italy, Poland and Slovenia. For more information on the project, it is possible to look at the Web site: [www.interreg-central.eu/Content.Node/PPI2Innovate.html](http://www.interreg-central.eu/Content.Node/PPI2Innovate.html).

(8) EU Comm., “Public Procurement Indicators 2015”, available at [ec.europa.eu/DocsRoom/documents/20679/attachments/1/translations/en/renditions/native](http://ec.europa.eu/DocsRoom/documents/20679/attachments/1/translations/en/renditions/native).

not only standard and off-the-shelf products, but, rather, what is more important, innovative goods and services with a view to promoting broader policy objectives.

Innovation is, in fact, a key factor in addressing contemporary societal challenges.<sup>(9)</sup> It establishes clear linkages between purchases by the public sector and significant policy objectives such as reducing the environmental footprint, increasing energy efficiency, addressing climate change, promoting sustainable healthcare for the ageing population, facilitating the access of start-ups and SMEs to the market, reducing life-cycle costs, modernizing public service delivery, etc.<sup>(10)</sup> Nonetheless, innovation procurement is still a niche practice in Europe. Organisational issues and the lack of practical and theoretical expertise by procurers result in a certain degree of risk-aversion and resistance to change,<sup>(11)</sup> as well as poor management of the citizens' money,<sup>(12)</sup> are some of the reasons why mainstreaming innovative procurement across Europe remains a challenge.

For this reason, the European Union (EU) and its Member States are creating an innovation-friendly environment for public procurement by establishing a set of policies on innovation, including legal and financial measures. They are implementing new measures to address societal challenges and needs through innovative solutions that already exist in the market in small-scale volumes (Public Procurement of Innovative Solutions, PPI) or the development of state-of-the-art products during the R&D phase (Pre-Commercial Procurement, PCP). The EU policy framework has, in fact, substantially supported the demand-side approach in upscaling innovative procurement across Europe for the last ten years.

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(9) Dir. No. 2014/24/EU, *op. cit.*, recital 47: Research and innovation, including eco-innovation and social innovation, are among the main drivers of future growth and have been put at the centre of the Europe 2020 strategy for smart, sustainable and inclusive growth. Public authorities should make the best strategic use of public procurement to spur innovation. Buying innovative products, works and services plays a key role in improving the efficiency and quality of public services while addressing major societal challenges. It contributes to achieving best value for public money as well as wider economic, environmental and societal benefits in terms of generating new ideas, translating them into innovative products and services and thus promoting sustainable economic growth. Cf. M. CERUTI, "Sustainable Development and Smart Technological Innovation within PPPs: The Strategic Use of Public Procurement", *EPPPL*, No. 12, 2017, pp. 183. I. ZAPATRINA, "Sustainable Development Goals for Developing Economies and Public-Private Partnership", *EPPPL*, No. 11, 2016, p.39.

(10) EU Comm., "Guidance on Innovation Procurement", 15 May 2018.

(11) *Ibid.*

(12) OECD, "Public Procurement for Innovation: Good Practices and Strategies", *OECD Publ. Gov. Rev.*, 2017, *op. cit.*

### ***3. Demand-Driven Approaches to Public Procurement in the EU Policy Framework***

The European Commission acknowledged the many challenges in using a supply-side approach to innovation (*i.e.*, the earlier approach of subsidising the private sector). Nonetheless, from 2007 onwards, the Commission still decided to promote innovation from the demand side despite the shortcomings and difficulties in doing so. In certain cases, the funding of undertakings and enterprises for the development and commercialization of innovative goods and services has led to the infringement of EU rules on State aid.<sup>(13)</sup> In fact, there were reported cases where the financial support by public authorities had distorted competition in specific relevant markets. To address this issue, public procurers are required to implement demand-side policies by developing a thorough needs identification process within their respective organizations. Moreover, the 2014 Framework on State Aid for research and development and innovation provides the requirements for this type of aid, which states in part, “the Commission will consider that no State aid is awarded to undertakings where the price paid for the relevant services fully reflects the market value of the benefits received by the public purchaser and the risks taken by the participating providers”.<sup>(14)</sup>

The EU Commission Communication 799 (2007) on PCP sets down at least two conditions that have to be met in order to identify State aid when paying

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(13) Art. 107 of the TFEU: 1. Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favoring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market. 2. The following shall be compatible with the internal market: (a) aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned; (b) aid to make good the damage caused by natural disasters or exceptional occurrences; (c) aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, in so far as such aid is required in order to compensate for the economic disadvantages caused by that division. Five years after the entry into force of the Treaty of Lisbon, the Council, acting on a proposal from the Commission, may adopt a decision repealing this point. 3. The following may be considered to be compatible with the internal market: (a) aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment, and of the regions referred to in Article 349, in view of their structural, economic and social situation; (b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State; (c) aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest; (d) aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Union to an extent that is contrary to the common interest; (e) such other categories of aid as may be specified by decision of the Council on a proposal from the Commission.

(14) EU Comm., “Communication of the Commission on State Aid Framework for Research and Development and Innovation”, C(2014)3282, 21 May 2014, available at [eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014XC0627\(01\)&from=EN](http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52014XC0627(01)&from=EN).

for innovation. First, the risk-benefit sharing between the public authority and the economic operator shall not take place under market conditions, and, second, the price paid for the provided services shall be higher than the market price.<sup>(15)</sup> Accordingly, these payments must be “assessed by the Commission according to Articles 107-108 TFEU and the State Aid Framework for Research and Development and Innovation”.<sup>(16)</sup>

Contracting authorities can drive innovation from the demand side through a strategic and timely planning of the procurement process on the basis of their needs, and by promoting innovation in a functional way, which can ensure the high quality of public services for the citizens. They must also consider both the short- and long-term benefits of the proposed innovation by facilitating cooperation between and among different actors that will create economic and social wealth while encouraging industry to invest in new skills, equipment and R&D activities.<sup>(17)</sup> More specifically, governmental authorities must ensure the efficient alignment between their long-term visions and short-term actions in accordance with the twelve principles in the OECD Recommendations on Public Procurement (*i.e.*, transparency, integrity, access, balance, participation, efficiency, e-procurement, capacity, evaluation, risk-management, accountability, and integration).<sup>(18)</sup> Interestingly, some of these recommendations play an even greater role in innovation procurement.

Nevertheless, a balanced approach in their implementation is required to ensure that policy objectives and specific procurement needs are achieved in a coherent way in order to achieve best value procurement. From this perspective, the EU Commission supports the products and services that are capable of responding to actual demand of the public sector, favouring the ‘creation of the market’ to satisfy the specific needs of public administrations.

Contracting authorities are likewise encouraged to guarantee, while ensuring competition and transparency, broader access for SMEs – even at the cross-border and transnational levels – which are usually characterized by their greater innovation potential. In this vein, contracting authorities are encouraged to “divide large contracts into lots”, possibly accompanied

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(15) EU Comm., “Pre-commercial Procurement: Driving innovation to ensure sustainable high-quality public services in Europe”, available at [ec.europa.eu/invest-in-research/pdf/download\\_en/com\\_2007\\_799.pdf](http://ec.europa.eu/invest-in-research/pdf/download_en/com_2007_799.pdf).

(16) *Ibid.* See D.C. DRAGOS and B. RACOLTA, “Comparing Legal Instruments for R&D&I: State Aid and Public Procurement”, *EPPPL*, No. 12, 2017, p. 408. S. BEDIN, “HT.618 Consultation on the draft R&D&I-Framework”, 2014.

(17) OECD, “Public Procurement for Innovation: Good Practices and Strategies”, *OECD Publ. Gov. Rev.*, *op. cit.*

(18) OECD, *Recommendation of the Council on Public Procurement*, Paris, OECD Publ.2015.

by a maximum number of lots that can be awarded to one bidder. Lots strategies can be developed on a quantitative basis or on a qualitative basis.(19)

To develop an accurate needs identification and assessment process, contracting authorities must also ensure that all stakeholders and end-users participate in the procurement cycle in accordance with the bottom-up approach, so that undertakings are encouraged to invest in R&D activities. This strategy could usefully be combined with a top-down approach (structured in thematic threads that have been pre-defined by the Commission), which is enhanced by the Europe2020 strategy, and may be used in a complementary way (possibly, in the future, through open calls making the process of needs analysis even more free and authentic). As a matter of fact, dialogue and understanding with qualified stakeholders (such as citizens, final users, providers of the service, etc.) are irreplaceable tools to identify an actual need.

Moreover, contracting authorities must address the perennial need to professionalize the procurement practice by providing quantitative and qualitative criteria for hiring or appointing of procurement professionals. Professionalization in public procurement breaks the vicious cycle of lack of capacity in procurement professionals, which results too often in pronounced risk-aversion.(20)

To validly assess the impact of innovative procurement, it is fundamental to develop indicators and benchmarks for a comprehensive evaluation, such as the use of risk-management techniques at every step within the procurement cycle. Digitalization of procurement procedures also helps in increasing access, competition, and innovation in public procurement.(21) When successfully carried out, innovative procurement ensures the optimum combination of higher quality, faster delivery and/or reduced life-cycle costs while opening more opportunities for innovative suppliers in

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(19) G.M. RACCA and S. PONZIO, “La scelta del contraente come funzione pubblica: in modelli organizzativi per l’aggregazione dei contratti pubblici”, *Dir. Amm.*, 2019, forthcoming; C. NICHOLAS and A. CAROLINE MÜLLER, “SME Participation in Government Procurement Markets. Legal and Policy Considerations under the WTO Agreement on Government Procurement and the UNCITRAL Model Law on Public Procurement”, in *Small and Medium-Sized Enterprises in International Economic Law* (T. RENSMANN ed.), Oxford, OUP, 2017, pp. 123-161; cf. B. RAGANELLI, “PMI, Procurement e favor participationis”, *Rivista italiana di Diritto Pubbl. Com.*, f. 3-4, 2007, pp. 839 and ff.

(20) See the chap. 3 in this book, R. CAVALLO PERIN and G.M. RACCA, “European Cross-border Procurement and Innovation”. See also P.T. MCKEEN, “The importance of a professionally educated public procurement workforce: lessons learned from the U.S. experience”, in *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (G.M. RACCA and C.R. YUKINS eds), Brussels, Bruylant, 2014.

(21) See the chap. 17 in this book, M. PIGNATTI, “Electronic Means as an Approach to Public Purchasing. S. PONZIO, “Joint Procurement and Innovation in the new EU Directive and in some EU-funded projects”, *op. cit.*, p. 10.

public procurement market that will eventually foster their economic and industrial growth.(22)

As already said, the European Union promotes a *demand-driven* innovation in public procurement through both PCP and PPI. If innovation constitutes the strategic objective of the public procurers, PCP and PPI represent two possible approaches in the procurement process. PCP and PPI may be used independently (*i.e.*, PCP and PPI are two distinct approaches in innovative procurement), or when the public authority decides to buy the outcomes of an R&D activity (such as in cases when a PPI follows a previous PCP) they might be applied in a complementary way.

PCP is designed to steer the development of innovative solutions to a particular public sector need.(23) In practice, PCP is not used for the procurement of already existing products or services. Instead, PCP explores the possible design for alternative solutions through either prototyping or developing a limited volume of products that are identified as one of the best possible outcomes.

The PCP approach doesn't imply an obligation to adopt the results of the process; it is rather related to an obligation of providing the means to develop a diligent performance of an R&D activity, thus allowing the contracting authority to compare different solutions on the basis of predefined indicators and objectives that must be adequately described to safeguard competition in each phase of the tender.(24) This approach is characterised by risk-benefit sharing according to market conditions, competitive development in phases, separation between R&D, and final commercialisation of end-products. PCP that operates completely outside the market is mainly concerned with the previous R&D phase.

In the case of successful R&D activities, the contracting authorities may confirm (or not) the idea of investing in a commercial phase by means of another open tender that re-opens the competition to those undertakings that are not included in the PCP process, but can help in developing more effective solutions and ensured a more efficient allocation of taxpayers' money.

In this context, central purchasing bodies (CPBs) play a key role in promoting the development of contracting authorities' networks and providing their expertise and, in case of for complex operations. CPBs also help in the monitoring of R&D procurements.

PPI, on the other hand, is an innovative approach in public procurement where contracting authorities act as launch customers (also called early

(22) EU Comm., "Guidance on Innovation Procurement", aforesaid.

(23) Dir. 2014/24/EU, Art. 47.

(24) See EU Comm., "Pre-commercial Procurement: Driving innovation to ensure sustainable high-quality public services in Europe", aforesaid.

adopters or first buyers) of innovative goods, works or services, which are near to the market or already available on a small-scale commercial basis. In a PPI project, procurers announce in advance their intention to buy a significant volume of innovative solutions in order to prompt the industry to bring to the market the proposed solutions with desired quality/price ratios within a specific period. PPI also provides economic operators the opportunity to test their new solutions under real-life conditions.<sup>(25)</sup>

Unlike PPI, PCP does not fall within the scope of EU public procurement law, but respects the general principles of transparency, equal access and fair competition.

The most suitable financial opportunities for innovation procurement are the European Structural and Investment Funds (ESIF) and the Horizon 2020 programme. In particular, Horizon 2020 finances both PCP and PPI projects that are cross-border in nature. It implements the Innovation Union, which is one of Europe 2020 flagship initiatives for securing European global competitiveness by boosting excellence in science, strengthening industrial leadership and addressing societal challenges. Its intention is to ensure the proper coordination and support actions (both in the preparation and execution phase) among EU State Members by bringing together procurers from different countries in identifying the grounds for possible collaboration (up to 90% for PCP and 35% for PPI).

#### ***4. The Challenges in Transposition of EU Procurement Regulations in Eastern Europe***

PPI is fully regulated by the provisions of the EU Public Procurement Directives.

European institutions support innovation procurement through dedicated funding schemes and have established an innovation-friendly legal framework.<sup>(26)</sup>

Nonetheless, the most important step for the creation of an EU innovation-friendly legal environment is the adoption of the new public procurement directive (2014/24/EU). The Directive has modernized public procurement by adjusting the legal framework to the needs of public buyers and economic operators on the basis of the most recent technological developments, economic

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(25) *Ibid.*; see also F. CLERMONT and F. FIONDA, "A Modern Approach for Procuring Research and Innovation: The Pre-Commercial Public Procurement", *EPPPL*, No. 11, 2016, p. 88. S. BEDIN, "HT.618 Consultation on the draft R&D&I-Framework", 2014.

(26) EU Comm., DG Growth, "Study on strategic use of public procurement", 2016.

trends, and, as a consequence of the increasing societal interests, by focusing on sustainable public spending.(27) New rules for fostering the aggregation of public procurement of goods, services and work as well as the innovation in public procurement, including through IT tools, have been provided.

Article 2, paragraph 22, of the 2014/24/EU Directive defines innovation as “the implementation of a new or significantly improved product, service or process, including but not limited to production, building or construction processes, a new marketing method, or a new organisational method in business practices, workplace organisation or external relations inter alia with the purpose of helping to solve societal challenges or to support the Europe 2020 strategy for smart, sustainable and inclusive growth”.(28) Because of its fundamental role in enhancing innovation, PPI is strongly supported at the European level. This implies the need for developing a new professionalism in public procurement and a new openness to different forms of cooperation among contracting authorities (in particular CPBs) from different Member States.(29) The new strategies of cooperation in public procurement may allow the contracting authorities “to derive maximum benefit from the potential of the internal market in terms of economies of scale and risk-benefit sharing”,(30) while encouraging the participation of SMEs and new innovative companies in public tenders.(31)

National policies and institutional frameworks that foster innovation are different in Eastern Europe countries with regard to the distribution of competences at various institutional levels (*i.e.* national, regional, and local).(32)

Croatia, for example, has issued the Strategy for Innovation Encouragement of Croatia 2014-2020, which emphasises the importance of developing alliances with SMEs in encouraging innovation, through the

(27) EU Comm., “Guidance on Innovation Procurement”, aforesaid.

(28) An important project that highlights the challenges on the transposition of the EU Directive to the national procurement policies and legal framework is the PPI2Innovate project. Within this project a “Trans-regional Study on Institutional Frameworks” has been realised covering the implementation of the EU Dir. 2014/24 in six participating countries: Croatia, Czech Republic, Hungary, Italy, Poland and Slovenia. This Study is available at [www.interreg-central.eu/Content.Node/PPI2Innovate/Transregional-study-on-institutional-frameworks-EN.pdf](http://www.interreg-central.eu/Content.Node/PPI2Innovate/Transregional-study-on-institutional-frameworks-EN.pdf).

(29) See chap. 3, in this book, R. CAVALLO PERIN and G.M. RACCA, “European Cross-border Procurement and Innovation”. S. PONZIO, “Joint Procurement and Innovation in the new EU Directive and in some EU-funded projects”, *op. cit.*, p. 10.

(30) Dir. 2014/24/EU, Wh. 73.

(31) The first results of EU-funded PCP projects demonstrate that half of the solutions developed in this context were deployed within a year, thus opening a route to the market for start-ups and innovative SMEs (71% of contracts are awarded to SMEs/start-ups); stimulating cross-border expansion (34,6% of contracts are awarded on a cross-border basis); and strengthening the European competitiveness (97,5% of contractors perform 100% of their research and development in Europe).

(32) The analysis concerns the partner countries of the mentioned PPI2Innovate project.

HAMAG-BICRO, the Croatian Agency for SMEs, Innovations and Investments. Under the supervision of the Ministry of Entrepreneurship and Crafts, HAMAG-BICRO supports the development of SMEs, improves the innovation process and encourages investments.(33) In Poland, the Polish Agency for Enterprise Development promotes the role of SMEs through its published document on Public Procurement Versus Innovation in SMEs.(34) In Italy, the Legislative Decree 50/2016 on public contracts encourages networks of central purchasing bodies (CPBs) in order to promote, among others, the participation of SMEs.(35) Hungary intends to make it easier for SMEs to access the procurement market through Act CXLII on Public Procurement, which took effect on 1 July 2016,(36) although the excess of formalism in the preparation phase in public procurement, underuse of e-procurement, heavy administrative burdens, and lengthy payment times from public authorities have all made it difficult for SMEs to have direct access to public procurement.(37) Slovenia has addressed similar challenges on ease of access to the procurement market by establishing the Slovenia Enterprise Fund, an independent agency that deals with co-financing and subsidizing SMEs activities.(38)

The Directive recognizes the need to support new innovative companies that have disruptive and totally new solutions to unmet needs but are facing difficulties such as limited distribution channels for market expansions. The Directive similarly clarifies the rules for more effective market consultations in the preparation of tenders and in the conduct of procurement procedures by allowing for the use of various forms of market consultation such as physical and online meetings or questionnaires, presentations and testing of samples allowing end-users to verify the suitability of the proposed solutions in real-life conditions, and conventional methods such as competitions, hackathons, idea markets or category innovation roadmaps.(39) In addition, the Directive promotes a greater consideration for environmental, social and innovation-related award criteria with emphasis on the total life-cycle cost of a certain solution, and strengthens the support for a larger market pull, and spreads the

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(33) “Trans-Regional Study on Institutional Frameworks”, aforesaid. Cf. E.M. SKUGOR, “EU Procurement Reform – the case of Croatia”, *PPLR*, 2017, No. 2, pp. 115-113. “Croatia needs to decide whether it is keen on making SME participation in public procurement procedures a matter of greater economic interest and, if so, how best to tackle the disparity between the situation in public procurement and the increasing worth of SMEs for the overall economy”.

(34) “Trans-Regional Study on Institutional Frameworks”, aforesaid, p. 9.

(35) *Ibid.*, p. 23.

(36) *Ibid.*, p. 6.

(37) *Ibid.*, p. 29.

(38) *Ibid.*, p. 10.

(39) EC, “Guidance on Innovation Procurement”, aforesaid.

individual procurement risk in early innovative projects through more neatly defined rules on joint and cross-border procurement.(40)

Furthermore, the Directive fosters innovation-friendly procurement procedures by introducing the innovation partnership, which enables contracting authorities to have an innovative solution tailored to their requirements through R&D funding similar to the procurement of the innovative solution.(41) This procedure, in contrast to PCP, constitutes an actual procurement procedure leaving contracting authorities greater flexibility in the design of the process (phased or not; with multiple awards or a single award; with the subdivision of risks and benefits or not), while the obligation to respect the principle of competition remains. The combination of PCP and PPI puts together R&D activities and the purchase of innovative solutions in a unique, phased procedure. Nevertheless, such advantage is counterbalanced by the risk that the final product or service might not be in line with the qualitative standards and needs of public administration which may change over time.

The Public Procurement Directive also clarifies the rules on the conduct of competitive procedures with negotiation, which may be used to improve and adapt tenders in a way to obtain the best possible outcomes. Furthermore, it simplifies the rules on the conduct of competitive dialogue, which is useful for the procurement of technically and financially complex projects. It is worth noting that the Directive gives preference to these procurement procedures over the “standard” open and restricted procedures because they allow for greater interaction and dialogue with the market.

The Directive(42) gives a more detailed structure for preliminary market consultation (PMC), describing it as a fundamental preparatory phase to enable procurers to cross-check their needs with actual offers on the market. Through PMC, contracting authorities will be able to identify the appropriate procurement approach, the desired minimum requirements for the innovative solutions, and the feasibility of the main assumptions derived from the business case, the subject of the PMC. PMC has feedback mechanisms that enable contracting

(40) In particular, Dir. 2014/24/EU (Art. 39) provides different means to permit contracting authorities from different Member States to act jointly in the award of public contracts through the possibility for contracting authorities of one Member States to use centralised purchasing activities offered by CPBs located in another Member State (and to offer, providing this possibility in the tender documents, its activities to contracting authorities from other Member States: *see* below, Art. 39, § 2: “Member States shall not forbid” this possibility); the possibility for contracting authorities from different Member States to jointly award a public contract, conclude a framework agreement or operate a dynamic purchasing system (*see* Art. 39, § 3, Dir. 24/2014/EU); the possibility to set up a joint entity, including European Groupings of Territorial Cooperation (EGTC) (*see* Art. 39, § 5, Dir. 24/2014/EU).

(41) *See*, on this issue, chap. 12 in this book, C. KRÖNKE, “Innovation Partnerships: Purpose, Scope of Application and Key Elements of a New Instrument of Strategic Procurement”. *See* also A. CASTELLI, “Smart Cities and Innovation Partnership A New Way of Pursuing Economic Wealth and Social Welfare”, *EPPPL*, No. 13, 2018, p. 207.

(42) *See* Art. 40, Dir. 24/2014/EU.

authorities raise the interest of the market to respond in an upcoming call for tenders and to increase the likelihood for economic players to respond to the said call for tenders. Contracting authorities are required to ensure transparency and non-discrimination even during the conduct of a PMC.

Innovation procurement using PMC allows public procurers to engage with the market at an early stage, more particularly, in cases where they have already identified their needs and have completed the corresponding cost-benefit analysis. PMC gives them an opportunity to gather relevant information about the project and evaluate the ability of economic operators to develop innovative solutions within a given time.<sup>(43)</sup> It also allows contracting authorities to effectively communicate their needs to suppliers as they prepare the tender and inform economic operators of their procurement plans and requirements. In doing so, contracting authorities can either adopt a top-down approach by asking economic operators to present their solutions, or a bottom-up consultation with end-users (e.g. medical staff and patients of a hospital) through an interview on their most significant unmet needs (e.g. high temperature in rooms) and their suggestions on possible ways to address their needs (e.g. by providing an energy-efficient air conditioning system).

The specific provision on PMC in the 2014/24/EU Directive has institutionalized the ‘technical dialogue’ under recital 8 of Directive 2004/18/EC by enhancing the legal security in consulting the market before drafting the technical specifications. The new directive recognizes the possibility of potential tenderers having a precise and understandable description of the goods or services to be supplied, and, participating in a preliminary market consultant will give them an opportunity to decide on whether the call for tender is of interest to them.

In Italy, for example, contracting authorities use a PMC before launching a procurement procedure to inform economic operators of their relevant plans and requirements and to define the functional specifications of the products/services to be procured.<sup>(44)</sup> The new PPAs in Croatia, Hungary and Slovenia allow the use of a PMC before the procurement procedures. PMC can be done with independent experts, public authorities and companies in order to provide economic operators with the relevant information about the procurement project. Despite the transposition of the EU Directive PMC provision in the national legal framework, there are issues on available data to support its implementation. For instance, in Croatia, “there are no data of occurring or

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(43) OECD, “Public Procurement for Innovation: Good Practices and Strategies”, *OECD Publ. Gov. Rev., op. cit.* Cf. O. PANTILIMON VODA and C. JOBSE, “Rules and Boundaries Surrounding Market Consultations in Innovation Procurement: Understanding and Addressing the Legal Risks”, *EPPPL*, No. 11, 2016, p. 179.

(44) “Trans-Regional Study on Institutional Frameworks”, aforesaid, p. 18.

occurred procedures” using PMCs,(45) while in Slovenia, PMC has not been used in innovation procurement.(46)

The other approach by which contracting authorities promote innovation in procurement is by including in the technical specifications (Art. 42, EU Dir. 24/2014) of the procurement documents for works, services and supplies their requirements for buying innovation. The technical specifications may include functional and performance requirements designed to achieve the objectives in the best possible way. Functional and performance-related requirements are appropriate means to favour innovation in public procurement.

In the Healthy Ageing Public Procurement of Innovations (HAPPI) project,(47) for example, partners made reference to functional requirements. For the procurement of a fall alert system, project partners drew up technical and functional requirements by describing the expected performances of the product, such as detecting falls by persons/residents/patients; alerting in the event of an actual fall, making it possible to ensure that the alert was noticed, and tracing alerts so that medical personnel would be able to access a history to permit optimized fall management. Partners also described the actual functionalities of the device (*i.e.* not changing the nature of the living space of the patient or resident; being neutral for the patient/resident, not requiring the wearing of a device; respecting the person’s privacy; allowing parameterization according to different fall contexts; allowing the transmission of the alert inside and outside the institution, with information on the place of the fall and the time of the alert).

In this phase, it is important to stress the need for a preliminary market consultation (PMC). A comprehensive and reciprocally beneficial dialogue with the market can help in identifying the most innovative products and in drawing up detailed technical specifications, while ensuring the principles of transparency, equal opportunity and competitiveness, in order to encourage a wider participation.

Aside from the technical specifications, the exclusion criteria may also be used in innovation procurement under the new EU procurement rules (Art. 57 of Dir. 2014/24/EU). These criteria allow a contracting authority to exclude economic operators from participating in the award procedure based on past behaviour (e.g. corruption, money laundering, participation in criminal activities, etc.) and/or the use of selection criteria such as the requirements for professional activity, economic and financial standing, technical and professional

(45) *Ibid.*, p. 15.

(46) *Ibid.*, 20.

(47) The HAPPI project is a cross-border PPI established by central purchasing bodies from 5 different Member States of the European Union in order to procure solutions for the healthy ageing through a single framework agreement divided in 5 different product lots.

ability to perform the contract, previous experiences on similar contract, and availability of qualified personnel.

In Italy, for instance, it is mandatory for all national contracting authorities to adopt all the discretionary exclusions grounds under paragraph 4 of Article 57 of the EU Directive 24/2014, thereby limiting their discretionary authority in deciding whether to exclude the affected economic operator.(48) Unlike in Croatia, discretion is exercised in the implementation of exclusion grounds,(49) and in the Czech Republic, exclusion may be disregarded on specific procurements, such as emergency procurements for the public interest, *i.e.*, health and environmental protection.(50) Poland has mandatory and discretionary exclusions. It is mandatory in cases of distortion of competition through bid-rigging, misrepresentation by the supplier in presenting the absence of grounds for its exclusion, and interference in the selection procedure, and discretionary in the case of bankruptcy, serious professional misconduct, unsolvable conflict of interests, and lack of effective compliance in previous procurement procedures.(51) Interestingly, Slovenia allows the contracting authorities to examine the bids before checking the absence of exclusion grounds in case of open procedures or specific procedures under the EU threshold, while also providing for the possibility to request economic operators to submit, supplement, clarify or complete the information or documentation.(52)

Finally, innovation procurement gives paramount significance to the award criteria. The 2014 EU public procurement directives provide preference to the use of Most Economically Advantageous Tender (MEAT)(53) in the award criteria. Accordingly, the award of the contract should not be based exclusively on the lowest price criteria but should also take into account other non-price factors such as the quality of the tender. As a result, economic operators are encouraged to ensure the highest quality/price ratio. In the end, it is still the duty of the public procurer to identify an optimal combination of award criteria that assesses the costs over the entire expected life-time of the product and the convergence between proposed solutions and users' needs.

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(48) "Trans-Regional Study on Institutional Frameworks", aforesaid, p. 29.

(49) *Ibid.*, p. 25.

(50) *Ibid.*, p. 27.

(51) *Ibid.*, p. 31.

(52) *Ibid.*, p. 32.

(53) Dir. 2014/24/EU, Art. 67.

### ***5. A Case Study on PPI in Eastern Europe: Lessons Learned from the PPI2Innovate Project***

The European Commission emphasized the significant advantages of introducing joint procurement in PPI projects to boost modernization of the public sector in bringing higher quality and efficiency of public services at a reduced price; promoting better value for money, which enables procurers to share costs and experiences in order to procure solutions that respond to concrete public needs; encouraging new innovative solutions to challenges of common interest by overcoming fragmentation and ensuring interoperability and coherent actions; promoting economic growth through the creation of broader job possibilities by means of greater involvement of SMEs; and, eventually, shortening time to market through a customer-driven approach (average 18 months).

The PPI2Innovate (Capacity building to boost usage of PPI in Central Europe) has been implemented within the EU-funded programme “Interreg CENTRAL EUROPE” by a consortium of ten partners from six countries in Central Europe (Croatia, Czech Republic, Hungary, Italy, Poland and Slovenia). The consortium gathers sectoral agencies,<sup>(54)</sup> research and innovation actors<sup>(55)</sup> and policy administrations<sup>(56)</sup> with the final goal of encouraging the use of Public Procurement of Innovative solutions (PPI) by public procurers across Central Europe. The project targets public procurers at all administrative levels in Central Europe in an effort to build regional capacities, change attitudes towards PPI, strengthen linkages among relevant stakeholders in regional innovation systems, and thus boost the implementation of PPI in Central Europe.

In order to achieve the aims of the project, thematic tools have been applied in three crucial public sectors (SMART-Health, SMART-Energy and SMART-ICT), which were fully customized to six national institutional frameworks and translated into each national language. These tools concern the theoretical background on public procurement of innovation as well as a practical approach. Such an approach includes the different phases of a PPI, from the preliminary activities to the implementation of the award procedure (through the identification of the organisational model and the subsequent procurement strategies), until the execution phase of the contract. The next steps foresee six action plans for the operationalization of Competence Centres that will be

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<sup>(54)</sup> Bicro, CTRIA, RARR.

<sup>(55)</sup> University of Turin-UNITO, ICT TN, DEX IC.

<sup>(56)</sup> Ministry of Public Administration of Slovenia, Piedmont Region, Somogy County and City of Lublin.

established by the networking partners, covering the implementation of PPI pilot projects at the regional level and in the energy, health and ICT sectors, thus favoring the implementation of PPI through the professionalization of public procurement.

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**CHAPTER 20**  
**The New Asian Development Bank**  
**Procurement Policy and Regulations:**  
**Promoting Innovation in Public**  
**Procurement in Asia?**

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***1. Introduction***

The Asian Development Bank (ADB) is one of the multilateral development banks that has recently issued new policies and regulations in public procurement.(1) In April 2017, ADB approved a new procurement policy, and three months later (July 2017) ADB released the new “Procurement Regulations for ADB Borrowers,” replacing the 2013 Guidelines on the Use of Consultants and the 2015 Procurement Guidelines. While ADB has been very vocal that its policies and guidelines are “amended from time to time,” it is, however, worth noting that in these new documents, ADB uses the word ‘regulations’ instead of guidelines, arguably suggesting more binding requirements to its borrowers and recipients. In fact, a year later (June 2018), ADB elaborated on and explained these new policies and regulations by issuing 24 Guidance Notes for ADB Procurement Policy and the Procurement Regulations,(2) which are divided into six areas: (1) preparation and planning – procurement risk framework, strategic procurement planning, procurement review, and alternative procurement arrangements; (2) procurement methods – open competitive

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(1) The African Development Bank issued the Procurement Policy for Bank Group Funded Operations in 2015; the World Bank issued Procurement Regulations for Investment Project Financing (IPF) Borrowers in 2016, and the European Bank for Reconstruction and Development released its Procurement Policies and Rules in 2017, among others. See also P. TREPTE, “All change at the World Bank? The new procurement framework”, *PPLR*, 2016, No. 4, pp. 121-150. J. JACKHOLT, “The procurement policies and rules and the procurement activities of the European Bank for Reconstruction and Development (EBRD)”, *PPLR*, 2016, No. 4, pp. 172-178. V. SHARMA, “An update on procurement reforms at the African Development Bank”, *PPLR*, 2016, No. 4, pp. 151-163. A. SALAZAR and M. LOPEZ, “The Inter-American Development Bank: reform to build up and increase the use of national procurement systems in Latin American and the Caribbean”, *PPLR*, 2016, No. 4, pp. 164-171.

(2) See Asian Development Bank, “Guide Notes on Procurement”.

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bidding, consulting services, non-consulting services, and framework agreements on consulting; (3) bidding procedures – procurement price adjustment, procurement prequalification, procurement subcontracting, and procurement domestic preference; (4) new principles and practices – value for money, quality, contract management and abnormally low bids; (5) complaints, compliance and eligibility – bidding related complaints, noncompliance procurement, standstill period and State-owned enterprises; and (6) specialized areas – procurement in fragile situations, e-procurement, public private partnership procurement, and high-level technology. This chapter highlights the significant changes in the new procurement policy, regulations, and their supporting notes; more particularly, this chapter tries to identify the strategic innovations in these new instruments that may promote innovations in public procurement in Asia.

## ***2. Asian Development Bank and Asia: Its Past, Present and Future***

The ADB was conceived in the early 1960s as a financial institution that would be Asian in character and would foster economic growth and cooperation in one of the poorest regions in the world.<sup>(3)</sup> From 31 members at its establishment in 1966, ADB has grown to encompass 67 members – of which 48 are from within Asia and the Pacific and 19 from outside. In partnership with member governments, independent specialists and other financial institutions, ADB is focused on delivering projects in developing member countries that create economic and development impact.

As a multilateral development finance institution, ADB provides not only loans, technical assistance and grants to its member governments, but also equity investments and loans to private enterprises of developing member countries. ADB raises funds through the issuance of bonds in the world's capital markets, the contributions from the members, the retained earnings from lending operations, and the repayment of loans. ADB's total operations of \$32.2 billion in 2017 consisted of \$20.1 billion in loans, grants, and investments from its own resources (up 51% from 2016) including non-sovereign operations<sup>(4)</sup> of

(3) See also the President and Chair of the Board of Directors Asian Development Bank, T. NAKAO, "Foreword", p. xii. P. MCCAWLEY, *Banking on the Future of Asia and the Pacific, 50 years of the Asian Development Bank*, Mandaluyong, ADB, 2017, "When ADB was established in 1966 [...] Asia was the poorest region in the world with an annual per capita income of about \$100 (less than ¼ of that of Latin America and below Sub-Saharan Africa) [...] Half a century later, Asia has emerged as a center of global dynamism. Today, it accounts for one-third of global GDP and contributes more than half of the world's economic growth [...] ADB has played an important role in the transformation of Asia".

(4) Nonsovereign operations comprise the provision of any loan, guarantee, equity investment, or other financing arrangement to privately held, State-owned, or subsovereign entities, in each case, (i) without a government guarantee... or (ii) with a government guarantee, under terms that do not allow ADB, upon default by the guarantor, to accelerate, suspend, or cancel any other loan or guarantee

\$2.3 billion (a 31% increase from 2016); \$11.9 billion in co-financing from bilateral and multilateral agencies and other financing partners; and \$201 million in technical assistance (an 11% increase from 2016).

### **3. ADB's Milestones in Procurement Reforms, 1960s to 2017**

ADB formulated its first policies on procurement as early as 1968,(5) and access to special funds (*i.e.*, funds that allowed ADB to make soft loans with long payback periods of up to 40 years and at low interest rates of 1.5%) from donor countries during those period were often “tied to procurement from donor countries”.(6) It was only in 1976 when ADB modified its domestic procurement guidelines for ADB-financed projects(7) by agreeing to finance the same portion or percentage of contract regardless of whether the contract was awarded to a domestic or foreign supplier/contractor, provided international competitive bidding was effectively carried out, and by permitting the procurement of domestic goods and construction services under ADB financing.(8)

Ten years later (*i.e.*, on the 10<sup>th</sup> annual meeting of ADB in 1977), ADB concluded the need to reform its operations by improving the procurement of goods and consultants. Borrowing countries noted that ADB was slow in disbursing funds because of its complicated procedures (including procedures on procurement).(9) In fact, it was this year (1977) when ADB conducted a comprehensive review of its financial policies, disbursements, and other loan administration matters in the hope of simplifying its procedures.(10) As a result, ADB issued revised guidelines on the use of consultants and procurement.(11)

A year later, in 1978, ADB reconsidered its procurement guidelines since it was one of the possible causes of delays,(12) and reviewed its domestic procurement and

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between ADB and the related sovereign. Asian Development Bank, “ADB Operations Manual Bank Policies and Procedures”, OM section D10, Iss. 24 May 2016.

(5) P. McCawley, *Banking on the Future of Asia and the Pacific: 50 years of the Asian Development Bank, op. cit.*, pp. 3 and ff., esp. p. 474.

(6) *Ibid.*, esp. p. 88: “In December 1969, the Agricultural Special Fund (ASF) was set up... following a contribution from Japan (7.2 billion yen, or \$20 million equivalent) to finance special projects in agricultural development. A similar agreement was signed with Canada for its contribution to the Multi-Purpose Special Fund (MPSF) (for \$25 million equivalent). These were voluntary and often tied to procurement in contributing countries”, *ibid.*, esp. p. 96.

(7) *Ibid.*, esp. p. 476.

(8) Asian Development Bank, *ADB Annual Report 1976*, pp. 23-25.

(9) P. McCawley, *Banking on the Future of Asia and the Pacific: 50 years of the Asian Development Bank, op. cit.*, pp. 3 and ff., esp. p. 123-124.

(10) *Ibid.*, p. 14.

(11) *Ibid.*, p. 16.

(12) *Ibid.*, pp. 3 and ff., esp. p. 140.

local currency financing;(13) ADB remained under pressure, though especially from industrialized countries, to maintain close controls over procurement arrangements.(14) In 1988, ADB intensified its project administration efforts and introduced innovative and streamlined project administration, *i.e.* through delegation of more authority to executing agencies, earlier procurement, and recruitment of consultants.(15)

Although the 1990s marked an era for new trade arrangements (*i.e.* establishment of the World Trade Organization), leaders from developing and industrial countries still disagreed over government procurement, among other issues.(16) Nonetheless, ADB (in 1995) became the first development bank to develop a governance policy to ensure that development assistance fully benefits the poor.(17)

Another decade passed before ADB responded to the concerns of borrowing countries and donors on complicated arrangements, by streamlining its business processes – in particular, simplifying procurement and documentation requirements.(18) In fact, the year 2000 marked an era for more accountable and effective assistance from ADB, when it became the first multilateral development bank to establish a two-phase accountability mechanism: an informal consultation phase for those affected by ADB projects and a compliance review phase to investigate alleged violations of operational arrangements.(19) ADB likewise engaged with civil society to achieve environmental and social objectives.(20) The ideals of environmental protection and sustainability came to be more strongly reflected in the Sustainable Development Goals (SDG) in 2015. SDGs are more extensive than MDGs because they embraced a triple bottom line, combining economic development, environmental sustainability and social inclusion.(21)

In 2008, ADB approved Strategy 2020 which reaffirmed both ADB's vision of an Asia and Pacific free of poverty and its mission to help its developing member countries improve their living conditions and quality of life.

Interestingly, in 2015, choices for borrowing countries in Asia widened. Two financial institutions were established – the Asian Infrastructure Investment Bank (AIIB) in Beijing and the New Development Bank (NDB) in Shanghai. Although both institutions were based in China, the latter was

(13) *Ibid.*, pp. 3 and ff., esp. p. 477.

(14) *Ibid.*, pp. 3 and ff., esp. p. 140.

(15) *Ibid.*, p. 18.

(16) *Ibid.*, pp. 3 and ff., esp. p. 159.

(17) *Ibid.*, p. 264.

(18) *Ibid.*, pp. 22 and ff., esp. pp. 264-267.

(19) *Ibid.*, pp. 22.

(20) *Ibid.*

(21) *Ibid.*, pp. 22 and ff. esp. pp. 301-302.

established by Brazil, the Russian Federation, India, the People's Republic of China and South Africa, and was considered the first MDB set up entirely by emerging economies.(22) Both institutions have adopted standards for addressing the environmental and social impacts of projects, as well as for fair and transparent procurement systems that are at par with those of the existing MDBs.(23)

In response to the call for a “stronger, better, and faster ADB,” ADB started a new initiative for incorporating advanced technologies in projects by strengthening project design, putting more emphasis on quality in procurement procedures and helping countries access the best expertise.(24) ADB likewise improved business processes through a 10-point program, which aimed at reducing procurement time while maintaining fiduciary oversight. ADB implemented faster processing of procurement contracts and delegated more authority to resident missions, and thereby enabled ADB's staff to work closely with their clients (*i.e.*, Member States and private enterprises).(25)

In 2017, ADB approved a new procurement policy that “marks a transition from a ‘one size fits all’ approach to a ‘fit for purpose approach’.(26) Accordingly, the new procurement policy will help achieve value for money by improving the quality of procurement decisions, reducing overall procurement time, permitting the use of customized procurement methods, and supporting high-level technologies.(27)

#### **4. ADB at 50: Innovations in Public Procurement**

The year 2016 marked not only the fiftieth anniversary of ADB, but also the second generation of procurement reforms.(28) ADB introduced procurement reforms intended to ensure value for money (VFM) by improving flexibility, quality, and efficiency throughout the procurement.(29) VFM has become a part of a holistic procurement structure with three support pillars: efficiency, quality, and flexibility.(30) The two key procurement principles of transparency and fairness weave across all elements of the structure.(31)

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(22) P. McCawley, *Banking on the Future of Asia and the Pacific: 50 years of the Asian Development Bank*, *op. cit.*, pp. 3 and ff., esp. p. 303.

(23) *Ibid.*, p. 18.

(24) *Ibid.*, pp. 3 and ff., esp. pp. 326-327.

(25) *Ibid.*, pp. 3 and ff., esp. p. 330.

(26) Asian Development Bank, *ADB Annual Report 2017*, p. 46.

(27) *Ibid.*, p. 33.

(28) T. NAKAO, “Remarks at ADB's 50th Anniversary”, 14 December 2016.

(29) Asian Development Bank, *Guide Notes on Procurement*, *op. cit.*, p. 3.

(30) *Ibid.*

(31) *Ibid.*

#### 4.1. Quality-based procurement principles

Article 14 of the ADB Charter states the operating principles of ADB, which for years have also been referred to as ADB's procurement principles, to wit: 1) Source of Procurement (*i.e.*, the proceeds of a loan can be used only for procurement of goods and works supplied from, and produced in member countries of ADB; 2), Economy and Efficiency, *i.e.*, contracts are to be procured through international competition unless other forms of procurement are more suitable and have been agreed upon between ADB and the borrower; 3) Fairness, *i.e.*, procurement procedures must give member countries adequate, fair, and equal opportunity to compete for contracts; and 4) Transparency, *i.e.*, as an essential principle to achieve economy and efficiency and to combat fraud and corruption.(32)

Without abandoning its fiduciary duty to ensure that the proceeds of any loan made, guaranteed, or participated in by ADB are used only for the purposes for which the loan is granted,(33) the new procurement policy expands the core procurement principles by adding two additional principles – quality and value for money.

##### 4.1.1. Quality

For the first time, ADB defines quality as a core procurement principle in its 2017 procurement policy.(34) ADB provides for definitions of quality for individual procurements.(35) For the standard of goods, quality is defined through technical specifications and standards and the product characteristics and tolerances.(36) For routine construction services, quality is defined through technical specifications for the defined inputs, and through industry standards applied to construction methods.(37) For large infrastructure projects, or where the use of high-level technology is proposed, quality is defined through the functional objectives achieved, serviceability, durability, and functionality, and through social, economic

(32) See also, par. 1.2, General Conditions of ADB Procurement Guidelines, April 2015. The 2015 Procurement Guidelines extended these principles into five basic procurements by including as one of its principles the interest of ADB in encouraging the development of domestic contracting and manufacturing industries in the country of the borrower.

(33) Par. (ix) and (xi), Art. 14 of the ADB Charter specify that ADB financing shall be used only for procurements in member countries of goods and services produced in member countries, except by Board waiver, and that ADB will ensure its finances are used only for the purposes for which the loan was granted and with due attention to considerations of economy and efficiency. See also Asian Development Bank, "ADB Procurement Governance Review", January 2013.

(34) Asian Development Bank, "Quality, Guidance Note on Procurement", June 2018, p. 4.

(35) *Ibid.*, pp. 40 and ff., 6.

(36) *Ibid.*

(37) *Ibid.*

and environmental impacts.(38) ADB emphasizes quality in the key stages of its procurement cycle(39) (*i.e.*, procurement planning,(40) development of specifications,(41) bid evaluation and contract award,(42) including contract management(43)).

The Guidance Notes on Quality list the potential issues that may arise at each stage of procurement, with suggested mitigation measures. There is also a quality checklist found in the appendix to provide the procurement practitioners with a list of items to consider at each key stage of the procurement cycle to ensure that quality is being incorporated in the decisions about the procurement process.(44)

Although quality is already recognized as a part of the value for money (VFM) equation(45) (*i.e.*, quality increases VFM),(46) ADB emphasizes that improving the quality of procurement decision-making and support will increase efficiency, reduce procurement time and help in the reduction of risk,(47) although this may be insufficient for more complicated goods, works and services which call for a complex trade-off between quality and costs.(48) Quality requires that the procurement arrangements be structured to procure inputs and deliver outputs of appropriate standard in a timely and effective manner and achieve the project outcomes and development objectives, taking into account the context, risk, value and complexity of the procurement.(49) ADB notes that the assessment of qualitative factors is open to the risk of possible abuse of discretion, as well as conscious and unconscious bias in decision-making.(50)

#### 4.1.2. Value for Money (VFM) as a core procurement principle

Value for money (VFM) is not really a new procurement principle in a multi-lateral development bank (MDB) or in Asia. VFM is an already expressed procurement principle of the other MDBs such as the World Bank,(51) and

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(38) *Ibid.*

(39) *Ibid.*

(40) *Ibid.*, pp. 40 and ff., esp. 8.

(41) *Ibid.*, pp. 40 and ff., esp. 13.

(42) *Ibid.*, pp. 40 and ff., esp. 19.

(43) *Ibid.*, pp. 40 and ff., esp. 26.

(44) *Ibid.*, pp. 40 and ff., esp. 29.

(45) *Ibid.*, pp. 40 and ff., esp. 1.

(46) *Ibid.*, pp. 40 and ff., esp. ix.

(47) *Ibid.*, pp. 40 and ff., esp. 54.

(48) *Ibid.*, pp. 40 and ff., esp. 3.

(49) *Ibid.*, pp. 40 and ff., esp. 4.

(50) *Ibid.*, pp. 40 and ff., esp. 55.

(51) World Bank, Value for Money: Achieving VfM in Investment Projects Financed by the World Bank, July 2016.

the African Development Bank.(52) Even in Asia, VFM had already been endorsed by the Asia Pacific Economic Cooperation (APEC) as early as 1998 to be one of the two non-binding principles in government procurement (*i.e.*, the other principle is open and effective competition).(53) Nonetheless, it was only in 2017 when ADB “for the first time” defined VFM as a core principle in its procurement policy,(54) thereby introducing “life cycle costing” (*i.e.*, taking into account not only the acquisition cost, but also a combination of paid price plus the cost of operating and maintaining the goods or services procured)(55) and the requirement for evaluation of benefits along with assessment of risks, non-price attributes and/or total cost of ownership (*i.e.*, acquisition costs, operating costs, maintenance costs and disposal costs).(56)

By incorporating VFM in its core procurement principles, ADB hopes to address concerns regarding the effort to obtain quality results. ADB seeks to prevent a contract decision based solely on efficiency or economy that may result in a contract being awarded to the lowest-priced bid regardless of other relevant factors, such as reliability, performance and maintenance, including externalities such as environmental and social impacts.(57) To achieve VFM, it is recommended that evaluation criteria must consider factors such as cost, quality, risk, sustainability and innovation. Non-priced criteria (*i.e.* quality of methodology and work plan, performance capacity or functionality features, and sustainable procurement) may be assessed based upon a scoring system using weighted criteria.(58) VFM is now considered as a factor in effectively managing a contract that can be best achieved through specific, measurable, relevant and time-bound (SMART) key performance indicators (KPIs) which are directly linked to the project objectives and deliverables.(59)

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(52) V. SHARMA, “An update on procurement reforms at the African Development Bank”, *PPLR*, 2016, No. 4, pp. 151-163, (“in a time of limited fiscal space, local governments are now more serious about achieving Value for Money (VfM) in procurement. Exclusive focus on ‘lowest price’ is no longer seen as adequate when spending public monies – considerations such as life-cycle costing sustainability, and environmentally and socially responsible procurement (ESRP) are bringing new variables into bid evaluation”).

(53) S. BROWN, “APEC developments – non-binding principles of value for money and open and effective competition”, *PPLR*, 1999, 1, CS16-19 (“Government procurement practices and procedures should be ‘directed to achieving the best available value for money in the acquisition of goods and services to deliver, or support delivery of, government programmes’. Purchase price alone does not provide complete information with respect to ‘total relevant costs’. The test agreed by Members involves a comparison of costs and benefits on a whole life basis. Benefits in terms of taxpayer and supplier savings may also be realised through improvement in procurement processes and management”).

(54) Asian Development Bank, “Value for Money, Guidance Note on Procurement”, ADB, June 2018.

(55) *Ibid.*, pp. 60 and ff., ix.

(56) *Ibid.*, pp. 60 and ff., 21.

(57) *Ibid.*, pp. 60 and ff., 3.

(58) *Ibid.*, pp. 60 and ff., 15.

(59) *Ibid.*, pp. 60 and ff., 18-19.

In case, however, of potential conflicts with other core procurement principles (*i.e.*, quality, efficiency, economy, transparency, fairness), ADB provides a list of mitigation measures such as the inclusion of VFM in transparency, identification of potential risks, a mechanism to address conflicts, and a valid complaints mechanism.(60)

#### 4.2. Procurement risk framework

Addressing the risk attached to public procurement is not a novel procurement policy.(61) In fact ADB had already introduced a risk-based procurement approach in 2013 but only for the purpose of streamlining its procurement processes to increase efficiency.(62) Accordingly, ADB implemented a 10-point procurement action plan(63) in 2014 that aimed to (i) improve ADB's business processes, (ii) increase ADB responsiveness and engagement, and (iii) more effectively respond to evolving changes of global procurement practices.(64) Despite the encouraging results of these actions,(65) ADB's procurement procedures were still perceived as cumbersome, inflexible, and not conducive

(60) Appendix 3: Interplay among the Core Procurement Principles, Asian Development Bank, "Value for Money, Guidance Note on Procurement", *op. cit.*, pp. 60 and ff., 30-33.

(61) See also the 2015 OECD Recommendations, which include risk management as one of the 12 principles for public procurement, *i.e.*, transparency, integrity, access, balance, participation, efficiency, e-procurement, capacity, evaluation, risk management, accountability and integration. These principles reflect the critical role that governance of public procurement must play in achieving and advancing public policy objectives.

(62) Asian Development Bank, "Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific", April 2014, p. 10. See also Asian Development Bank, "The Strategic Importance of Public Procurement", *ADB Brief*, 23 November 2011.

(63) Asian Development Bank, "Midterm Review of Strategy 2020: Meeting the Challenges of a Transforming Asia and Pacific", *op. cit.*, pp. 60 and ff., esp. p. 69. "On 25 February 2014, ADB approved the 10 Point Action Plan on Procurement Reform... which includes the following actions: (i) undertake new procurement assessments under an enhanced procurement risk assessment methodology; (ii) approve new procurement thresholds for international competitive bidding and national competitive bidding; (iii) introduce new prior-review thresholds and procurement supervision approach, including post-review based on sampling; (iv) increase ADB's Procurement Committee approval threshold to \$40 million and implement new decision authorities; (v) classify projects by procurement risk and complexity during project concept clearance; (vi) fully roll out the procurement review system; (vii) agree on master bid documents during project preparation; (viii) streamline the Procurement Committee process; (ix) implement a single standard procurement approval form for all levels of procurement; and (x) undertake a thorough review of consultant selection, approval, and contract variation processes."

(64) Asian Development Bank, "Improving ADB Project Performance through Procurement Reforms", March 2017.

(65) *Ibid.*, pp. 1-2, "An increase in the value of the contracts awarded in ADB projects by almost 40% from \$6.8 billion in 2013 to \$9.5 billion in 2016 was recorded and attributed to the implementations of the 10 point agenda, specially, the reforms due to the introduction fo project procurement risk based classifications based on value and complexity, *i.e.*, of 220 projects in 2015, 25% or 55 were classified as category A or "higher risk, thus requiring close support and oversight by procurement specialist; completion of 10 country-based procurement risk assessment, including sector-specific assessment; introduction of post-review on lower-risk procurement transactions, and creation of regional procurement committee. Project procurement risk-based classifications resulted to an increase in the value of the contracts awarded in ADB projects by almost 40% from \$6.8 billion in 2013 to \$9.5 billion in 2016".

to timely or high-quality results;(66) hence, the need for a new procurement framework that will not only increase efficiency and reduce procurement time, but will also reduce risk, and deliver value for money.(67)

ADB's new procurement risk framework hopes to manage risk throughout the procurement cycle from the country partnership strategy to contract closeout.(68) It introduces four risk management tools – the country and sector/agency procurement risk assessment, procurement risk categorization, project procurement risk assessment, and a contract management plan – that the country, sector, agency and project can use in identifying, assessing and managing the risks within their respective levels,(69) whilst allocating responsibilities for risk management in the procurement cycle between ADB and the borrower.(70) ADB is not only responsible for risk management during country partnership strategy and project conceptualization, but also accountable for risk management during procurement planning.(71) The borrower is only consulted during the first two stages in the procurement cycle (*i.e.* country partnership strategy and project conceptualization), and its responsibility for risk management begins during procurement planning, project implementation and contract management. It is worth noting that ADB's overt actions on risk management diminish during project implementation and contract management, as it has become the primary responsibility of the borrower subject only to consultation with ADB.(72)

Risk management includes risk assessment and treatment. Procurement risks are estimated according to their likelihood to occur (*i.e.* rare to almost certain), their consequences (*i.e.*, insignificant to severe), and rated (*i.e.*, likely to high) for the purpose of prioritizing for possible treatment (*i.e.*, risks rated 'extreme' and 'high' should be given special attention, but treatments to mitigate 'medium; and 'low' risk should also be considered).(73) ADB likewise suggests four possible risk treatment options – 1) Avoid (not proceeding with the project activity); 2) Reduce (reduce the likelihood and consequence of the occurrence, e.g., procurement approach, contract management, etc.); 3) Transfer (transfer the risk to another party, e.g., insurance); and 4) Accept (accept the risk without mitigation, e.g., low risk).(74)

(66) Asian Development Bank, "Improving ADB Project Performance through Procurement Reforms", *op. cit.*, p. 72.

(67) Asian Development Bank, "Procurement Risk Framework, Guidance Note on Procurement", June 2018, p. xi.

(68) *Ibid.*, pp. 74 and ff., 1.

(69) *Ibid.*, pp. 74 and ff., 7.

(70) *Ibid.*, pp. 74 and ff., 9.

(71) *Ibid.*

(72) *Ibid.*, p. 78.

(73) *Ibid.*, pp. 74 and ff., 12.

(74) *Ibid.*, pp. 74 and ff., 13.

Since all projects are prone to risk and uncertainty,(75) ADB's new procurement risk framework emphasizes the need to treat and manage risks after identification by highlighting risk management as an ongoing activity.(76)

### 4.3. New practices

In addition to the two core principles, ADB introduced contract management and abnormally low bids as among the new public procurement practices.

#### 4.3.1. Contract management

ADB highlights the three stages in contract management: a) preparation and planning activities prior to contract award, b) contract administration during contract implementation, and c) contract closure.(77) Aside from preparing a contract management plan (CMP) acceptable to ADB prior to contract signing, borrowers should monitor the performance and progress of contracts under the CMP and provide timely reports to ADB. Reporting to ADB should be regarded as an ongoing activity throughout contract implementation. For contracts subject to post review, the borrower shall seek ADB's no-objection for any significant variation.(78)

The Guidance Notes on Contract Management summarize the borrower's responsibility in contract management as follows: 1) planning contract management during the pre-contract award stage and incorporating contract management requirements into the draft contract; 2) developing a CMP prior to contract award, 3) submitting a completed CMP to ADB prior to contract signing, 4) implementing the CMP to ensure that contract performance is satisfactory, appropriate stakeholders are informed, and all contract requirements are met; 5) submitting quarterly performance reports to ADB during contract implementation, 6) requesting ADB's no objection where any modification would individually or in aggregate increase the original contract price by over 15% (for contracts subject to post review), and 7) preparing and submitting post contract closure performance report.(79)

#### 4.3.2. Abnormally low bids

ADB addressed for the first time the issue of abnormally low bids (ALBs). Under the new procurement regulations, it is possible to reject a bid, require an

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(75) *Ibid.*, pp. 74 and ff., 6-7.

(76) *Ibid.*, pp. 74 and ff., 16-17.

(77) Asian Development Bank, "Contract Management, Guidance Note on Procurement", June 2018, p. ix.

(78) *Ibid.*, pp. 84 and ff., 17.

(79) *Ibid.*, p. 85.

increase in the amount of the performance security as a condition to award the contract (the amount of the performance security shall generally not exceed 20% of the contract price), or accept the bid as such,(80) subject to the proper procedural determination of an ALB. The ALBs Assessment Process adopts three broad steps in dealing with ALBs, to wit: 1) Identify, 2) Clarify and Analyze, and 3) Decide.

To identify ALBs, it necessary to revalidate the engineer's cost estimates and compare those with the bid price, compare the bid price with the other responsive bids received and compare the bid price with prices paid in similar contracts.(81) Thereafter, check for omissions, errors and underpricing, seek explanations for resources, inputs and pricing, review scope and compliance, check for redundancy, contingency, and profit margins, check the rate or price quoted by the bidder for similar nature of works in other projects, either government, or development partner-funded (clarify and analyze).(82) Finally a decision is to be made on whether to accept or reject, based on the evidence presented, and then a report is made on the outcome of the ALB process.(83)

It is worth noting that there is no automatic exclusion due to a bid falling above or below a predetermined assessment of bid values,(84) as there may be good reasons for a low bid price (*i.e.* the economy of the manufacturing process, the services provided, or the construction method, the technical solutions chosen or any exceptionally favorable conditions available to the bidder for the supply of the products or services or for the execution of the work, the originality of the bidder's works, supplies, or services proposed, change in underlying input prices, e.g. commodities, economies of scale, effective supply chain management, or as a loss leader to establish a market presence, and the bidder may intend to quote only at cost (without profit margin) to establish its business in a country or sector to gain experience to compete for future bidding).(85)

An ALB is not in and of itself negative.(86) Dealing with ALBs may even increase efficiency and reduce implementation time (*i.e.*, improve contract implementation by identifying potential costing issues up front, reduce time delays during contract implementation, avoid possible project failure), ensure quality (help to identify unfit or unreliable bidders, and ensure that reliable, competent bidders are selected), reduce risk, (*i.e.*, 'de-risk' projects in which the

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(80) Asian Development Bank, "Abnormally Low Bids, Guidance Note on Procurement", June 2018, p. ix.

(81) *Ibid.*, pp. 87 and ff., 12.

(82) *Ibid.*, pp. 88.

(83) *Ibid.*

(84) *Ibid.*, pp. 87 and ff., 2.

(85) *Ibid.*, pp. 88 and ff., 3.

(86) *Ibid.*, p. 92.

bidder does not sufficiently account for the financial implications of employment regulations, health, safety, security and environmental requirements, environmental obligations and/or technical requirements), and improve value for money (identify unrealistic or inaccurate borrower project cost estimates).(87) Nonetheless, an ALB requires additional investigation, as it could be a sign of risks such as (i) a lack of technical or commercial competence, (ii) an intent to not follow design standards or specifications, and/or (iii) an intent to not comply with environmental or labor laws.(88)

#### 4.4. Specialized areas

ADB addresses specialized areas in procurement by issuing separate guidance notes on procurement during fragile, conflict-affected and emergency situations, e-procurement, procurement for public-private partnership, and procurement of high-level technology.

##### 4.4.1. Fragile, conflict-affected and emergency situations

Recognizing the enormous challenges in operating in fragile and conflict-affected situations (FCAS) and in emergency situations, ADB offers simplified and flexible procurement measures in addressing FCAS according to country conditions.(89) While ADB distinguishes fragility from conflict, including post-conflict, ADB generally characterizes FCAS as countries with political instability, weak governance and institutional capacity, economic and social insecurity, high levels of poverty, wide gaps in the level of social and economic services, lack of competition, disputes over access to resources and the sharing of their profits, and greater vulnerability to the effects of natural hazards and climate change.(90) Emergency situations include disasters, which refer to sudden, calamitous events that seriously disrupts the function of the community and society causing widespread human, material, economic or environmental losses that exceed the community's or society's ability to cope using its own resources.(91) An emergency occurs after a natural or manmade disaster, or conflict, when unforeseen circumstances require immediate action and the local capacity is insufficient to address and manage traumatic events.(92)

ADB enlists flexibility measures in procurement depending on operational situations (*i.e.*, FCAS or emergency situations), but provides common

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(87) *Ibid.*, p. 87.

(88) *Ibid.*, p. 92.

(89) Asian Development Bank, *Fragile, Conflict-Affected, and Emergency Situations, Guidance Note on Procurement*, June 2018.

(90) *Ibid.*, pp. 96 and ff, 4.

(91) *Ibid.*, p. 97.

(92) *Ibid.*

procurement flexibilities to either situation. These include special procurement arrangements, *i.e.*, simplified procurement such as community participation and the use of the borrower's national procurement procedures acceptable to ADB, allowance for split packaging, *i.e.*, broadening the pool of qualified local contractors and suppliers, the use of framework agreements, the use of procurement agents, including contract management support (*i.e.*, especially when large-volume procurement is involved), lower bidder qualifications, waiver of performance securities (*i.e.*, for goods and small works), increase in advance payment, and use of alternative forms of contracting (*i.e.*, use of lump-sum and output-based contracts).<sup>(93)</sup>

As of 2017, ADB listed 11 FCAS countries, *i.e.* Federated States of Micronesia, Kiribati, the Marshall Islands, Nauru, Papua New Guinea, Solomon Islands, Timor-Leste, Tuvalu and Vanuatu, and two conflict-affected countries, *i.e.*, Afghanistan and Myanmar.<sup>(94)</sup>

#### 4.4.2. E-procurement

Like most multilateral development banks (MDBs), ADB encourages the use of electronic procurement (e-procurement) in different stages of the procurement process. In fact, in harmonization with other MDBs, ADB adopted the latest version of the modules published by the World Bank Group on e-bidding or e-tendering in borrower-led e-procurement, *i.e.* E-tendering Requirements for MDB Financed Procurement, an electronic reverse auction (e-RA) module in e-procurement, and other modules such as catalog management or e-marketplace.<sup>(95)</sup> As a result, a prior clearance from ADB is required before using an e-procurement system in ADB-financed projects.<sup>(96)</sup>

ADB borrowers are required to use ADB's Consultant Management System (CMS) to advertise all consulting opportunities listed for competitive selection under the procurement plans for projects financed in whole or in part by an ADB loan or grant, or by ADB-administered funds. For goods, works and non-consulting services, borrowers are encouraged to use e-procurement for all procurement methods (e.g. open competitive bidding with international or national advertisement, limited competitive bidding, request for quotations). At a minimum, borrowers are required to publish an advance procurement notice and procurement plan on the ADB Web site, as well as advertise all their

<sup>(93)</sup> *Ibid.*, "Appendix: Flexibility Measures Available in Fragile, Conflict-Affected and Emergency Situations", pp. 96 and ff., 19-21.

<sup>(94)</sup> Asian Development Bank, "Abnormally Low Bids, Guidance Note on Procurement", *op. cit.*, p. 92.

<sup>(95)</sup> Asian Development Bank, "E-procurement, Guidance Note on Procurement", 2018, pp. 6-7.

<sup>(96)</sup> *Ibid.*, pp. 102 and ff., 7.

open competitive bidding procurement contracts with an international advertisement on this site.

Except in the case where the use of e-procurement is limited to advertising opportunities and publishing contract awards, ADB requires prior accreditation of an e-procurement system. Only an e-procurement system that is previously accredited by ADB or another MDB may be used in its projects.(97) Nonetheless, non-accredited systems will be reassessed, and remedial measures will be recommended to address their non-compliance.(98) Only after these issues are addressed and agreed upon by ADB and the borrowing country will ADB authorize the use of an e-procurement system.(99)

ADB emphasizes that an effective implementation of e-procurement increases efficiency and reduces procurement time (e.g., automated and electronic system reduces the processing and communication times in procurement for both buyers and bidders), reduces risk (e.g. automated processes reduce the risk of mistakes that could compromise the procurement), improves transparency and fairness (e.g. supports the timely online publication and disclosure of information pertaining to procurement plans, opportunities, processes, and results); and delivers VFM (e.g. a cross-government e-procurement system minimizes duplication of process, etc.,).(100)

#### 4.4.3. Public-private partnerships

The Guidance Note on Procurement for Public-Private Partnerships discusses only the selection of PPP operators for ADB's sovereign lending operations and does not apply to other operations of ADB, such as but not limited to non-sovereign operations, downstream procurement of goods, works and services by the private operator, etc.(101) Interestingly, the key considerations in PPP procurement find support from other PPP resources such as the ADB *Public-Private Partnership Handbook*(102) and the World Bank *Public Private Partnership Reference Guide*.(103) Accordingly, procurement for PPP may be through either (i) unsolicited proposals or direct negotiations ("sole sourcing"), (ii) competitive negotiations, or (iii) competitive bidding.(104)

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(97) *Ibid.*

(98) *Ibid.*

(99) *Ibid.*

(100) *Ibid.*, pp. 102 and ff., ix-x.

(101) Asian Development Bank, "Public-Private Partnership, Guidance Note on Procurement", June 2018.

(102) Asian Development Bank, "Public – Private Partnership Handbook", 2008.

(103) World Bank Group, "Public-Private Partnerships Reference Guide", V. 3, 2007.

(104) Asian Development Bank, "Public-Private Partnership, Guidance Note on Procurement", *op. cit.*, citing "Public – Private Partnership Handbook", 2008, *op. cit.*, pp. 108 and ff., 6.

#### 4.4.4. High-level technology

ADB launched the High-Level Technology Fund(105) to promote the adoption of high-level technology (HLT) and innovative solutions(106) by its developing members. Accordingly, projects that have any of the following characteristics may be considered HLT and innovative for purpose of securing ADB's HLT Fund: (i) improves efficiency, productivity, quality, functionality, and/or access to service delivery; (ii) addresses climate change mitigation and/or adaptation, including resilience to disaster risks; (iii) introduces innovation in processes, methods, techniques, and the use of new or improved equipment and materials in construction, operations, and maintenance; (iv) reduces environmental and social costs; (v) reduces total cost of ownership, increases durability, and improves long-term performance; (vi) enhances the scaling up of HLT and market opportunities for scale-up; and (vii) promotes synergies and increases scale and impact through cross-sector collaboration.(107)

HLT can be incorporated into ADB operations in several ways: a) an acquisition of equipment and goods that employ HLT that is new globally, in ADB operations, or to an ADB DMC; b) construction or civil works based on specifications that require contractors to meet enhanced performance standards and/or employ HLT in the construction process, materials, and other inputs; and c) consulting services that require specific knowledge and expertise in the use of HLT in different phases of the innovation cycle, as well as different sectors and applications.(108)

#### 4.5. Strategic procurement planning

ADB's principle-based procurement approach paves the way for the adoption of the process of strategic procurement planning (SPP).(109) Unlike the previous compliance-based procurement planning approach, SPP begins during the project conceptualization stage and continues as a main activity within the procurement planning stage.(110)

The ADB Guidance Note on Strategic Procurement Planning lists some of the tools and techniques that the borrower may use in developing procurement strategy and procurement plans, e.g., strengths – weaknesses – opportunities

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(105) Asian Development Bank, "Public-Private Partnership, Guidance Note on Procurement", *op. cit.*, pp. 108 and ff., 1.

(106) Asian Development Bank, "High-Level Technology, Guidance Note on Procurement", June 2018.

(107) *Ibid.*, pp. 113 and ff., 1-2.

(108) *Ibid.*, pp. 113 and ff., 114 and ff., ix.

(109) Asian Development Bank, "Strategic Procurement Planning, Guidance Note on Procurement", 1, 2018.

(110) *Ibid.*, p. 116.

– threats analysis to determine the capacity and capability of the borrowing country,(111) external influences analysis to identify any external drivers of change to the project,(112) and stakeholder analysis to identify and position all the internal and external stakeholders who may be involved in a project during the planning and implementation of a project.(113) SPP likewise encourages the borrower to conduct a robust market analysis through the use of strategic analytical tools such as Porter’s five forces analysis, supply positioning, and supplier preferencing.(114) Risk management through project procurement risk assessment and a risk register is an important part of the SPP process as it will help in identifying and mitigating the potential risk to the project and its procurement contracts.(115) Options Analysis is used in evaluating the available options to fulfill the project’s development objectives,(116) which helps in the formulation of the procurement strategy in the SPP document.(117) The final step of the SPP is the synthesis of the analysis, preferred options, and strategy into the project procurement plan.(118)

Another important process in strategic procurement planning is the conduct of a procurement review and the possibility of adopting alternative procurement arrangements in the conduct of public procurement.

#### 4.5.1. Procurement review

In line with its fiduciary duty, ADB conducts procurement reviews in one of two ways: (1) prior review, in which ADB reviews and approves key documents and decisions prior to them being implemented, and (2) post review (sampling), in which ADB reviews documents, decisions, and procurement processes, on a sample basis, after contract signing.(119) Prior review is conducted on contracts that are categorized as high risks and requires a ‘no-objection’ from ADB to each step in the procurement process to confirm that the borrower’s proposed actions comply with ADB’s 2017 procurement policy and regulations, the project’s financing agreement, procurement plan, and other relevant documents.(120)

Procurement post review (sampling) may be conducted at each reimbursement cycle, where series of withdrawal applications are received, or as part of

(111) *Ibid.*, pp. 116 and ff., 6.

(112) *Ibid.*, pp. 116 and ff., 7.

(113) *Ibid.*, p. 119.

(114) *Ibid.*, pp. 117 and ff., 11.

(115) *Ibid.*, 24-26.

(116) *Ibid.*, 27-33.

(117) *Ibid.*, 34.

(118) *Ibid.*, 35.

(119) Asian Development Bank, “Procurement Review, Guidance Note on Procurement”, June 2018.

(120) *Ibid.*, pp. 126 and ff., 3.

project review missions by ADB or its consultants.(121) Under the post review (sampling), the borrower approves the award and signs the contracts, while ADB will post review only a sample of contracts awarded and signed.(122) The sample size should endeavor to capture contracts representing (i) about 30-50% of total project value and (ii) about 20% of the total number of contracts identified for post review (sampling).(123) Post review likewise helps ADB in checking possible integrity violations, *i.e.*, checking the list of contracts against ADB's list of suspended and debarred firms and individuals, including any entities debarred or suspended under MDB's Agreement for Mutual Performance and Debarment Decisions (2006).(124) Each borrower is rated on its management of the procurement process concerning compliance with the agreed procurement procedures, which shall be evaluated as 'satisfactory', 'partly satisfactory', or 'unsatisfactory', assessed for its overall risk rating, *i.e.*, high, medium or low, and thereafter, the findings are discussed with the borrower for an opportunity to clarify any issues and to provide the necessarily mitigating and strengthening measures.(125)

#### 4.5.2. Alternative procurement arrangements

ADB addressed for the first time the usage of alternative procurement arrangements (APAs) in its mainstream procurement operations,(126) either through the use of an APA under another multilateral or bilateral agencies' procurement rules and procedures involved in the project (e.g. other MDBs or specialized United Nations agencies), or with an agency or entity of the borrower accredited by the ADB.(127) In doing so, co-financing agreements must be executed between ADB and its partners, e.g., other donors. In any case, partners are required, among other things, to protect the privileges and immunities of ADB(128) and to comply with the universal requirements under ADB's Article of Agreement (e.g., member country eligibility requirements, adherence to the provisions for United Nations sanctions and MDB agreed cross debarments etc.)(129) Effective application of alternative procurement arrangements may increase efficiency and reduce procurement time, ensure quality and manage risk, and deliver value for money.(130)

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(121) *Ibid.*, 6.

(122) *Ibid.*, p. 129.

(123) *Ibid.*, p. 128.

(124) *Ibid.*, p. 126 and ff., 11.

(125) *Ibid.*, p. 126 and ff., 11-12.

(126) Asian Development Bank, "Alternative Procurement Arrangements, Guidance Note on Procurement", June 2018.

(127) *Ibid.*, pp. 133 and ff., 3.

(128) *Ibid.*, pp. 134.

(129) *Ibid.*, pp. 133 and ff., 4.

(130) *Ibid.*, pp. 133 and ff., ix.

#### 4.6. Procurement methods

Open competitive bidding (OCB) is still the preferred procurement method for ADB-funded projects.(131) OCB consolidates the competitive procurement of goods, works, and services under a single procurement method.(132) Unlike the previous guidelines (Procurement Guidelines 2015, as amended from time to time), the new guidelines require the evaluation of past performance either through the submission by the bidders of evidence of their previous contracts or through third-party inquiry. In either event, bidders are given opportunities to respond to any adverse information.(133)

OCB encompasses competitive recruitment methods for consulting services and removes conceptual boundaries (for example, the understanding that merit point scoring should not be used in the procurement of goods or civil works) that previously limited the flexibility needed to achieve successful procurement and development outcomes.(134)

Moreover, the ADB 2017 procurement regulations empowered a bidder to raise “any issue of ambiguity, contradiction, omission, etc., prior to the submission of its bid to assure submission of a fully responsive and compliant bid that includes all the supporting documents requested in the bidding documents,”(135) including the right to write directly to ADB if the bidder is not satisfied with the explanation of the borrower (*i.e.*, in debriefing, the unsatisfied bidder can write ADB).(136)

##### 4.6.1. Consulting services and non-consulting administered by ADB borrowers

Prior to the 2017 ADB procurement regulations, ADB did not differentiate between customized intellectual and advisory services that are generally considered to be consulting services and standardized services that are generally considered to be non-consulting service.(137) Now, ADB introduces non-consulting services as a separate category of services, which comprise both physical and intellectual activities that are routine and measurable in nature (e.g., installation and maintenance services, household surveys, standard

(131) Asian Development Bank, Open Competitive Bidding, Guidance Note on Procurement, June 2018.

(132) *Ibid.*

(133) Asian Development Bank, Appendix 3, “Open Competitive Bidding, Guidance Note on Procurement”, *op. cit.*, pp. 138 and ff., 25.

(134) *Ibid.*, 3.

(135) *Ibid.*, 18.

(136) *Ibid.*, 20.

(137) *Cf.* Asian Development Bank, “Non-Consulting Services Administered by ADB Borrowers, Guidance Note on Procurement”, 1, June 2018.

audits, Web site maintenance, event management, interisland shipping, and vocational training).(138)

Consulting and non-consulting services can sometimes be difficult to distinguish, as both can include professional services.(139) Non-consulting services include (i) services for which the physical aspects of the activity predominate, that are bid and contracted on the basis of performance of a measurable physical output, and for which industry and performance standards can be clearly identified and consistently applied; or (ii) routine services which, while requiring expert inputs, are based on recognized standard offerings that are readily available and which do not require evaluation of tailored methodologies or techniques.(140) Consulting services refer to services which are of an intellectual and advisory nature, *i.e.*, evaluation of technical proposals that offer tailored approaches, methodologies, and specially qualified experts, *e.g.*, policy and governance studies; advice on institutional reforms; engineering designs; construction supervision; legal advice; forensic audits; procurement services; social and environmental studies; and the identification, preparation, and implementation of projects.(141)

ADB discusses in detail the characteristic five procurement modalities for non-consulting services – open competitive bidding, limited competitive bidding, request for quotations, direct contracting or single-source selection and framework agreements.(142)

#### 4.6.2. Framework agreements for consulting services

While ADB allows an executing agency (*i.e.*, borrowers) to establish its own framework agreement or to draw from one established by ADB, its guidance note is particularly focused on explaining how framework agreements for consulting may, among others, be established and administered in accordance with best practice and applicable ADB policies.(143) ADB discusses in its new procurement guide notes the process under which single contracts or ‘call-offs’ from a framework agreement are made and administered.

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(138) *Ibid.*, p. 143.

(139) *Ibid.*, pp. 143 and ff., 3.

(140) *Ibid.*, p. 145.

(141) Asian Development Bank, “Consulting Services Administered by ADB Borrowers, Guidance Note on Procurement”, June 2018.

(142) Asian Development Bank, “Non-Consulting Services Administered by ADB Borrowers, Guidance Note on Procurement”, *op. cit.*, pp. 143 and ff., 19-20.

(143) Asian Development Bank, “Framework Agreements for Consulting Services, Guidance Note on Procurement”, June 2018.

#### 4.7. Bidding procedures

ADB introduces the following new features in the conduct of bidding procedures.

First, ADB has adopted two new features to its prequalification process. These include the ability to limit the number of qualified applicants that are invited to bid and the inclusion of historical contract nonperformance in the criteria for assessing the suitability of the applicant to work on the project before inviting it to submit the bid.(144)

Second, ADB provides for different price adjustment formulas depending on the sizes and components of the contracts.(145) Price adjustment formulas allow contractors to offer more realistic prices at the time of bidding, by estimating actual cost implications that will be encountered.(146) Price adjustment provisions include formulas designed to protect both the borrower and contractors from price fluctuations.(147)

Third, ADB allows the contractor to use subcontractors to perform its obligations under contracts for the supply of goods, works, or plant, to the extent permitted in the bidding document used,(148) subject to the requirements on the treatment of subcontractors. Accordingly, ADB distinguishes three types of subcontractor under projects financed in whole or in part by an ADB loan or grant, or by ADB-administered funds: (i) those nominated by the borrower that all bidders must use, (ii) those specialist subcontractors that bidders may propose to deliver highly specialized equipment or key contract activities, and (iii) those subcontractors that bidders may propose for other purposes. It highlights risks to quality and supply chain integrity that can occur through subcontracting and suggests ways for borrowers to mitigate those risks.(149)

Finally, ADB removed the distinction between international and national competitive bidding (*i.e.*, the 2017 ADB regulations consolidate these two into ‘open competitive bidding’) which resulted in the removal of the limitation on the use of domestic preference only when international competitive bidding was used (*i.e.* domestic preference is now applicable even when only national advertising is used).(150) Although the domestic preference schemes are very similar to the past provision under the 2015 Procurement Guidelines,

(144) Asian Development Bank, “Prequalification, Guidance Note on Procurement”, June 2018.

(145) Asian Development Bank, “Price Adjustment, Guidance Note on Procurement”, June 2018.

(146) *Ibid.*, p. 151.

(147) *Ibid.*

(148) Asian Development Bank, “Subcontracting, Guidance Note on Procurement”, 3, June 2018.

(149) *Ibid.*, p. 154.

(150) Asian Development Bank, “Domestic Preference, Guidance Note on Procurement”, June 2018.

the new schemes allow more flexibility (*i.e.*, the margins of preference are no longer fixed and may be adjusted within specified ceilings).(151) A new method for the procurement of consulting services is also introduced, that is, the “use of national experts for key positions” as an evaluation criterion in technical evaluation.(152) In the past, the only possibility available was to require certain positions to be ‘national’.(153)

#### 4.8. Complaints, compliance and eligibility

Procurement-related complaints with regard to a bidding process may be brought to the attention of the borrower or ADB, or both, at the appropriate stage of the procurement process. Such complaints must be addressed objectively and in a timely manner, with transparency and fairness.(154) To ensure an effective complaints handling mechanism, ADB, for the first time, addresses the submission and handling of bidding-related complaints in a comprehensive manner.(155)

Bidding-related complaints may arise during the procurement planning, bidding (including prequalification), bid evaluation, contract award, post-award, and implementation stages of the ADB procurement cycle.(156) They can arise prior to the submission of bids, after bid submission but prior to contract award, and/or after contract award.(157) Complaints can arise under three possible scenarios: 1) fraud, corruption and other prohibited practices complaints;(158) 2) complaints arising out of, or related to, a bidding process subject to an alternative procurement arrangement (APA) that may allege fraud, corruption, and/or some other bidding-process-related irregularity or omission; and 3) breach of ADB’s policy and/or regulations (*i.e.*, misapplication or omission in application of ADB’s 2017 procurement policy and/or procurement regulations during a bidding process financed in whole or in part by an ADB loan or grant, or by ADB-administered funds).(159)

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(151) *Ibid.*, p. 156.

(152) *Ibid.*

(153) *Ibid.*

(154) Asian Development Bank, “Procurement Regulations for ADB Borrowers, Goods, Works, Nonconsulting and Consulting Services”, 8, 2017.

(155) Asian Development Bank, “Bidding-Related Complaints, Guidance Note on Procurement”, June 2018.

(156) *Ibid.*, pp. 161 and ff., 1.

(157) *Ibid.*, p. 162.

(158) Any violation of the ADB’s Anticorruption Policy (1998, as amended to date) and Integrity Principles and Guidelines (2015, as amended from time to time).

(159) Asian Development Bank, “Bidding-Related Complaints, Guidance Note on Procurement”, *op. cit.*, pp. 161 and ff., 2-3. See also *id.*, “Anticorruption and Integrity”, 2010; and *id.*, “Integrity Principles and Guidelines”, 2015.

In cases where the borrower fails to follow the applicable provisions of the 2017 procurement regulations or the agreed procurement arrangements, ADB provides a more flexible and proportional approach to noncompliance in procurement.(160) Some of the typical situations of noncompliance by a borrower may include, among others (i) using a bidding document that has not been endorsed by ADB, (ii) implementing a bid evaluation recommendation that has not been endorsed or approved by ADB, (iii) responding to a bidding-related complaint in ways contrary to those recommended by ADB, (iv) omitting to undertake required steps under a procurement method prescribed in the project procurement plan, (v) providing ADB with an incomplete or misleading record of a procurement transaction, and (vi) failing to take appropriate action when a party awarded the contract has breached its contractual obligations.(161)

Interestingly, however, under the 2018 Guidance Note on bidding-related complaints, noncompliance in procurement and complaints under the alternative procurement arrangements (APAs) do not include complaints arising from integrity violations as those complaints arising thereto are covered by ADB's anticorruption policy and integrity principles and guidelines. Accordingly, integrity violations such as fraud, corruption, coercion, collusion, among others, must be promptly referred to ADB's Office of Anticorruption and Integrity (OAI)(162) in accordance with ADB's Anticorruption Policy (1998, as amended to date) and ADB's Integrity Principles and Guidelines (2015, as amended periodically).(163)

In the same manner complaints under the alternative procurement arrangements (APAs) are handled according to the applicable procurement regime. In APA situations, in the absence of actual or suspected integrity violations, bidding-related complaints are handled by either the lead co-financier, under the relevant mutual reliance agreement(s), or by the accredited agency of the borrower under the relevant project agreement and applicable local procurement rules and procedures.(164) Nonetheless, APA transactions are still covered by the ADB's anticorruption policy and integrity principles and guidelines. Therefore, ADB reserves the right to determine whether any of its policies and procedures have been violated, including independently

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(160) Asian Development Bank, "Non-Compliance Procurement, Guidance Note on Procurement", June 2018.

(161) *Ibid.*, pp. 167 and ff., 5.

(162) Asian Development Bank, "Bidding-Related Complaints, Guidance Note on Procurement", *op. cit.*, pp. 161 and ff., 3.

(163) Asian Development Bank, "Non-Compliance Procurement, Guidance Note on Procurement", *op. cit.*, pp. 167 and ff., 4.

(164) Asian Development Bank, "Bidding-Related Complaints, Guidance Note on Procurement", *op. cit.*, pp. 169.

investigating integrity violations under an APA procurement. In such circumstances, ADB's findings of noncompliance to its anticorruption policy may result in remedial action, including sanctions imposed by OAI. ADB may also exercise its right to withdraw, suspend, or terminate its own participation or financing under the relevant mutual reliance agreement and/or financing agreement.(165)

Complaints brought to the attention of the borrower or ADB must be submitted in writing and must be addressed objectively and in a timely manner, with transparency and fairness.(166) If received, ADB will promptly forward any submission or complaint relating to transactions subject to post review (sampling) to the concerned executing agency for review and resolution, provided that the said executing agency is not the responsible agency for any delay or expiration of any applicable period for the filing of the complaint, subject of review and resolution. If any such complaint received by ADB relates to allegations of integrity violations on the part of the executing agency and/or other parties, ADB will promptly forward such complaints to its Office of Anticorruption and Integrity for investigation and necessary action.(167)

Another novel practice that ADB introduced is the application of standstill periods in procurement in accordance with the national standstill provisions, or those of another development partner, to give unsuccessful bidders the opportunity to challenge a contract award decision.(168) ADB recommends a standstill period of not less than 10 working days following the notification of intent to award a contract, during which the bidders may challenge the award decision.(169)

Standstill periods take effect at the contract award stage of ADB's procurement cycle.(170) The purpose of a standstill period is to give unsuccessful bidders an opportunity to challenge an intended contract award decision before the actual notification of award. Although it delays the contract award for a period, it mitigates the risk of legal challenges that may delay a contract for far longer than the standstill period. It may improve levels of competition, as it will increase potential bidders' confidence that the procurement process will be transparent and fair.(171)

Standstill periods will not be applied under the following conditions: (i) for framework agreements, the mandatory standstill period applies at the stage

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(165) *Ibid.*, p. 161.

(166) *Ibid.*

(167) Asian Development Bank, "Bidding-Related Complaints, Guidance Note on Procurement", *op. cit.*, pp. 161 and ff., 16, Appendix 3.

(168) Asian Development Bank, "Standstill Period, Guidance Note on Procurement", June 2018.

(169) *Ibid.*, p. 175.

(170) *Ibid.*, pp. 175 and ff., 1.

(171) *Ibid.*, 2.

at which the agreement itself is awarded, but not during subsequent call-offs or mini-competitions within the agreement; (ii) in cases where only one bid or proposal was submitted in an open competitive bidding process; (iii) in cases of direct contracting, also referred to as single-source selection; (iv) in the first stage of a two-stage bidding process; (v) in the technical evaluation of a two-envelope bidding process; and (vi) for the results of prequalification.(172)

When a standstill period applies, ADB recommends that the bidding documents allow bidders 3 business days from their receipt of the notification of intent to award a contract to make a written request to the borrower for a debriefing, and the process for doing so will be described in the bidding documents. The borrower is required to debrief the bidder within 5 business days after receiving a debriefing request in writing. If the borrower fails to deliver a debriefing within this 5-day period, for reasons not within the control of the bidder requesting the debriefing, the standstill period shall be extended by 5 business days after the debriefing is delivered. All costs incurred for participating in a debriefing shall be borne by the bidder.(173)

If, after the standstill period concludes, a bidder wishes to ascertain the grounds on which its bid was not selected, the bidder may request an explanation from the borrower. If the bidder is not satisfied with the explanation provided by the borrower, or if the borrower fails to provide such debriefing, the bidder may forward the request directly to ADB. This should be done in writing to the director general of the Procurement, Portfolio and Financial Management Department, who will arrange a meeting at the appropriate level and with the relevant ADB staff as specified in Appendix 9 of the 2017 procurement regulations.(174)

#### 4.8.1. State-owned enterprises (SOEs)

ADB recognizes the continuing significance of state-owned enterprises (SOEs)(175) in its developing member country (DMC) economies in the context of procurement, but limits SOE participation in any bidding process financed in whole or in part by an ADB loan or grant, or by ADB-administered funds, to situations that do not compromise ADB's procurement principles.(176) More

(172) *Ibid.*, 4.

(173) *Ibid.*, 6.

(174) *Ibid.*, 7.

(175) Although there are different ways to define SOEs, the term 'SOE' (for purposes of the new procurement regulations) includes, but is not limited to, any entity recognized by the borrower's national law as an enterprise in which the State or government exercises direct or indirect (whole or partial) ownership or control. This term includes majority or minority owned, listed or unlisted, joint stock and/or limited liability companies, partnerships, unincorporated associations, and statutory corporations. Asian Development Bank, "State-Owned Enterprises, Guidance Note on Procurement", 3, June 2018.

(176) Asian Development Bank, "State-Owned Enterprises, Guidance Note on Procurement", *op. cit.*, p. 182.

particularly, ADB agrees to the participation of SOE bidders in the borrower's country only if the SOE (i) can operate as a commercial entity, (ii) is legally and financially autonomous, and (iii) is not a dependent agency of the borrower. (177) By meeting these conditions, ADB will be satisfied that robust competition is maintained through a "level-playing field" by (i) avoiding any conflict of interest between the borrower and an SOE bidder; and (ii) preventing any undue competitive advantage benefiting such SOE bidder, to ensure that the 2017 procurement policy, including the core procurement principle of fairness, and ADB policies and guidelines related to integrity and conflict of interest will be satisfied. (178) Nevertheless, integrity risks may still exist due to the participation of SOE bidder(s), and appropriate due diligence should be applied and maintained throughout the procurement process. (179)

While SOE eligibility conditions protect the integrity of the bidding process and help to avoid the risks of undue competitive advantage and broader potential or actual conflict situations, conflicts of interest in terms of potential or actual violation of ADB's Anticorruption Policy (1998, as amended to date) and ADB's Integrity Principles and Guidelines (2015, as amended periodically) is a separate and independent ground for challenging any SOE or borrower activities arising out of, or in connection with, a bidding process, contract award, and/or subsequent contract management until completion. (180)

### **5. Moving Forward: ADB Strategy 2030 Achieving a Prosperous, Inclusive, Resilient and Sustainable Asia and the Pacific**

Moving forward, ADB has recently approved its new long-term corporate strategy known as 'Strategy 2030' that sets ADB's broad vision and strategic response to the evolving needs of Asia and the Pacific. (181) Accordingly, ADB will continue to strive to be stronger, better and faster by, among others, pursuing dramatic modernization of its business processes including timely and value-for-money procurement and the greater use of country systems, and accelerating its digital transformation. (182) While ADB seeks to increase the use of country systems in its public sector operations, (183) ADB must also

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(177) *Ibid.*

(178) *Ibid.*, pp. 182 and ff., 6.

(179) *Ibid.*, p. 185.

(180) *Ibid.*, p. 182.

(181) "ADB Launches Strategy 2030 to Respond to Changing Needs of Asia and Pacific", 26 July 2016.

(182) Asian Development Bank, "Strategy 2030: Achieving a Prosperous, Inclusive, Resilient, and Sustainable Asia and the Pacific", 11 July 2018.

(183) *Ibid.*, p. 188.

focus on enhancing the access to independent administrative review bodies and courts in addressing procurement related complaints (*i.e.*, the procuring entities are still the most common fora for procurement related complaints).(184)

Under Strategy 2030, ADB commits to uphold environmental and social safeguards,(185) increase its consideration on other socio-economic dimensions (*i.e.*, in Asia, some governments focus exclusively on environmental issues),(186) while addressing one of the most common barriers for sustainable procurement in Asia (*i.e.*, the market for sustainable products and services in Asia has yet to mature, and availability continues to be an important barrier to be addressed).(187)

## 6. Conclusion

Although the focus of this chapter is on documenting significant changes in the new procurement policies and regulations of ADB, it is clear that there is more to be done not only in promoting innovation in public procurement but also, and more importantly, in building capacity among procurement professionals. Countries with high-income economies have already begun their professionalisation of public procurement, either by requiring specific trainings and/or professional qualifications for procurement specialists (e.g., college degree of twenty-four semester hours of study in the specified business/legal subjects for contracting officials in the United States)(188) or by advancing policy recommendations for the promotion of professionalisation in public procurement (e.g., European Commission Recommendation on Professionalisation of Public Procurement dated 3 October 2017(189)). Given the breadth of its procedural reforms outlined above, ADB must also do the same for procurement professionals. ADB should include a capacity-building component for procurement officials in all of its projects, more particularly, those projects that will adopt the new procurement regulations. ADB should also require prior training of contracting officials on the use of its new procurement regulations as part of its country risk-assessment initiatives. In the end, it is important to note that no matter how advanced the ADB's procurement regulations are, if the procurement professionals working for the borrowing/recipient countries

(184) World Bank Group, "Benchmarking in Public Procurement 2017: Assessing Public Procurement Regulatory Systems in 180 Economies", 39, International Bank for Reconstruction and Development / The World Bank, 2016.

(185) Asian Development Bank, "Strategy 2030: Achieving a Prosperous, Inclusive, Resilient, and Sustainable Asia and the Pacific", *op. cit.*, pp. 188 and ff., 18.

(186) UNEP, "Global Review Sustainable Public Procurement", 2017, p. 7.

(187) *Ibid.*, pp. 193 and ff., 45.

(188) G.M. RACCA and C.R. YUKINS, "The Promise and Perils of Innovation in Cross-Border Procurement", Introduction in this book.

(189) *Ibid.*

do not have the necessary skills and competencies to implement them in ADB funded projects in their countries, the same issues in procurement will continue to pose fiduciary and performance risks in ADB funded projects, whilst slowing the advance of a more sustainable Asia and the Pacific.

BRUYLANT

**CHAPTER 21**  
**Innovation in Public Procurements**  
**in the Egyptian PPP Legislation**  
**(With reference to PPP Legislation**  
**in Dubai and Kuwait)**

BY

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**1. Introduction**

Public Private Partnership (PPP) is a new challenge, albeit an opportunity for delivering public service in the Arab region in the 21<sup>st</sup> century.

The term *public service* often refers to services which are offered to the general public (or end users), or services for the public interest, and, may, likewise, refer to the ownership or a status of the entity providing the service. In the latter situation, public service fuses with the concept of the public sector which covers the State and its organs, the bodies governed by public law, and the undertakings controlled by public authorities.(2)

In PPP, the private sector assumes a direct responsibility in serving the public interest, as part of its contractual obligations *vis-à-vis* the public sector. The fundamental aspect of PPP policy frameworks in Arab countries is the use of performance based contracts in which the private sector provides public services within a given period payable by the public sector, or the end users, or both.(3) Over the past 25 years, more than 5,000 infrastructure projects in 121 low- and middle-income economies have been delivered through PPPs, representing investment commitments of \$1.5 trillion. PPPs

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(1) LL.B., LL.M., Ph.D. (Cairo); FCI Arb (UK) State Prize Laureate, Academic Legal Research, Egypt, 2011, Senior Consultant for the Legislation and Legal Opinion Commission, Kingdom of Bahrain and Member of the *Comité français de l'arbitrage*.

(2) For more elaboration, see M.A.M. ISMAIL, *Globalisation and New International Public Works Agreements in Developing Countries*, London, Routledge, 2016, ch. 4; C. BOVIS, *EC Public Procurement: Case Law and Regulation*, Oxford, OUP, 2006, p. 11; S. ARROWSMITH, *The Law of Public and Utilities Procurement*, London, Sweet & Maxwell, 2014, vol. 1.

(3) M.A.M. ISMAIL, "International Infrastructure Agreements and PPPs in Developing Countries: Substantive Principles, With Special Reference to Arab and Latin American Countries", *EPPPL*, Lex., 3/2011, p. 154; and *id.*, "Legal Globalization and PPPs in Egypt", *EPPPLR*, Lex., 1/2010, pp. 54-67.

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have supported the development of crucial infrastructure such as roads, bridges, light and heavy rails, airports, power plants, and energy and water distribution networks.(4) PPPs are long-term contractual agreements(5) for the delivery of infrastructure or the provision of services in which the private sector bears a significant amount of risk and management responsibility and can play an important role in closing the infrastructure gap.(6) In Gulf States, governments have long used the high revenues from hydrocarbons to provide the needed funds for infrastructure projects in their annual budgets without the need for support from the private sector. Recently, however, low oil prices have paved the way for a growing interest in PPP. The current low oil price environment has encouraged the Gulf States governments to revisit the PPP option. Dubai, Kuwait, and other countries such as Oman, Qatar and Saudi have started to look at PPP structures for assistance in their infrastructure programs. The reduction in oil revenues has a high impact not only on the government cash flows, but also on the capital reserves of local banks, which has significantly affected their liquidity. However, this does not mean that the government should pay more, instead, it should encourage the public authority to focus more on 'value-for-money'.(7)

In Egypt, PPP contracts are subject to PPP legislation No. 67 of 2010 and not to the provisions of law No. 129 of 1947 on Public Utilities' concessions, law No. 61 of 1958 on concessions relating to the Investment of Natural Resources, nor of law No. 89 of 1998 for State Procurement and any specific laws on granting concessions of public utilities (Art. 1, Promulgation articles). Consequently, PPP contracts in Egypt(8) are not administrative contracts.(9) In Gulf States, countries that have PPP legislation (e.g., Kuwait and Dubai) allow the parties in PPP agreements to subject the said arrangements to the PPP legislation. On the other hand, Arab countries which do not have special legislation for PPP may consider PPP as an administrative contract since the legal arrangement for PPP depends mainly on the substantive clauses in the PPP contract.(10)

(4) The World Bank, "Benchmarking Public-Private Partnership Procurement", 2017; International Bank for Reconstruction and Development, "Benchmarking PPP Procurement: Assessing Government Capability to Prepare, Procure and Manage PPPs", 2016, p. 14.

(5) S. HANAFI and K. EL DARDIRY, "PPPs in Egypt", *ICLR*, 27, Part 4, Informa, October 2010, pp. 432-447.

(6) See C. BOVIS, "Public Private Partnerships in the European Union", in *Critical Studies in Public Management*, London, Routledge, 2014; *id.*, *EC Public Procurement: Case Law and Regulation*, Oxford, OUP, 2006.

(7) S. KNIGHT, *Dubai Embraces PPP again*, London, Allen & Overy, 2016.

(8) S. HANAFI and K. EL DARDIRY, "PPPs in Egypt", *op. cit.*, pp. 432-447.

(9) M.A.M. ISMAIL, "International Infrastructure Agreements and PPPs in Developing Countries: Substantive Principles", *op. cit.*, p. 154.

(10) M.A.M. ISMAIL, *Public Economic Law and the New International Administrative Contract*, Beirut, El Halabi Publ., 2010; *id.*, *Globalisation and New International Public Works Agreements in Developing Countries*, *op. cit.*, ch. 4.

Government procurement has considerable economic relevance for a large percentage of the Gross Domestic Product in both developed and developing countries.(11) Government procurement provisions also play a central role in international trade agreements.(12) As efficiency is one of the main goals for government procurement, the Arab legislatures in Egypt, Kuwait and Dubai play a significant role in incorporating provisions that promote innovation in the award procedures in their respective PPP legislation. To achieve many targets for Arab governments, PPP legislation in Arab countries has created a new procedural framework for the award of PPP contracts to private sector entities. The new rules are highlighted in the Egyptian PPP legislation No. 67 of 2010 and its executive regulations, the Kuwaiti PPP Legislation No. 116 of 2014 and its executive regulations, and the recently enacted Dubai PPP legislation No. 22 of 2015.

This chapter deals with innovation in public procurements in PPP legislation in Egypt, with reference to Kuwait and Dubai, and how PPP can improve life, infrastructure and services in Arab countries. It is important to note that many Arab countries have already initiated the promulgation of their respective PPP legislation, which are similar to Egypt, Kuwait and Dubai. For instance, the Kingdom of Bahrain is about to enact its PPP legislation to encourage the inflow of Foreign Direct Investments (FDI) to various economic sectors.

While the focus of this chapter is on procurement of PPP, more particularly in the process for selecting a private partner to undertake the responsibility of developing PPP projects, this chapter likewise presents the recognized good practices in selecting private partners for PPP contracts, and, thereafter, examines whether the PPP Arab legislation and regulatory frameworks adhere to them or not. Moreover, this chapter looks into the application of the principles of transparency, objectivity and fairness in the procurement process and the evaluation criteria for bids, and identifies if there are specific provisions that may result in a possible lack of competition. Nonetheless, this chapter is limited to the use of *de jure* data in capturing the characteristics of laws and regulations encompassing PPP procurement rules and other relevant legal texts.

This chapter is divided into three parts. The first part presents the conceptualization of the main targets for the new award procedures in PPP legislation in Egypt, Kuwait and Dubai. The second part provides an analytical perspective on the new award procedures in PPP legislation in Egypt 2010,

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(11) G.M. RACCA, R.C. PERIN and G.L. ALBANO, "Competition in the Execution Phase of Public Procurement", *Publ. Contr. L.J.*, Vol. 41, No. 1, fall 2011, p. 92.

(12) *Ibid.*, pp. 93 and ff.

Kuwait 2014 and Dubai 2015 in order to define the profile of innovation in award procedures. The third part highlights the conclusions on the adherence of Egypt, Kuwait, and Dubai to the international best practices and principles using the measurements provided in the 2017 Benchmarking PPP Procurement by the World Bank Group and in the Methodology for Assessing Procurement Systems (MAPS) by the Organization for Economic Cooperation and Development (OECD).

## ***2. New Award Procedures in PPP Legislation in Egypt, Kuwait and Dubai: Concepts***

Statistics show that about 9 trillion USD is the world annual spending by governments for public contracts. This expenditure amounted to 12-20% of the total world GDP.(13)

The Sustainable Development Goals (SDGs) expressly seek to “develop quality, reliable, sustainable, and resilient infrastructure, including regional and trans-border infrastructure, to support economic development and human well-being, with a focus on affordable and equitable access for all”. The SDGs also recognize the importance of the relationship between the public sector and the private sector when emphasizing the need to encourage and promote effective public-private partnerships.

To help achieve the SDGs, governments must have the capacity to identify the projects that are best accomplished through PPP. They must also address the need for an appropriate award procedural framework while ensuring adherence to the principles of transparency and efficiency in the conduct of public procurement, and to achieve the expected value-for-money and sustainable investments.(14) Governments, private sectors, and international development organizations have already agreed on the importance of quality infrastructure in fostering economic growth, and, thereby, recognized their role in supporting the efforts to reduce poverty.(15) In Arab countries, the aim of government procurement systems in general, and, more particularly on the procurement for PPP, is to assess the selection process for private partners, whilst ensuring transparency, objectivity, and fairness of the process, as well as the bid evaluation criteria.

A transparent and non-discriminatory government procurement becomes a best tool to achieve ‘value for money’ when the main subject of the procedural

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(13) OECD, Arabic translation of “Methodology for Assessing of National Procurement System” (MAPS), Vers. 2016 (Draft for Public Consultations, July 2016), p. 1.

(14) L.W. CARTER and A.L. CLAROS, Foreword, in *Benchmarking Public-Private Partnership Procurement*, *op. cit.*

(15) *Ibid.*

rules of legislation is to implement the principles of government procurement. In addition to transparency and non-discriminatory principles, there are other principles that are maintained in PPP legislation in Egypt, Kuwait and Dubai such as integrity, objectivity, accountability, fair competition, equal treatment, equality, objective evaluation for bids, and balance. These principles when implemented reflect the efficiency of PPP legislation. As a matter of fact, the PPP award procedures in Egypt, Kuwait and Dubai are the fundamental tools in implementing the basic principles adopted by OECD MAPS and OECD Recommendations on Public Procurement 2015.(16) For instance, the Egyptian legislation develops effective, accountable and transparent administrative organs such as the PPP Central Unit (PPPCU) at the Egyptian Ministry of Finance. PPP legislation aims at promoting public procurement practices that are sustainable, in accordance with national policies and priorities. The award process is a very crucial stage in the government procurement chain. Efforts in promoting competition, transparency, equal treatment, and objectivity, on one hand, while preventing corruption, on the other hand, play a fundamental role in the public procurement process. In Egypt, Kuwait and Dubai, PPP legislation and its executive regulations require the procuring entity to have objective awarding criteria that aim to protect public interests and public funds.

There are various mechanisms and guarantees to prevent corruption and bureaucracy in PPP legislation in Egypt, Kuwait and Dubai. On-line bidding systems exist (to some extent) in some Arab countries as one of the mechanisms to maintain objectivity, fight corruption, and avoid bureaucracy. Arab countries have not yet implemented full on-line bidding systems.

The type of legal system and whether it is a common law or civil law weigh heavily on the type of PPP legislative and regulatory frameworks that exist in particular jurisdictions. Jurisdictions with 'common law' legal systems tend to rely on policy documents and administrative guidance materials, whereas jurisdictions with 'civil law' legal systems are more likely to set up a detailed PPP framework in a binding legal document or statute or legislation.(17) Egypt, Kuwait and Dubai have civil law legal systems.(18) The selection of the private partner is usually carried out through a public tendering process, applying either general public procurement legislative and regulatory rules, or procurement legislative and regulatory rules specially adopted for PPP.

It is of fundamental importance that award procedures in PPP legislation achieve the agreed standards recognized by the international organizations. The sub-indicator below adopted by the OECD is significant in the PPP award

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(16) OECD, "Methodology for Assessment of the National Procurement System", *op. cit.*

(17) *Benchmarking PPP Procurement Report, op. cit.*, p. 22.

(18) *Ibid.*

procedures context in Egypt, Kuwait and Dubai. The purpose of the sub-indicator below, as it is stipulated by the OECD, is to determine: a) the structure of the regulatory framework covering public procurement; b) the extent of its coverage; and c) the public access to the laws and regulations.(19)

Scoring Criteria	Score
The legislative and regulatory body of norms complies with all the following conditions: (a) Is adequately recorded and organized hierarchically (laws, decrees, regulations, procedures,) and precedence is clearly established. (b) All laws and regulations are published and easily accessible to the public at no cost. (c) It covers goods, works, and services (including consulting services) for all procurement using national budget funds.	3
The legislative and regulatory body of norms complies with (a) plus one of the above conditions.	2
The legislative and regulatory body of norms complies with (a) of the above conditions.	1
The system does not substantially comply with any of the above conditions.	0

It is clear that the legal systems in Egypt, Kuwait and Dubai regarding the legislative and regulatory frameworks of PPP public procurement are consistent with these sub-indicator requirements.

### ***3. Award Procedures in PPP Legislation in Egypt, Kuwait and Dubai: Innovations(20)***

#### **3.1. Profile of innovation in award procedures in the Egyptian PPP legislation**

Egypt is located at a crossroads between Africa, Asia and Europa. It has the third-largest GDP in the Arab world, after oil-rich Saudi Arabia and the United Arab Emirates (UAE). It is considerably more diversified than many economies in the region, with manufacturing and agriculture as key

(19) OECD MAPS, “Sub-indicator 1 (a), the scope of application and coverage of the legislative and regulatory framework”, pp. 10-11.

(20) On PPPs in Egypt and Arab countries, *see gen. M.A.M. ISMAIL, Public Economic Law and the New International Administrative Contract, op. cit.*; R. MAHMOUD, *PPP Agreements, Comparative Study to these Contracts in French Administrative Law*, Cairo, Dar el Nahda el Arabia, 2007, and the second edition, *PPP Agreements*, Cairo, Dar el Nahda el Arabia, 2010. On PPPs in Europe, *see C. BOVIS, “Public Private Partnerships in the European Union”, op. cit.*; and *see S. ARROWSMITH, The Law of Public and Utilities Procurement, op. cit.*

contributors, making up 14.5% and 15.7% of GDP, respectively, according to the Central Bank of Egypt, as well as oil and gas extraction.

Egypt's economy has continued to expand, with the IMF forecasting GDP growth of roughly 4% for 2015 and 4.4% for 2016. For the past century and a half, the Suez Canal (*i.e.*, one of the oldest concessions worldwide) has been a major conduit for international trade, including oil. For many centuries, Egypt has taken the lead in Arab countries, and, is still carrying out major governmental transformation in the aftermath of the 2011 revolution. Despite the greater political stability and growth in Arab nations beginning 2015, Egypt is still facing some economic challenges. Creating jobs, developing infrastructure and enhancing services, building homes for its growing population and improving living standards for the poorest are among the most important priorities by the Egyptian government. Egypt also aims at increasing the inward flow of Foreign Direct Investments (FDI) in various economic sectors.(21)

Cultural and legal globalization(22) play significant roles in transnational and socio-economic phenomena in Arab countries' legal systems. The influence of civil law jurisdictions (*i.e.*, the traditional concept of *le contract administratif*) is clear in many Arab countries.(23) Legal globalization has influenced legislation, case law, and traditional concessions which are rigid contractual types in Arab countries.(24) New contractual patterns have emerged in Arab countries(25) and the codification of PPP transactions in Arab legislation is an evidence(26) (e.g., Egypt law No. 67 of 2010, Kuwait law No. 116 of 2014 and Dubai law No. 22 of 2015). Among the new modernized and liberalized rules in Arab legislation are the new and innovative award procedures in PPP legislation in Egypt, Kuwait and Dubai.(27)

(21) The targets for developments in Egypt through PPPs structures were reviewed in 2009, see The Egyptian Ministry of Finance, "Update on the National Program for Public Private Partnership", Min. Fin. Publ., June, 2009, p. 6.

(22) J.E. STIGLITZ, *Globalization and Its Discontents*, New York, W.W. Norton & Co. Inc., 2004; see also J.E. STIGLITZ, *Making Globalization Work*, New York, W.W. Norton & Co., 2007; B. SNOWDOWN, *Globalization, Development and Transition*, Cheltenham, Edward Elgar, 2007; M.S. WAHAB, *Cultural Globalization and Public Policy: Exclusion of Foreign Law in the Global Village*, Oxford, OUP, 2005, Vol. 8, p. 306.

(23) In the traditional theory of *le contract administratif* in Egypt and Arab legal systems, see S.E. TAMAWY, *General Principles in Administrative Contracts*, 5<sup>th</sup> ed., Cairo, Dar El Fikr El Arabi, 1995; S. EL SHARKAWY, *The Administrative Contracts*, Cairo, Dar el Nahda el Arabia, 2003.

(24) M.A.M. ISMAIL, *Public Economic Law and the New International Administrative Contract*, *op. cit.*; *id.*, *Globalisation and New International Public Works Agreements in Developing Countries*, *op. cit.*, ch. 4.

(25) H.S.E. DIN, *Legal and Contractual Frameworks of Infrastructure Projects Financed by the Private Sector*, Cairo, Dar el Nahda el Arabia, 2001, ch.4.

(26) M.A.M. ISMAIL, *International Infrastructure Agreements and PPPs in Developing Countries: Substantive Principles*, *op. cit.*, p. 154; and *id.*, "Legal Globalization and PPPs in Egypt", *op. cit.*, pp. 54-67.

(27) *Benchmarking report on Public-Private Partnership Procurement* defines the term 'Regulatory Framework' as: "Regulatory framework. A framework encompassing all laws, regulations, policies, binding guidelines or instructions, other legal texts of general application, judicial decisions, and

In the Egyptian legal system, administrative contracts are generally subject to the State Procurement Law No. 89 of 1998 and its executive regulations which stipulate that the only way to select the private partner in PPP is through a public tender under the State Procurement Law. Selecting the private partner in PPP projects through the State Procurement Law is a very complicated process. After promulgation of the PPP legislation in 2010, PPP agreements and selecting the private partner are no longer subject to the provisions of the State Procurement Law in Egypt (Art. 1 from the Promulgation Articles).

The current legislation in Egypt strengthens the selection of private partners using the most efficient and innovative patterns for award procedures in public procurement, an approach that is clearly emphasized in the Egyptian PPP legislation. There are many strategic points which are considered creative and innovative steps towards achieving international good practices and principles in public procurement for PPP.

Egyptian PPP legislation stipulates that investor selection is subject to the principles of publicity, transparency, free competition, equal opportunity, and equality pursuant to the rules and procedures of this law and its executive regulations. Publication, advertising and preparation for the participatory competition are in accordance with the PPPCU in the manner described at the executive regulations of the PPP legislation.(28)

Generally, there is no special administrative organ in Egypt concerned with State procurement,(29) however, the PPP legislation in Egypt stipulates that a special pre-qualification committee (hereinafter referred to as 'the Committee') shall be established by an administrative decree from the concerned authority (the representative of the public juristic entity on the PPP contract). The Committee shall contain legal, technical and financial experts. The Committee has among its members a representative or more from the

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administrative rulings governing or setting precedent in connection with PPPs. In this context, the term policies refers to other government-issued documents that are binding on all stakeholders, that are enforced in a manner similar to laws and regulations, and that provide detailed instructions for the implementation of PPPs. It should not be confused with policy in the sense of a government's statement of intent to use PPPs as a course of action to deliver public services. The regulatory framework includes but is not limited to those laws, regulations, policies, and other government actions specifically dealing with PPPs. (For example, procurement of PPPs may be governed by the general procurement framework.). In this chapter, 'Regulatory framework' technically means regulations issued by the executive power in Arab countries through administrative decrees, and which do not include legislation (laws). In this book chapter the term 'legislation', 'legislative framework', or 'laws' means legislation promulgated by Parliaments in Arab countries according to procedural criterion. Legislation must contain rules which are general and abstract according to substantive criterion".

(28) Art. 19 Egypt. PPP legis.

(29) It is important to refer to the fact that some Arab countries do have specialized organs for procurement; for example, the Kingdom of Bahrain, has a unified administrative organ concerned with bidding processes for all public juristic entities in the Kingdom.

partnership unit at the administrative body if there is such a unit.(30) The executive regulations determine the competencies of this committee and its disciplines.

Investors whose names are not listed among qualified investors may question the Committee's decision in disqualifying them. Any objection to the Committee's decision must be forwarded to PPPCU for evaluation and decision. The executive regulations provide the time-bar, the procedures for filing an objection, including the procedures for decision-making. The mechanism for filing an objection or an appeal at this stage is one of the guarantees to ensure that there is objectivity, integrity, equal opportunity and equality in the preliminary stages for procurement.(31)

The administrative body may coordinate with PPPCU in inviting qualified investors for introductory meetings to discuss issues relating to the project specifications and its preliminary conditions. Answers to all queries should be accessible to all qualified investors. Any qualified investor may request before the concerned authority of the administrative body to maintain confidentiality on his/her offer or his/her financial or economic expectations. This does not contradict with the principle of transparency as it merely protects the economic and financial interests of the private investor.

Qualified investors are subject to equal opportunity and equality principles. To achieve the best quality for infrastructure and services which maintain regularity for public utilities, the concerned authority of the administrative body may decide to re-study specifications of the project and its preliminary conditions in the light of the abovementioned meetings and without violation of the qualification criteria. This must be done before issuing tenders invitations.(32)

Egyptian PPP legislation allows the concerned authority at the administrative body to use a two-phase tendering process in the submission of the financial and technical tenders subject to prior consent from PPPCU.(33) Phase one refers to the submission of a non-binding offer containing the main features of the financial and technical offer, followed by competitive dialogue,(34) whereas, phase two is the submission of the final offers for final evaluation. The executive regulations of the PPP legislation provide the rules and regulations of tendering in these two phases.

The use of a dialogue process maintains fair competition and equality on one hand, and enables the administrative authority to select the best technical

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(30) Art. 20 of Egypt. PPP legis.

(31) *Ibid.*

(32) Art. 21 Egypt. PPP legis.

(33) Art. 22 Egypt. PPP legis

(34) Art. 23 Egypt. PPP legis.

and financial private partner without compromising the principles of integrity and objectivity on the other.(35) The administrative authority aims to achieve a *win-win* situation for the administration and the private partner. The public juristic entity shall maintain competition among qualified investors who submitted their non-binding offers through competitive dialogue and with each investor separately.(36) The aim of this dialogue is to obtain information regarding financial and technical offers. Dialogues must be confidential and must promote equality among qualified investors. It is worth noting that the confidentiality provision in the Egyptian PPP legislation does not violate the principle of fair competition as confidentiality in this context aims, among other goals, at avoiding cartels or secret dealings against the administrative body which may result in harm to the public interest and the national economy. Confidentiality, in this context, also raises protections for foreign investors as it protects their financial offers (contracts prices and price formulas offered by them) and keeps that information confidential from competing private entities in the international markets. The executive regulations set the rules and disciplines in the conduct of these dialogues.

The administrative body, in coordination with PPPCU, drafts the stipulations and specifications for the project. The stipulations and specifications shall define the conditions which are not negotiable with the investor.(37) The above-mentioned conditions shall determine the mechanisms and basis for evaluation between offers, and, in case there is an evaluation with points, the evaluation criterion should be clarified, and the bases for comparison of the financial and technical offers must be highlighted with a score to each offer and with a mechanism for applying evaluation criterion to those offers. The legislative stipulations are provided to ensure objectivity, equality, fair competition, and to protect public interests.

For more liberalization in the process and without violating the principles of integrity and transparency, the administrative body shall invite qualified investors (and with no advertisements in the newspaper as stipulated in traditional procurement in law 89 of 1989)(38) to discuss the stipulations pursuant to the rules and bases in the implementing rules (*i.e.*, the executive regulations for Egyptian PPP legislation).

PPP legislation in Egypt highlights the guarantees for public interests and regularity for public utilities by stipulating that the technical offer must contain the detailed specifications of the project to achieve the required

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(35) *Ibid.*

(36) *Ibid.* On competitive dialogue, see S. ARROWSMITH, *The Law of Public and Utilities Procurement*, *op. cit.*

(37) Art. 24/d, e, Egypt. PPP legis.

(38) Art. 26 Egypt. PPP legis.

standards for services in the project, in accordance with the conditions and specifications pointed out by the administrative body.(39)

As a matter of fact, the legislative policy behind the award procedures' provisions in the Egyptian PPP legislation is to achieve the public interest; to maintain the best selection for the investor; to procure so that good standards for services and products are available through the PPP process; to achieve the principles of the new PPP award procedures as they are set out in the PPP legislation;(40) to maintain regularity, continuity and good disciplines of public utilities; and to provide incentives to attract Foreign Direct Investment (FDI) to Egypt. The award procedures in PPP legislation in Egypt aim to create balance between achieving the public interest and maintaining the fundamental principles for PPP award procurement on one hand, and creating through legislation and a regulatory framework the best environment to attract Foreign Direct Investment (FDI) on the other. The principle of equality in the Egyptian PPP legislation(41) is an assurance giving wider scope of application to the fundamental principle in Arab administrative law and practice of 'equality before public utilities'. However, the principle of equality on the PPP award procedures' context has a broad ambit as it aims to strengthen the traditional equality principle in practice to achieve equality for investors before the administrative authority, equal opportunity among investors before an administrative authority (the awarding authority), as well as equality among end-users before public utilities.

As transparency, objectivity and equal opportunity are listed among the fundamental principles which govern the award procedures of PPP contracts in Egypt, the Egyptian PPP legislation allows that offers may be submitted through a consortium consisting of more than one qualified investor, unless the administrative body stipulates that qualified investors must submit their offers individually. If a consortium has submitted an offer, any member of this consortium is prohibited from submitting any other offer, either directly or indirectly, and either as an individual or through another consortium, or through any other company in which this investor owns the majority of its capital, or has a monopoly over its management, unless the administrative body stipulates otherwise.(42) Any offer which is submitted in violation of this paragraph is null and void. This legislative stipulation is a new provision in award procedures in the Egyptian legal system as it aims to ensure transparency, integrity, objectivity in public procurement, whilst maintaining fair competition and equal opportunity among investors.

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(39) Art. 27 Egypt. PPP legis.

(40) Art. 19 Egypt. PPP legis.

(41) Art. 19, 21 and 23 Egypt. PPP legis.

(42) Art. 28/2 Egypt. PPP legis.

### 3.2. Award evaluation in the Egyptian PPP legislation

PPP legislation in Egypt has stipulated that the competent authority at the administrative body shall issue an administrative decree to form a Committee to receive offers and study each financial and technical offer. The Committee is composed of technical, financial, and legal experts. The executive regulations shall provide for the competence and disciplines required from the Committee, as well as the bases for ranking of offers of the technically accepted offers, and the grounds for disqualification of an offer. To ensure the correct selection of the private partner, the Committee must have members from the legal opinion department at the *Conseil d'État*, Ministry of Finance, and PPPCU.

The Committee may form a sub-committee consisting of its members to study the offers from technical, financial and legal perspectives, or may appoint other experts to exercise the same functions. The sub-committee or the appointed expert has to make sure that offers are compatible with the stipulations and specifications determined by the administrative body. The sub-committee has to submit a report on the result of its evaluation with recommendations to the Committee. The Committee will evaluate compatible offers according to the evaluation criteria provided by the administration, and, thereafter, decide for the best economically feasible offer for the State. Each offer is given an evaluation grade according to the bases and the mechanism in evaluation of offers that are provided in the final offer submission request. The individual grades are used in ranking the technically accepted offers. The principle of 'Value for money' is highly considered by the Egyptian legislature.

Offers which are not compatible with stipulations and specifications have to be rejected. The offerors with accepted technical offers are invited to attend the financial offers' selection session. The project has to be awarded to the offeror who is financially feasible among technically accepted offerors after applying the 'relative weight' of the technical and financial criteria in the specifications. The executive regulations shall clarify the rules for the evaluation of technical and financial offers. As a tool to assure the selection of the best offer, the Egyptian PPP legislation stipulates that negotiations may be exercised with the winning offeror to clarify some issues and details on the financial and technical conditions. Negotiations should not deal with any contractual clauses which are considered non-negotiable clauses in the invitation to the offer. Any amendments to the technical or financial conditions which reduce the standards that the offer contains are prohibited.(43)

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(43) Art. 31 Egypt. PPP legis.

The following shows the main features of PPP procurement in Egypt as illustrated in the World Bank Benchmarking Report on PPP Public Procurement in 2017:

*EGYPT, ARAB REP(44) GNI PER CAPITA (IN USD) \$ 3,340*

**Preparation of PPPs**

Central Budgetary Authority’s approval	Yes	Both before the tendering and contracting signature
PPP’s prioritization consistent with public investment prioritization	Yes	Detailed procedure not regulated
Economic analysis assessment	Yes	No specific methodology developed
Fiscal affordability assessment	Yes	Specific methodology developed
Risk identification	Yes	Specific methodology developed
Financial viability assessment	Yes	No specific methodology developed
PPP v.s. Public Procurement comparative assessment	Yes	Specific methodology developed
Market assessment	Yes	No specific methodology developed
Draft PPP contract included in the request for proposals	Yes	
Standardized PPP model contracts and/or transaction documents	Yes	

**Procurement of PPPs**

Evaluation committee members required to meet specific qualifications	Yes	Detailed membership and/or qualification not regulated
Public procurement notice of the PPP issued by procuring authority	Yes	Available online
Minimum period of time to submit the bids (>= 30 days)	Yes	No specific period of time regulated
Tender documents detail the stage of the procurement process	Yes	
Clarification questions for procurement notice and/or the request for proposals	Yes	Answers are publicly disclosed
Financial model submitted with proposal	Yes	
Proposals strictly and solely evaluated in accordance with published evaluation criteria	Yes	
Procedure when only one proposal is received	Yes	Detailed procedure established
Publication of award notice	Yes	Available online
Notification of the result of the PPP procurement process	Yes	Inclusion of grounds for selection not regulated
Regulation of negotiation with the selected bidder before contract signing	Yes	
Publication of contract	No	

(44) *Benchmarking Report on PPPs Public Procurement, op. cit.*, p. 77.

### Unsolicited Proposals (USP not regulated)

Assessment to evaluate unsolicited proposals  
 Competitive PPP procurement procedure for USP  
 Minimum period of time to submit the bids (>=90 days)

### 3.3. PPP legislation in Dubai

PPP's in the UAE or the wider Gulf States have been well known for many years. Dubai has partially embraced PPP in the form of operation and maintenance contracts such as the Dubai Metro (rather than full PPP). Gulf States' governments also have a successful history of quasi-PPP's in the electricity and water sectors such as the ADWEA IWPP programme. In Gulf States, instead of framing the need as one for significant infrastructure programmes without having to pay for them up-front, Gulf States' governments have focused on bringing in new skills, better allocating risks to the private sector (including completion on-time and on-budget) and diversifying their economies away from carbon reliance. Nonetheless, the current low oil price environment has likewise encouraged the Gulf States' governments to revisit the PPP approach. Dubai, Kuwait, and other Gulf countries such as Oman, Qatar and Saudi Arabia have looked at the PPP structure as a pivotal tool to assist their infrastructure developments.(45)

The objectives of PPP's in Dubai are set out in the new PPP legislation.(46) The PPP legislation in Dubai aims at many targets such as: regulating public private partnerships; encouraging private sector participation in development projects and increasing investment to serve Dubai's economic and social growth; enabling the government to perform strategic projects efficiently; using the private sector to enable the end-users to obtain the best services at the least cost; increasing productivity and improving the quality of public services; transferring knowledge and experience from the private sector to the public sector; minimizing the financial risks to the government; and increasing competition for projects locally, regionally and internationally.(47)

PPP Legislation in Dubai stipulates in Article 14 that a special Committee for PPP shall be formed, and it shall carry out and exercise all duties mentioned in Dubai PPP law. The investor selection shall be subject to the principles of

(45) S. KNIGHT, *Dubai Embraces PPP again, op. cit.*

(46) Art. 3 new PPP legis. in Dubai.

(47) S. KNIGHT, *Dubai Embraces PPP again, op. cit.*

publicity, transparency, fair competition, equal opportunity, equality, advertising for the competition, and public interests' considerations.(48)

The law also illustrates the principles of equality amongst users of the services, publicity, transparency, competitiveness, equal opportunities, equality, announcement of competition and the public interest.(49) Projects are to be approved by (a) the director general of the relevant government department, if the total costs to the government are less than AED200m (about USD55m), (b) the Department of Finance (DoF), if total costs are between AED200m (about USD55m) and AED500m (about USD135m) and (c) the Committee, if the costs are higher,(50) although any financing obtained by the project company is to be approved by the government department (in coordination with DoF).(51) In any case, the majority of projects will require the approval by the Committee.(52)

PPP Legislation in Dubai confirms that Dubai will not apply the Procurement Law No. 6 of 1997 other than where the PPP Contract contains no clear provision on a matter. Implementing PPP schemes in Dubai assume that there is a new procurement system in Dubai for PPP, as the application of the Procurement Law No. 6 of 1997 would create various unpredictabilities. The traditional procurement law in Dubai contains a number of requirements concerning tender conditions, timescales and contract terms, which do not sit easily with either the PPP procurement process or a PPP contract. PPP legislation in Dubai contains provisions relating to the pre-qualification, tender and selection processes and PPP contract terms including bidding terms and conditions and financial security; conditions of the PPP contract, bid bond value, performance bond value calculations and means of comparing bids; and tender scoring and evaluation procedures.(53) These provisions provide the public juristic entity with a high degree of flexibility to specify the tender and contract conditions on a case-by-case basis. The overriding award criterion is the 'most financially and technically advantageous bid', but the government entity has discretion to specify the detail of this, including the balance between technical and financial criteria, in the tender documents. PPP legislation allows private entities to make unsolicited proposals for PPP projects and allows the public juristic entity to contract directly with the entity that makes such a proposal. There is no requirement for such proposals to be put to tender.(54)

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(48) Art. 14/A PPP legis. in Dubai.

(49) Art. 14 and 29 PPP legis. in Dubai.

(50) Art. 8 PPP legis. in Dubai.

(51) Art. 36 PPP legis. in Dubai.

(52) S. KNIGHT, *Dubai Embraces PPP again, op. cit.*

(53) Art. 14 to 24 PPP legis. in Dubai.

(54) See Art. 12 and 14 PPP legis. in Dubai. See also DLA Piper, "Infrastructure Update, Dubai's New PPP Law".

The PPP Legislation does not apply to electricity and water projects that are governed by the Electricity & Water Sector Law No. 6 of 2011 or simple works contracts or supply contracts that are governed by the Procurement Law No. 6 of 1997.(55)

### 3.4. Direct contracting in Dubai PPP legislation

Dubai PPP legislation points out that irrespective of sub-clause of Article 14/A, the public juristic entity may enter into direct contracting (without tendering) with the project company if there is a new and creative project offered by this company.(56) The criterion for selecting the private investor through direct contracting is to access a new and creative project by this investor. The direct contracting mechanism undermines, to some extent, objectivity, equality and fair competition principles in selecting private partner. It may be argued that direct contracting remains to be a rapid and liberal mechanism for selection of the private partner since it avoids bureaucracy. As a matter of fact, it is, to some extent, against equal opportunity, equality and fair competition principles.

To assure transparency, equal opportunity and free competition, the Dubai PPP legislation illustrates that administrative bodies must start the procedures by undertaking the necessary process for the qualifications of companies which may enter in partnership with the government, and ensuring that the project and its details are advertised in the media before starting award procedures. The administrative body may start preliminary meetings with the qualified partners to discuss the specifications of the project and the preliminary conditions.(57) This mechanism is to assure the best specifications for the project, to maintain running public utilities in a regular manner, and to apply '*value for money*' principles in public utilities' projects.

Qualified partners may stipulate a confidentiality in their dealings with the administrative body, and request nondisclosure of any information regarding their economic or financial expectations relating to the project subject to partnership. It is argued that confidentiality on this context is to protect investors from unauthorized disclosure of their financial secrets to their competitors. A counter argument, however, suggests that confidentiality provision violates the principle of transparency.

Further, dealing with a qualified partner should be in light of the principles mentioned in Article 14, that is, to procure equal opportunity and absolute equality among them. If the administrative body amends specifications of the

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(55) DLA Piper, "Infrastructure Update, Dubai's New PPP Law".

(56) Art. 14/c PPP legis. in Dubai.

(57) Art. 15 PPP legis. in Dubai.

project, with no violation to qualification criteria, it has to expressly advertise in the media, with enough time before starting receiving offers.(58) This legislative stipulation not only assures the application of fair competition principle, but it is also in accordance with the good international practices that are mentioned by the OECD MAPS, OECD Recommendations and the World Bank Benchmarking Report on PPPs Procurement 2017.(59)

### 3.5. The PPP legislative and regulatory frameworks in Kuwait

In Kuwait, the PPP legislation of 2014 stipulates in announcement and in the project procurement procedures that the selection of the investor shall be subject to the principles of transparency, openness, freedom of competition, equal opportunity and equality in accordance with the rules and procedures provided for under this Law and its executive regulations.(60) The legislation and its executive regulations provide for further guarantees.

PPP legislation in Kuwait consider PPPs as an exception from the Public Procurement law in Kuwait law No. 37 of 1964. PPP procurement and all rules for submitting offers and their financial and technical assessment, the competent entity, documentation, pre-qualification and post-qualification, objections from the competent entity decisions, its procedures, time-bar, its rules and procedures, and competitive dialogue are organized by the executive regulations if not organized by PPP legislation.(61) In addition to PPP legislation, the executive regulations shall regulate the general bases for projects tendering, and the advertising for these projects in the media.(62)

The executive regulations point out the methods for proposing PPP projects and the approval mechanism.(63) The proposal for the procurement and implementation of a PPP project may be submitted by the following entities:

- 1- Public Entities: a public entity wishing to propose a project that falls within its competences in accordance with the PPP Law shall submit a request to the public authority along with the comprehensive feasibility studies of the project in accordance with the Law, its executive regulations and the Guidebook.
- 2- The Higher Committee: the Higher Committee approves the request of the relevant public entity for the procurement of a PPP project in accordance with a PPP model, and it may propose PPP projects to public entities.

(58) Art. 16 PPP legis. in Dubai.

(59) *Benchmarking Public-Private Partnership Procurement, op. cit.*

(60) *See* Art. 8 PPP legis. in Kuwait.

(61) Art. 9 PPP legis. in Kuwait.

(62) Art. 27 PPP legis. in Kuwait.

(63) Art. 2 Exec. Regul. of the PPP legis. in Kuwait.

- 3- The private sector: the private sector may submit before the authority a draft concept along with preliminary feasibility studies, as per the authority's requirements, for the implementation of a project and the approval of the procurement thereof in accordance with the provisions of the Law.

The authority, in coordination with the public entity, shall review the feasibility studies presented by the aforementioned entities and finalize the same, as needed, in order to submit an appropriate recommendation thereon to the Higher Committee. The authority may prepare the project's comprehensive feasibility studies and procurement documents, and, it may, in all cases, seek support from advisory firms and specialized offices whether local or foreign as it deems suitable for this purpose in accordance with the provisions of the laws and regulations.

The executive regulations of the Kuwaiti PPP legislation point out that a competition committee shall be established. The authority shall establish, following the approval of the higher committee and in accordance with the requirements of the business, a committee for each PPP project named 'Competition Committee', in which the public entity(ies) whose competences and responsibilities correspond to the nature of the project shall be represented, by at least one member being no less than an assistant undersecretary, and provided that technical, financial and legal expertise are also represented therein. The committee shall review, complete and prepare the project related studies, instruments and procurement documents, and, shall approve the same. The committee shall also evaluate the technical and financial offers and shall supervise the public session set for opening the financial envelopes of the technically accepted offers. (64)

The quorum for the committee's meetings shall be at least three quarters of its members. The committee shall issue its decisions and recommendations upon a majority vote of the attending members of the committee. In case of a tie in voting, the vote of the president of the committee shall prevail. The committee may seek support from any expert as it deems necessary, and the latter shall have no voting rights. The committee is considered a one-window service through which the investor deals. Each member of the committee shall be granted all the powers of the public entity he/she represents, within the competences of the committee, thus allowing him/her to collaborate in taking necessary decisions and recommendations without having to refer to the related entity.

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(64) Art. 3 Exec. Regul. of the PPP legis. in Kuwait.

The method for the approval of concepts proposed by the private sector is evaluated as the authority shall, in coordination with the proposed public entity, present the results of the initial feasibility studies of the concepts proposed<sup>(65)</sup> by the private sector to the higher committee along with the authority's recommendation for the preliminary approval of the project as an initiative or a distinguished project or the rejection thereof. In case of approval of a project concept, the concept proposer shall be granted a period of six months to prepare the comprehensive feasibility studies unless the authority decides, based on the nature of the project, to grant him an additional period for this purpose in accordance with the terms and proceedings set by the authority and approved by the higher committee.<sup>(66)</sup>

The authority shall present to the higher committee the results of the comprehensive feasibility study, whether prepared by the competition committee, the private sector or the public entity, along with the authority's recommendations for the approval of the project and its procurement in accordance with the PPP model, or the rejection thereof. If the approval of the project in accordance with the PPP model is recommended, the recommendation shall include a proposed method of competition for the procurement of the project either through a competitive bidding process or a competitive tender process; type of proposed PPP model to be adopted; identification of the public entity(ies) which has/have competences and responsibilities for a project of this nature, in order for them to participate in the preparation of the procurement documents, approve the technical specifications, participate in the evaluation of offers in preparation for the award of the project, sign the PPP agreement and follow-up on the implementation and operation until the transfer to the State; the proposed timetable for the project's procurement stages and proceedings; the proposed investment term; the proposed exemptions and privileges as well as any specific advantage to be granted if the project was submitted through a concept for approval; the proposed service to be provided, its economic, social and/or service importance, or whether it is a development or improvement of an existing service or reduction of the cost thereof or improvement of its efficiency; any request for the allocation of land for the project, if any; any other specifications or requirements according to the nature of the project and based on the Guidebook.<sup>(67)</sup> This is the method for approval of proposed projects.

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(65) Art. 1 Exec. Regul. defines the Concept Proposer as any natural person or legal entity, Kuwaiti or non-Kuwaiti, presenting a Concept for the implementation of a project in accordance with the PPP model before the Authority through a preliminary feasibility study of the project in compliance with the State's strategy and development plan for the approval and the procurement thereof in accordance with the provisions of the Law.

(66) Art. 4 Exec. Regul. of the PPP legis. in Kuwait.

(67) Art. 5 Exec. Regul. of the PPP legis. in Kuwait.

The higher committee shall issue its decision regarding the submitted projects in light of the recommendations presented by the authority.(68)

The executive regulations highlight the general terms for procurement of PPP projects. Regarding the expression of interest, the authority may announce the request for expression of interest for PPP projects, as a procedure preceding the qualification proceedings, in order to assess the interest and willingness of the private sector to participate in the implementation of the project prior to undertaking the procurement proceedings, in the Official Gazette and other local or international media that are suitable with the nature of the project, and through the publication of the same on the website of the authority.(69)

The announcement shall include a short description of the project, its objectives and the proposed location for the implementation thereof, if any, the method for presenting the request and any other information or conditions related to the project. The duration for receipt of a request for expression of interest shall be no less than two weeks from the date of publication of the announcement. The requests for expression of interest may be accepted through electronic mail.

The authority shall review and study the requests for expression of interest submitted by the investors. The authority shall, upon that study, decide on the feasibility for undertaking the proceedings set by the law and invite interested parties for pre-qualification to participate in the competition for the implementation of the project or to refrain from undertaking such proceeding, in preparation to present a recommendation in this respect to the higher committee.

The invitation for qualification is also regulated. The authority shall, following the approval of the higher committee on the PPP project and the determination of the PPP model and the method of procurement in accordance with the provisions of Article 8 of the executive regulations, in collaboration with the public entity appointed by the higher committee, announce the invitation for qualification for the project in the *Official Gazette* and at least two Kuwaiti dailies in both Arabic and English, and in local or international media as may be deemed necessary in accordance with the nature of the project, as well as publishing it on the website of the authority. The announcement of the invitation for qualification shall include determination of the public entity or the public entities relevant to the project; a short description of the project and its objectives; the required expertise for qualification; the contracting model and term; the fee due for the collection of qualification

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(68) Art. 6 Exec. Regul. of the PPP legis. in Kuwait.

(69) Art. 13 Exec. Regul. of the PPP legis. in Kuwait.

documents and the authority may postpone the payment thereof until the submission of qualification requests; the duration fixed for submission of the requests for qualification, the address for its submission and the mail or electronic mail address as per the circumstances. The duration for submission of the qualification requests shall be no less than fifteen days from the date of publication in the *Official Gazette* unless it was decided to undertake a post-qualification in which case the duration shall be included in the duration for submission of proposals.(70)

### 3.6. Terms for qualifications

The terms for qualifications stipulate that each investor wishing to participate in a project being tendered in accordance with the provisions of the law shall prove its capacity to implement the project and fulfil its obligations. The determination of the investor's capacity is undertaken through qualification proceedings. The higher committee may either undertake a pre-qualification or a post-qualification process based on the recommendation of the authority and in accordance with the nature of the project, in order to ensure the proper selection of investors capable of implementing each project separately.(71)

The pre-qualification proceedings are of fundamental importance on this context.(72) After the approval of the higher committee of the feasibility studies and qualification documents, the authority shall announce the acceptance of requests for qualification from investors wishing to invest in a PPP project through the pre-qualification proceedings, in order to ensure the ability of the applicant for a request for qualification to implement the project, based on the terms and conditions specified in the qualification documents. On the other hand, the higher committee may decide to merge the qualification phase with the request of proposals phase; in this case the qualification of investors wishing to invest in the project shall be considered a post-qualification. The terms of post-qualification shall be similar to that of the pre-qualification. The investor wishing to invest shall present the qualification documents in an envelope that is separate from the other envelopes containing the technical and financial proposals. The envelopes of post-qualification shall be opened prior to the opening of the technical and financial envelopes and a list of the qualified applicants shall be prepared and submitted to the higher committee for approval prior to reviewing and evaluating the technical and financial proposals. The investors who do not

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(70) Art. 14 Exec. Regul. of the PPP legis. in Kuwait.

(71) Chap. 5 Exec. Regul., Art. 15 and ff.

(72) Art. 16 Exec. Regul. of the PPP legis. in Kuwait.

meet the post-qualification criteria may request the reimbursement of their bid bonds.(73)

The qualification decision process has to be exercised by the competition committee which shall review and study the requests for qualification submitted by the investors, and it shall prepare a report addressing all of its review and the results of the evaluation of the qualification requests, as well as the investors that are approved to participate in the second phase of the procurement, the investors who are proposed to be excluded and the justifications of any such exclusions. A report regarding the same shall be presented to the authority. After reviewing the aforementioned report, the authority shall present its recommendations with regards to the requests for qualification to the higher committee so that it may issue an appropriate decision in this matter. The authority shall notify the investors of the final decision regarding their requests for qualification at the addresses stated in their requests.(74)

The invitation for submission of proposals is a significant step as it is clear in the executive regulations. The authority in collaboration with the public entity shall invite the qualified investors to collect the project's procurement documents and to submit their proposals. The invitation shall be made through publication in the *Official Gazette* and at least two Kuwaiti dailies in both Arabic and English and other local or international media as may be deemed necessary as per the nature of the project, as well as through publication on the website of the authority, as the authority deems appropriate in this regard.(75)

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(73) Art. 17 Exec. Regul. of the PPP legis. in Kuwait. Art. 18 details the Qualification Documents as follows: "Taking into consideration the special nature of each PPP Project, the qualification documents shall comprise the following: 1. Information for the parties wishing to apply for qualification indicating the means for preparation and submission of the request of qualification; 2. A description of the PPP Project procured for investment including its location, nature and main features as well as the surface of the proposed land for project implementation, if any; 3. A statement of specific expertise that the investor is required to meet in order to be qualified in the qualification phase; 4. Qualification standards; 5. The deadline for collection of qualification documents, indicating the date and hour thereof; 6. The place and the method of submission of qualification documents; the Higher Committee may decide to accept them through means of electronic communication; and 7. The deadline for submission of qualification documents which shall be no less than (15) fifteen days as of the date of the publication of the announcement for qualification in the *Official Gazette*".

(74) Art. 21 Exec. Regul. of the PPP legis. in Kuwait.

(75) Pursuant to Art. 31 Exec. Regul., the invitation for submission of proposals shall include the following: 1. The deadline for the collection of the project's procurement documents; 2. The relevant Public Entity(ies) that will enter into the PPP Agreement and the appendices thereto; 3. The Investment Term; 4. The location of the project stating whether it is being implemented on State-owned land; 5. The fees due and the method of collection of the project's procurement documents, after signing the confidentiality agreement; 6. The deadline for submission of proposals indicating the date and hour which shall be no less than ninety days after the date of publication of the invitation in the *Official Gazette*, as well as the method and place for submission; 7. The incentives and tax and custom exemptions granted for the project. The proposals may be submitted by electronic means of communication which support the necessary confidentiality provided the prior approval of the Higher Committee thereon.

Clarifications regarding the project's procurement documents are significant as the authority may, in collaboration with the public entity, request clarifications from the bidders with respect to their request for qualification or proposals and that in connection with any inquiry or ambiguity it might find in a proposal. It may as well, in any stage of the procurement, request information, data and additional documents confirming the ability of the investor to implement the project. Such clarifications or documents provided by the investor in this regard shall constitute an integral part of its proposal. The investors may submit inquiries with regards to the terms of qualifications and competition in accordance with the conditions and limitations set in the qualification documents and project procurement documents.(76)

The procurement of the project in two stages is illustrated in the executive regulations. The higher committee may, based on the recommendation of the authority, decide to procure the project in two stages in accordance with the nature and requirements thereof, and conduct a competitive dialogue(77) at the intermediary bid-submission stage of the process in order to obtain clarifications in relation to the elements of the technical and financial offers presented during this stage.

In the second stage, final proposals shall be submitted. If the project is to be procured in two stages, the authority in coordination with the relevant public entity must, during the first stage, prepare the procurement documents provided they include the general information regarding the project, its specifications, standards and performance indicators or requirements for financing or its specific basic contractual arrangements and any other information as the authority deems necessary; the obligation for the investor to submit its suggestions with regards to its annotations or observations made on the project's documents, to be reviewed by the competition committee and taken as guidance during the stage of preparation of the final project procurement documents; the initial offers shall not include any information or financial data regarding competitive prices to be offered by the investor.

The offers submitted at this stage shall be limited to the technical, legal, environmental and general financing issues as well as topics permitted under the terms of reference. Upon receipt of the initial offers and the review and study thereof, the authority may invite the investors that have presented their offers to undertake a competitive dialogue with them with regards to their proposed comments made to the project's elements and the initial terms

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(76) Art. 32 Exec. Regul. of the PPP legis. in Kuwait.

(77) The Competitive Dialogue is defined in Art. 1 and ff. Exec. Regul., as: the terms and proceedings adopted by the Authority when having an intermediary bid submission in order to receive the suggestions of the private sector with regards to the project's components and procurement terms.

for its procurement. In case the aforementioned invitation to the investors is made, the investors must all be granted an equal opportunity or duration for discussion.

The authority, in coordination with the public entity, shall review the characteristics of the project and the proposed standards and performance indicators, the financing arrangements and the contractual terms as well as any other matter for which a competitive dialogue has been undertaken, in order to specify those that comply with the public interest, in preparation for making appropriate amendments to the project's final procurement documents to be prepared by the competition committee as per the procedures set under the law, its executive regulations and the guidebook. The authority must review and study such amendments and prepare appropriate recommendations thereon to be presented to the higher committee in order to consider approval thereof as the project's procurement documents.(78)

### 3.7. Evaluation of offers

As the Kuwaiti legal system aims to achieve a high standard of objectivity, equality and maintain free competition, the evaluation of offers procedures are of great significance as the competition committee shall undertake the evaluation of the technical proposals based on the standards and weights stated in the project's procurement documents, prior to reviewing the financial offer. A proposal that does not include a bid bond as stated in the procurement documents shall be rejected. The evaluation of the technical offer must conform to the following:

- 1- Provisions for technical safety included in the offer, including the technology to be used and techniques complying with the terms specified in the project's procurement documents.
- 2- Conforming to the environmental standards specified under the procurement documents.
- 3- Evidence of the quality of the services and facilities to be implemented and provided through the project and their conformity with standards and performance indicators specified under the terms of reference.
- 4- The extent to which suitability between the main components of the project have taken into consideration the provisions of the technical offer and the financial offer.
- 5- Feasibility of the proposed time schedule for the implementation of the project and the effects of such schedule.(79)

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(78) Art. 34 Exec. Regul. of the PPP legisl. in Kuwait.

(79) Art. 37 Exec. Regul. of the PPP legisl. in Kuwait.

The competition committee shall submit a report with respect to the evaluation of the technical offers along with its recommendations to the authority for approval thereof. The authority shall notify the investors whose technical offers were approved and those who were rejected. The latter may submit a grievance as to this before the grievance committee in accordance with the terms and conditions provided for under the executive regulations.

The competition committee shall arrange a public session to open the financial envelopes for the offers submitted by the investors. The qualified investors who have submitted their offers in connection with the project being tendered shall be invited. A representative of the relevant public entity(ies) shall also be invited to attend the session. The committee immediately at the beginning of the public session shall confirm the attendance and ensure the safekeeping of the financial envelopes, and it shall prepare a report with regards to the same. The financial envelopes shall be opened in alphabetic order of the bidders' names. The value of each proposal shall be read out and shall be recorded in a schedule made for this purpose. In case of inclusion of several values within the same proposal, the highest value shall be retained, without prejudice to the authority's right to exclude or reject such proposal in accordance with the terms of the project's procurement documents.(80)

The competition committee must prepare a report in connection with the evaluation of the technical and financial offers in light of the conclusions made during the public session in preparation for the submission thereof to the authority, including its recommendation for the appointment of the preferred investor and the subsequent investor in terms of preference among the submitted proposals.(81)

### 3.8. Submission of one proposal

In case of submission of only one proposal or if the other proposals are invalid because they are in breach or they do not comply with the terms for participation in the competition, the competition committee must prepare a

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(80) Arti. 38 Exec. Regul. of the PPP legis. in Kuwait.

(81) The Authority shall specify in light of the recommendation presented by the Competition Committee the Preferred Investor as being the provider of the best proposal in accordance with the Terms of Reference based on which the project is being procured. The Authority must notify the concerned Investor and the Public Entity of the Investor that was determined as being the Preferred Investor in order to proceed with the negotiations with it. The Authority must also notify the other Investors who passed the financial proposals phase of their ranking. The Authority shall keep the bid bond of the Preferred Investor and the subsequent Investor in the ranking and it may release the bid bonds of the other Investors unless it decides to keep them until the appointment of the Successful Investor or the expiry of the duration of the submitted bonds or their refusal to renew their bonds or the extension thereof as per the terms provided for under the project procurement documents. *See* Art. 39 Exec. Regul. of the PPP legis. in Kuwait.

report in this respect and submit it to the general director of the authority in preparation for the presentation of the same before the higher committee along with the recommendation he deems appropriate.

The higher committee may decide to approve the sole offer or to re-procure the project or to undertake amendments it deems appropriate in the project's procurement documents or it may cancel the investment opportunity without any liability whatsoever.

In case of two equal offers where each forms the best offer as per the terms of the competition, the proposal containing a better technical offer must prevail whenever the technical offer has weight in the formulae used for the award of the project. Otherwise, the bidders may be requested, based upon the recommendation of the authority and the approval of the higher committee, to submit two new financial offers within the limits of their submitted offer, in new envelopes. A public session must be held for the opening thereof, to which the submitters of the two offers must be invited. The value of the offers must be read out during the session. The competition committee shall prepare a report in this respect to be submitted to the authority in preparation for the submission thereof to the higher committee to issue its decision in this respect without prejudice to the higher committee's right to cancel the competition or to re-procure the project without any liability whatsoever. These procedures aim at achieving the principles of equality and fair competition.(82)

The authority shall invite the preferred investor to negotiate the offer it has submitted along with the details and clarifications thereon and its reservations to the project's procurement documents. The authority shall specify in the invitation the topics that shall be negotiated and term of such negotiation. The competition committee, under the supervision of the authority, shall handle negotiations with the preferred investor, and it may seek assistance of professionals, experts and consultancy firms, whether local or foreign, with which the authority may enter into agreements to perform its duties. In all cases, the negotiations shall not address any contractual terms deemed in the invitation for submission of proposals as being non-negotiable or as material deviations according to the project's procurement documents. No amendments may be undertaken with respect to the technical and financial terms and conditions upon which the proposals have been evaluated. The negotiations may not lead to an amendment in the competition terms presented to the preferred investor, or relieve it from its liabilities in accordance with the provisions of the terms of reference under the risk allocation schedule specified in the project's procurement documents. The minutes of negotiations shall be recorded in a report to be signed by the investor and the negotiating parties; any clarifications or

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(82) Art. 41 Exec. Regul. of the PPP legis. in Kuwait.

details made by the preferred investor in this respect shall be considered an integral part of its offer.(83)

Should the negotiations fail to reach a final agreement with the successful investor with respect to the agreement's documents, the authority must notify the investor of the suspension of the negotiations and will request from it the provision of its final position in writing of the best offer that it can provide, and such offer will be presented to the higher committee to issue its decision in this respect along with the authority's recommendations thereon. Should the offer be rejected or should the preferred investor fail to submit the required offer within the period provided, negotiations must be terminated with it, subject to the approval of the higher committee. After the lapse of the grievance duration of the decision for suspension of the negotiations, the authority shall invite the other bidder or bidders as per their ranking to negotiate in order to reach a final agreement with one of them with respect to the terms of the agreement and the settlement thereof. The authority may not resume the negotiations with any of the bidders with whom negotiations are terminated and it may not negotiate with two bidders or more at the same time. It also may not waive for the benefit of the subsequent preferred investor a condition that was a point of disagreement with the former preferred investor. In all cases, the higher committee may decide to cancel the investment opportunity and re-procure the project.(84)

The award of the competition is in all cases subject to the approval of the State Audit Bureau in accordance with Article 31 of the Law. The procurement documents and the offer of the preferred investor shall all be presented to the State Audit Bureau, as well as any of the minutes of any negotiations undertaken with it and the final terms agreed upon, taking into consideration the duration of validity of the bid bond. After obtaining the approval of the State Audit Bureau, the authority in collaboration with the public entity shall draft a comprehensive report on this matter for submission before the higher committee along with the authority's recommendations for approval of the successful investor and invitation for it to sign the letter agreement.(85)

The authority shall in collaboration with the public entity(ies) stated in the decision of the higher committee prepare the project procurement documents in accordance with the provisions of the Law, ensuring the non-disclosure of confidential technical, economic and financial information of the project submitted by the concept proposer and specifically the technical designs of the

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(83) This whole framework was detailed in Art. 42 Exec. Regul. of the PPP legis. in Kuwait.

(84) Art. 43 Exec. Regul. of the PPP legis. in Kuwait.

(85) Art. 44 Exec. Regul. of the PPP legis. in Kuwait.

project and any technique proposed for the implementation thereof as well as any other confidential information.

The principle of confidentiality shall not hinder the procurement of the project in accordance with the principles of free competition, whereby during the preparation of the project documents all the sufficient data and information to prevent the project's monopoly by the concept proposer are provided, ensuring the competition thereon while being procured as per the standards of transparency and fairness.(86)

### 3.9. Review proceedings

The Grievance Committee(87) established through a Council of Ministers decision in accordance with Article 32 of the PPP Law shall review all complaints and grievances submitted by concerned persons with regards to any proceeding or decision issued in violation of the provisions of the law and its executive regulations. The complaint or grievance shall be submitted to the committee within fifteen days after the notification to the concerned person or after the concerned person became aware of such decision. The committee shall have a secretary in charge of receiving complaints and grievances submitted to the committee and of preparing registers to record all such complaints and grievances along with associated memoranda, documents and files. The secretary shall also record the minutes of meetings of the committee, he shall follow-up on the implementation of the decisions issued by the committee and shall undertake all other actions and tasks as may be requested by the committee. The secretary shall record the complaint or grievance immediately upon receipt thereof in a register prepared for that purpose and he shall submit the same to the president of the Grievance Committee within a period not exceeding the end of the next working day following the date of receipt of the complaint or the grievance, and he shall, within that same period, notify the higher committee or the authority of the submission of the complaint or grievance.(88)

### 3.10. Innovation in PPP award procedures to encourage Foreign Direct Investments (FDI) in Arab Countries(89)

G20 Guiding Principles for Global Investment Policymaking points out the objective for investment policy, that is, "With the 'objectives' of (i) fostering an open, transparent and conducive global policy environment for investment, (ii)

(86) Art. 56 Exec. Regul. of the PPP legis. in Kuwait.

(87) Grievance Committee is the committee established in accordance with Art. 32 of the Law for the review of complaints and grievances submitted by concerned persons against decisions or proceedings undertaken by the Higher Committee or the Authority.

(88) Art. 70 Exec. Regul. of the PPP legis. in Kuwait.

(89) "G20 Trade Ministers Meeting Statement: Annex III", Shanghai, 9-10 July 2016.

promoting coherence in national and international investment policymaking, and (iii) promoting inclusive economic growth and sustainable development”.

The non-binding principles to provide general guidance for investment policymaking are proposed by the G20 members as follows:

- 1- Recognizing the critical role of investment as an engine of economic growth in the global economy, governments should avoid protectionism in relation to cross-border investment.
- 2- Investment policies should establish open, non-discriminatory, transparent and predictable conditions for investment.
- 3- Investment policies should provide legal certainty and strong protection to investors and investments, tangible and intangible, including access to effective mechanisms for the prevention and settlement of disputes, as well as to enforcement procedures. Dispute settlement procedures should be fair, open and transparent, with appropriate safeguards to prevent abuse.
- 4- Regulation relating to investment should be developed in a transparent manner with the opportunity for all stakeholders to participate, and embedded in an institutional framework based on the rule of law.
- 5- Investment policies and other policies that impact on investment should be coherent at both the national and international levels and aimed at fostering investment, consistent with the objectives of sustainable development and inclusive growth.
- 6- Governments reaffirm the right to regulate investment for legitimate public policy purposes.
- 7- Policies for investment promotion should, to maximize economic benefit, be effective and efficient, aimed at attracting and retaining investment, and matched by facilitation efforts that promote transparency and are conducive for investors to establish, conduct and expand their businesses.
- 8- Investment policies should promote and facilitate the observance by investors of international best practices and applicable instruments of responsible business conduct and corporate governance.
- 9- The international community should continue to cooperate and engage in dialogue with a view to maintaining an open and conducive policy environment for investment, and to address shared investment policy challenges.

These principles can serve as a reference for national and international investment policymaking, in accordance with respective international

commitments, and taking into account national, and broader, sustainable development objectives and priorities.

In fact, PPP legislative and regulatory frameworks are fundamental pillars and determining factors in any legal system which can be described as incentives to attract and increase the inward flow of Foreign Direct Investment (FDI) on the legislative side and on the governmental policies' side. There is a direct link between the existence of an advanced PPP legislative and regulatory framework on one hand, and the increase of the inward flow of FDI and the improvement of life of the ordinary citizens in Arab countries on the other.

### 3.11. How innovation in award procedures in PPP in Arab countries can improve socio-economic developments

As PPP legislation in Arab countries aims at achieving and implementing fundamental principles in award procedures stipulated in the international practice on one hand, it is clear that PPP award procedures in Arab legislation aims to create a clean environment which increases the threshold of protection to foreign investors through fighting corruption and aims consequently to increase incentives for foreign investments which raise the inward flow of FDI to Arab countries. Principles of achieving public interests, integrity, objectivity, equality, equal opportunity, free competition, fair competition, publicity, and transparency are pivotal mechanisms to fight corruption and they are the same principles which procure a better environment to increase the inward flow of FDI to Arab countries. In the Egyptian PPP legislation,(90) Kuwaiti PPP legislation(91) and Dubai PPP legislation,(92) the Arab legislature assures the fundamental importance of the abovementioned principles. It is true that there is an overlapping between the principles which govern award procedures in PPP legislation in Arab countries and principles which attract FDI to Arab countries as they are similar principles which are required to maintain clean environments for various economic sectors. Principles for both targets may cooperate to encourage PPPs, socio-economic developments, increasing productivity, and developing infrastructure, enhancing services in Arab countries.

As award procedures aim to achieve objectivity, integrity, equal opportunity, fair competition and many other principles, they likewise aim to enhance

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(90) Art. 19-33 Egypt. PPP legis.

(91) Art. 8, 9 and 27 Exec. Regul. of the PPP legis. in Kuwait.

(92) Art. 3, 14-25 PPP legis. in Dubai.

the life of ordinary citizens in Arab countries whether these countries have special PPP legislation or not. Award procedures aim to attain properly structured PPP projects that are more likely to provide 'value for money' to the government and be commercially viable for the private partner.

The innovation in award procedures is a pivotal tool to enhance the life of Arab ordinary citizens as follows:

- 1- Awarding PPP projects aims to increase the inward flow of FDI to Arab countries. Increasing the inward flow of FDI to various economic sectors in Arab countries is a fundamental factor to fight unemployment and decrease the unemployment rate. The increase of unemployment rate in Arab countries is a fundamental factor behind the increase of crime and terrorism in the Middle East region. PPP projects create thousands of job opportunities in Arab countries in various economic sectors.
- 2- The increase of PPP projects in Arab countries enhances the quality of products and services in those countries as in most cases the private partner is a huge multinational company which has unique profile and distinguished experience in the PPP projects' fields. The private partner injects its technological input and modern techniques to achieve the best standards for the running and management of public utilities as these inputs and techniques have direct positive impact to the end-user's life.
- 3- The increase of PPP projects in Arab countries maintains sustainable developments in Arab countries which has a direct impact on ordinary citizens' lives and standard of living, education, health and other crucial services offered by Arab States.
- 4- The increase of PPP projects transfers modern and advanced technologies to Arab countries through awarding many PPP projects in these countries.
- 5- Transfer of technology is a pivotal factor to create highly qualified trained expertise and labour in Arab countries as citizens of Arab countries shall have more job opportunities in PPP advanced technology projects.
- 6- Arab countries shall have the opportunity to export qualified and trained labour and expertise to the surrounding countries and to other regions of the world as a result of awarding PPP projects in Arab countries, given PPPs' leading role in the Arab region in creating highly qualified expertise.
- 7- Awarding PPP projects would inject billions in hard currency to Arab countries, which maintains the stability of the currency exchange rate in the Arab region as it increases the supply of hard currency in Arab markets against demand.

#### *4. Conclusions*

The chapter is an attempt to offer an in-depth analysis of legislative and regulatory frameworks for PPP procurement in some Arab countries. It concludes with the following legal facts:

- 1- As this chapter reaches an assessment of the quality and effectiveness of the PPP procurement system in Egypt, Dubai and Kuwait, the OECD MAPS are of special significance as in most cases, Arab PPP laws have implemented OECD principles in award procedures. The extensive review on the legislative and regulatory frameworks in Arab countries as well as World Bank Benchmarking Report on PPP Procurement 2017 were conducted to identify whether Arab legislation and regulations have implemented the internationally accepted good practices or not. Further, this chapter reaches a conclusion that the development of PPP award procedures in Arab countries had a direct positive impact on the inward flow of foreign investments to Arab countries as well as the potential significant improvements on the socio-economic life of citizens.
- 2- The World Bank Benchmarking Public-Private Partnership Procurement Report 2017 pointed out that:

“The PPP Procurement thematic area explores a range of elements that spread throughout the procurement process, such as bidders’ access to procurement-related information, the clarity and comprehensiveness of the procurement documents, the qualification of bid evaluation committee members, the bid selection criteria used, the way governments deal with cases of sole proposals, and the restriction on negotiation during the award phase. The recognized good practices that could be drawn from the areas covered in the procurement of PPP projects are summarized in box 3.

Box 3. Good practices in the procurement of PPPs. Good practices which help to ensure fair competition and transparency during the PPP procurement process are:

- The bid evaluation committee members meet minimum technical qualifications;
- The procuring authority publishes the public procurement notice online;
- The procuring authority grants at least 30 calendars days to potential bidders to submit their proposals;
- The tender documents detail all the stages of the procurement process; Assessing Government Capability to Prepare, Procure and Manage PPPs;

- Potential bidders can submit questions to clarify the public procurement notice and/ or the request for proposals and the answers are disclosed to all potential bidders;
- Bidders prepare and present a financial model with their proposal;
- The procuring authority evaluates the proposals strictly and solely in accordance with the evaluation criteria stated in the tender documents;
- The procuring authority follows a specific procedure in the case that only one proposal is submitted to guarantee *value for money*;
- The procuring authority publishes the award notice online;
- The procuring authority provides all bidders with the results of the PPP procurement process including the grounds for the selection of the winning bid;
- Any negotiations between the selected bidder and the procuring authority after the award and before the signature of the PPPs contract are restricted and regulated to ensure transparency;
- The procuring authority publishes the signed PPPs contract online”.(93)

It is clear that PPP laws in Egypt, Dubai and Kuwait have implemented most of the above-mentioned procedures suggested by the World Bank PPPs Benchmarking Report in 2017.

- 3- Only about 15% of the world economies have an issue with sole bidders being regulated with greater detail. In those economies, the law mandates a special procedure that needs to be followed before awarding PPP projects. This is the case, for example, in Egypt, where the regulatory framework specifies the conditions and process for accepting sole bids. A single bid may be accepted through a decision by the competent authority based on the recommendation of the bid evaluation committee, after the approval of the Supreme Committee for PPP affairs, if the public interest does not allow for retendering procedures, or if retendering would be futile, and if the sole bid is technically acceptable and meets the specifications of the tender.(94) As the OECD recommendation states, governments should use competitive tendering and limit the use of exceptions and single-source procurement. Competitive procedures should be the standard method for conducting procurement as a means of driving efficiencies, fighting corruption, obtaining fair and reasonable pricing

(93) *Benchmarking Public-Private Partnership Procurement, op. cit.*, p. 32.

(94) *Ibid.*, pp. 35, 36. The report refers to the situation in Nigeria: “Similarly, in Nigeria, although the regulatory framework allows for direct negotiation with a sole bidder, it requires the procuring authority to ensure that the bid is technically and financially advantageous compared with market prices and to include, in the record of procurement proceedings, a statement of the grounds for its decision and the circumstances justifying the single-source procurement”.

and ensuring competitive outcomes. If exceptional circumstances justify limitations to competitive tendering and the use of single-source procurement, such exceptions should be limited, pre-defined and should require appropriate justification when employed, subject to adequate oversight taking into account the increased risk of corruption, including by foreign suppliers.(95)

- 4- In some economies, procuring authorities can also use a “competitive dialogue” procedure, which involves more extensive engagements with two or more bidders as they prepare their proposals. In this procedure, bidders submit technical proposals, which are then subject to feedback and discussion with the procuring authority. These discussions allow them to align their proposals with the authority’s needs before they submit a final proposal. In 45% of the surveyed economies, competitive dialogue either is allowed by law or takes place in practice. The latter case can be seen in Bangladesh, Canada, Jamaica, Myanmar, and the United States. Even where competitive dialogue is possible, its content and results are not always disclosed to all potential bidders, as in Egypt, where there are no requirements for such disclosure of information.(96) The OECD Recommendation of the Council on Public Procurement pointed out that the government should engage in transparent and regular dialogues with suppliers and business associations to present public procurement objectives and to assure a correct understanding of markets. Effective communication should be conducted to provide potential vendors with a better understanding of the country’s needs, and government buyers with information to develop more realistic and effective tender specifications by better understanding market capabilities. Such interactions should be subject to due fairness, transparency and integrity safeguards, which vary depending on whether an active procurement process is ongoing. Such interactions should also be adapted to ensure that foreign companies participating in tenders receive transparent and effective information.(97)
- 5- According to the OECD Recommendation of the Council on Public Procurement, Arab States should ensure that procurement officials meet high professional standards for knowledge, practical implementation and integrity by providing a dedicated and regularly updated set of tools, for example, sufficient staff in terms of numbers and skills, recognition of public procurement as a specific profession, certification and regular

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(95) OECD, *Recommendation of the Council on Public Procurement*, *op. cit.*, p. 8.

(96) *Benchmarking Public-Private Partnership Procurement*, *op. cit.*, p. 37.

(97) OECD, *Recommendation of the Council on Public Procurement*, *op. cit.*, p. 9.

trainings, integrity standards for public procurement officials and the existence of a unit or team analysing public procurement information and monitoring the performance of the public procurement system. It is suggested that Arab countries should provide attractive, competitive and merit-based career options for procurement officials as this is of fundamental importance, and as it promotes the national and international good practices in career development to enhance the performance of the procurement workforce.(98)

- 6- OECD Recommendation of the Council on Public Procurement advises to harmonise public procurement principles across the spectrum of public services delivery, as appropriate, including for public works, public-private partnerships and concessions. When delivering services under a wide array of arrangements with private-sector partners, adherents should ensure as much consistency as possible among the frameworks and institutions that govern public services delivery to foster efficiency for the government and predictability for private-sector partners. It is clear that Arab PPP legislation eliminates the application of the States' procurement legislation in Egypt, Kuwait and Dubai and applies the current promulgated PPP legislation.(99)
- 7- It is suggested that in Arab PPP legislation award procedures should insist upon using technologies which are friendly to the environment. The transfer of technology during recent decades is playing a significant role in facilitating the cultural and legal globalisation process. It allows the application of new techniques in public procurements in PPP. Furthermore, international public works agreements nowadays play an important role in spreading environmentally friendly technologies from developed States to developing nations.(100) Environmental legislation stipulations currently tend to be an integral and compulsory part of tender documents. Hamilton pointed out an example in Canada (Vancouver city efforts to reduce emissions in 2001) where there was

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(98) *Ibid.*, p. 11.

(99) *Ibid.*, p. 13.

(100) Methane is of special concern since it generates a global warming effect 23 times that of CO<sub>2</sub>. For details on the role of PPPs in mitigating climate change and increasing FDI, see G. HAMILTON, "FDI – the Global Crisis and Sustainable Recovery", Working Paper for Public Private Partnerships, and *id.*, "FDI as a Means of Securing a Sustainable Recovery", paper submitted to the Fourth Columbia International Investment Conference, Vale Columbia Centre, Columbia Law School, Columbia University, 5-6 November 2009. For more information, see also J.D. SACHS, *Common Wealth 'Economics for a Crowded Planet*, London, Penguin Books, 2008, Chap. 4, "Global Solutions to Climate Change", pp. 84-114. See also [www.globalwarmingart.com/wiki/Image:Mauna\\_Loa\\_Carbon\\_Dioxide.png](http://www.globalwarmingart.com/wiki/Image:Mauna_Loa_Carbon_Dioxide.png); C. BOVIS, "Editorial", *EPPPL*, 1/2010; *id.*, *EC Public Procurement: Case Law and Regulation*, *op. cit.*; M.A.M. ISMAIL, "Legal Globalisation and PPPs in Egypt", *op. cit.*; *id.*, *Globalization and New International Public Works Agreements in Developing Countries*, ch. 4, *op. cit.*

a private partner who financed, designed, built, owned and operated a landfill and a 2.9 kilometers pipeline to take gas from the landfill to a nearby agricultural complex, where they built a common power generating plant. The latter plant was built by the private partner to generate electricity to supply 5000 homes and to reduce carbon dioxide emissions by approximately 200,000 tons per year (emission of about 40,000 cars).

- 8- On-line bidding systems are not fully deployed in Arab countries, however, using technology in award procedures is growing as it is one of the tools of the current legal globalization phenomenon in Arab countries. It is suggested that using fully automated systems in on-line bidding is one of the guarantees to achieve best practices in award procedures particularly maintaining objectivity, integrity, and avoiding bureaucracy.
- 9- A fundamental question arises regarding Articles 8 and 9 of the Kuwaiti PPP legislation of 2014: Can executive regulations stipulate or impose new award procedures' rules which are not existing in the Kuwaiti PPP legislation of 2014? Is this a matter of unconstitutionality pursuant to the Kuwaiti constitution? Executive regulations may provide details, procedures only within the legislative framework stipulated in the Kuwaiti PPP legislation. For instance: can executive regulations stipulate award evaluation criteria which do not exist in legislation? Can executive regulations add to the award evaluation criteria which are stipulated in legislation?(101) The question of unconstitutionality remains unanswered!
- 10- As the main focus in this chapter is on the award procedures, it is also of fundamental importance to refer to the fact that there is an innovation in substantive rules in PPP legislation which is remarkable in Egypt, Dubai and Kuwait as it aims to maintain financial equilibrium during contract performance and until final completion of the project. It is a new and inventive step towards the liberalization of the PPP transactions from the administrative contracts' *clauses exorbitantes*. (102)

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(101) See M.A.E. BANA, *The Judicial Review Upon the Constitutionality of Regulations*, Cairo, Dar Nahdah el Arabia, 1992.

(102) As this chapter deals with award procedures in PPP Arab legislation, it is appropriate to refer, in a very brief way, to the fact that PPP Legislation in Arab countries has unique innovation in contract price: The Egyptian PPP legislation in Art. 8 permits the contracting parties to stipulate in the contract that they can amend the contract to maintain financial equilibrium (the law pointed out to the unforeseen circumstances and if there are any new legislation which may violate financial equilibrium). Art. 31 of the PPP legislation of Dubai stipulates that in case of unforeseen circumstances, the contract can be amended to promote financial equilibrium. Art. 36 of the PPP legislation of Kuwait pointed out that

- 11- Direct contracting in Dubai PPP legislation is of a great concern, as it violates equality, objectivity and fair competition principles.

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the amendment of the Partnership Agreement may be agreed upon in accordance with the principle and the rules provided for under the agreement, if unforeseen circumstances occurred after the conclusion of the Partnership Agreement, including amendments to the laws in force at the time of conclusion of this agreement and leading to a financial imbalance of the agreement. PPP legislation in Egypt, Dubai and Kuwait contains provisions to maintain financial equilibrium during performance and until the final completion of the contract through contractual mechanisms and without need to start litigation or arbitration. PPP legislation in Egypt and Kuwait contains provisions to maintain stabilization for the price against changes of law during contract performance and until final completion. It is appropriate to refer, briefly, to the profile of innovation in some substantive issues. This issue is relating directly to contract price and the new mechanisms by which contractors can guarantee that the contract price shall not violate their economic expectations during performance and until the end of the project. PPP agreements are complex long-term agreements and price value has to be stable during the contract duration and until the end of performance. Contract price, generally, has become nowadays a dynamic process rather than a static process as in the past and in the light of the traditional theory of *Le contrat administratif*. In public works agreements as it is in most traditional administrative contracts, it is suggested that review to contract price should be on a monthly basis in order to update the value of payments and to face the rapid change in raw materials prices in the Egyptian markets. For instance, in the first month of performance, the first certificate equals £E100,000, meanwhile, the true value of the 19th or the 20th certificate (assuming that each certificate equals £E100,000) is £E118,000. The current depreciation of the Egyptian Pound caused fundamental unpredictability to contractors with the State. Following this concept, it is clear that there is an essential need to update the value not the price. (*i.e.* the true value of the Egyptian pound in month zero equals £E1, while it equals £E0.78 in month 36). It is suggested that currency units at the time of contracting should equal the same units at the final completion date of the project.

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**CHAPTER 22**  
**Autonomy and Innovation**  
**in Italian Regional Procurement:**  
**the Sicilian Case**

BY

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***1. Regional Contracts and Competition***  
***from a European Perspective***

This chapter explores the correlation between the European legal system and the Italian regional system. The principles of open market and free competition allow the European law to remove barriers and other forms of discrimination in accessing the EU markets, prescribe the requirements for information dissemination, prohibit State aids, and apply sanctions for unfair competition in every legal system.

Flexibility characterizes the model of European law. The national, regional laws and other local regulations can either provide services through direct public management or adopt privatization or liberalization. The EU sets the minimum requirements by which these choices may be exercised, though it allows enough space for organizational structure.

The relevance of flexibility in public procurement is emphasized in the 2017 Public Procurement Strategy of the EU Commission, which states that “the new generation of public procurement directives, adopted in 2014, provides a framework for procuring in a more flexible way” by simplifying the awarding procedures and improving the access of SMEs to the public procurement sector.(1) The overall objectives of the 2014 EU Public Procurement Directives (EU Directives) are to obtain better value for public money and deliver better outcomes for citizens while promoting other public policy objectives to increase the efficiency of public spending. Moreover, the EU Directives have stronger provisions on integrity and transparency with an ultimate target of fighting

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(1) EU Comm., “Making Public Procurement work in and for Europe”, COM/2017/0572 final, 3 October 2017.

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corruption and fraud.(2) Interestingly, even the EU Court of Justice has frequently reaffirmed the possibility for public authorities to deliver in-house services instead of contracting out services, an option that is not ‘strictly’ pro-competitive.(3)

In particular, the EU Treaty recognizes the authority of the States to participate in the exercise of public powers.(4) It provides that for public entities it is not mandatory to outsource their services, but, if they decide to turn to the market, they will have an obligation to respect the principle of competition. Consequently, the decision to choose between outsourcing services to economic operators or providing them through an in-house service is a free choice by the public administration, subject to the limitations set by domestic law, *i.e.* those set by general and applicable rules, including administrative principles of efficiency, economy and effectiveness.(5)

In fact, the flexibility in the EU Directives can be seen in the promotion of innovations in public procurement.(6) Flexibility has already paved the way for the introduction of new public procurement procedures and techniques such as “competitive procedure with negotiation” and “innovation partnership”. Public officials have shown a growing preference for negotiated procedures immediately after the publication of either a call for competition for competitive procedure with negotiation or a contract notice for an innovation partnership. In both cases, the EU Directives point up the need for greater attention to flexibility, especially in procurements involving complex requirements.

Flexibility raises the need for an exchange of knowledge and experience among the contracting authorities and economic operators, always assuring the respect of the competition principle.(7)

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(2) *Ibid.*, p. 3.

(3) E.g.: EU Directive 2014/24, recital No. 5.

(4) The EU Treaty refers to the two principal treaties on which the EU is based: (1) the Treaty on European Union (TEU, Maastricht Treaty, effective since 1993) and (2) the Treaty on the Functioning of the European Union (TFEU, Treaty of Rome, effective since 1958).

(5) R. CAVALLO PERIN, *Paper to the Conference “Public procurement: innovation and rationalization. Aggregation and European cooperation strategies in the new Directives”*, Council of State, Rome, 14 May 2014, pp. 36 and ff.; S. Ponzio, “Joint Procurement and Innovation in the new EU Directive and in some EU-funded projects”, *Ius Publicum Network Review*, No. 2/2014; C.H. BOVIS, *EU Public Procurement Law*, Cheltenham, Edward Elgar, 2007, p. 72.

(6) P. TREPTE, *Regulating Procurement. Understanding the Ends and Means of Public Procurement Regulation*, Oxford, OUP, 2004.

(7) W. RHODRI, “Modernising the EU public procurement regime. A summary of the key changes to the public sectors”, in *PPLR*, 1/2014, pp. 18-28; R.H. GARCIA, *International public procurement: a guide to best practice*, London, Globe Law and Business, 2009.

## ***2. The Coexistence of a National Legislation with the System of Regional Competencies in Public Procurement in Italy: The Sicilian Case***

In Italy, the State has the exclusive legislative authority in regulating competition, especially during the public contracts award phase.<sup>(8)</sup> Under the previous legislative framework, Regions had filed claims before the Italian Constitutional Court to assert their authority in design and planning public procurement procedures and strategies, rule on contracts below threshold and exclusion of abnormally low tenders.<sup>(9)</sup> Interestingly, the Italian Constitutional Court ruled only on the limited discretion of the Regions in choosing the composition and functions of the jury.

Nonetheless, the principles contained in the delegating Law for the implementation of the 2014 EU Directives strengthen the provisions in the Italian Public Contracts Code (IPCC), which recognize the exclusive legislative competence of the State to address 'competition issues'.<sup>(10)</sup>

The 2016 Italian Public Contracts Code therefore confirms the choice that was already outlined in 2006, and establishes the dividing line between the State legislative power and the regional regulatory powers resulting in a rigid separation regarding areas of intervention between the State and the Regions. The distinction between regions with ordinary statutes and regions with special statutes, however, is not relevant in matters within the exclusive legislative competence of the State, such as competition. The State's requirements for the 'protection of competition' (e.g., the rules relating to the selection and award criteria or the regulation on abnormally low tenders) preclude all regions from setting any policy that may alter the rules of EU market functioning.

The Sicily Region is among those regions with a special statute, which affirms that the exclusive competence of the Region must be exercised within the limits established by the Italian Constitution, the principles of the national legal system and the international provisions.<sup>(11)</sup> Reference should therefore be made to the Constitutional provision regarding respect for international obligations, which can also be traced back to the EU general principles and the provisions contained in the EU Treaties.<sup>(12)</sup> However, the respect for the

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(8) It. Const., Art. 117, par. II.

(9) The 2004 EC public procurement directives were implemented in Italy with the Legisl. Decr. No. 163 of 2006; It. Corte Cost. No. 221 of 2010; It. Corte Cost. No. 401 of 2007; It. Corte Cost. No. 160 of 2009.

(10) It. Law No. 11 of 2016, Art. 1(6); legislative Decree No. 50 of 2016.

(11) Sicilian Statute, Art.14.

(12) It. Const., Art. 117, par. I.

EU principle of free competition (*i.e.*, the principle that guarantees European freedom) points out the limits in the exercise of the Region's exclusive legislative competence.

As regards the specific sectors, contracting authorities which are framing public contracts must consider that the provisions therein are aimed at avoiding any type of behaviors leading to distortion of the competition rules. Preference must be given to liberalization of the market. The rules involving the phases prior to the conclusion of the contract must be specifically designed to ensure 'competition for the market.'

The regions with special statutes can exercise an exclusive legislative competence in the implementation of the rules on public evidence administrative procedures. However, also in this case, they must respect the principle of fair competition in order to preserve the EU's freedoms, and ensure adherence to the provisions of the IPCC, which directly implement the European Directives on public contracts throughout the public procurement cycle (*i.e.*, from the award phase until the execution of the contract).

In doing so, these regions encounter a limit on their legislative competence, and are likewise precluded from adopting a discipline different from the national one.

Notwithstanding, and in case of conflict between the national and the regional laws, the exclusive legislative competence of the Sicilian Region in public contracts implies the prevalence of regional law over the national one. Although the law covering the exclusive competence of the Region mandates the application of the new Code of Conduct to Sicily, it should not contradict the law covering the Regional agreements on public contracts.(13)

The Regional Law has amended the previous rules on the award procedures, based on a lowest price award criterion, that are not of cross-border interest and are below the European thresholds.(14) Under the previous rules, contracting authorities had the discretion to provide for the automatic exclusion of abnormally low tenders, calculated according to predefined criteria. According to this rule, the identification of the thresholds led to the automatic exclusion of some tenders that were considered abnormal. According to the regional provisions, this system guaranteed the fair access of companies to the public procurement market, resulting in the possible improvement of competition. The Italian Government contested the aforementioned provision, resulting in a decision ascertaining its constitutional legitimacy. According to the Italian Ministry of Infrastructure and Transport, the mathematical mechanism provided by the regional automatic exclusion system was inadequate because it

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(13) Regional Law No. 8, 17 May 2016, Art. 24.

(14) Regional Law No. 14 of 2015.

has resulted in a substantial variation in the number of tenders that are excluded automatically. By the end of 2015 (or until 31 December 2015) the regulation on automatic exclusion had lost its effect, and the legislation returned to the pre-existing situation.(15)

As a substitute for this provision, public contracts with an estimated value of over one million euros will be awarded using the criterion of the most economically advantageous tender (MEAT), although this may result in excess discretion by contracting authorities.

In this case, it must be considered that a rigidly automatic system of awards is suitable to meet public interests only if the public administration can clearly identify in advance the expected performance; otherwise, the danger of obtaining a weak performance is very high. A rigid automatic system of award is possible only in public contracts with very simple performance requirements, and not in complex and complicated contracts.

The automatic system of award is typically based on the lowest price offered by tenderers and, more often, this price does not correspond to the best value for money for the contracting authority, so the expected success in advancing public interest through an automatic system of award based on lowest price remains low.

Moreover, the subjective use of the authority or ‘power’ to award public contracts is sometimes regarded as a criminal behavior. Therefore, it is important to examine the extent of the repeal of the provision that requires the submission of anti-mafia certifications by the members of the governing body and the board of statutory auditors of the tenderers/candidates in award procedures.(16) Nonetheless, contracting authorities have the discretionary power to implement the IPCC with the “admitted” amendments.(17)

Contracting authorities in Sicily have used their competences to facilitate a more efficient and faster award of public contracts. They had secured architecture and engineering services based on clear and transparent rules.They also relaunched a two-level competition as the best tool in promoting the quality of architectural designs.

(15) Regional Law No. 8 of 2015.

(16) Regional Law No. 12 of 2011, Art.17.

(17) It has issued the Ass. Decr. of Sicily 5 December 2018, No. 30/GAB which contains the standard notices that the contracting authorities / entities, operating in the territory of the Sicilian Region, must use in design competitions and assignments of services of architecture and engineering (SAI). These rules implementing Art. 7 of the Regional Law Sicily 12/2011, Discipline of public contracts relating to works, services and supplies. The forms must be used by all the Contracting Authorities and Entities of the Region. With the decree signed on 5 December 2018 by the Regional Department for Public Works of the Island, the standard calls come into force, with general application to all the Sicilian public administrations.

In particular, if the design concerns works of specific architectural interest, contracting authorities, in addition to resorting to internal expertise, may ban competitions of different types.(18)

The regional standards distinguish among: 1) one-level design competition, aimed at the purchase of a technical and economic feasibility project; 2) two-level design competition, which in the first degree acquires notional proposals and in the second a technical and economic feasibility project; 3) two-stage design competition, aimed at the purchase of a technical and economic feasibility project in the first phase and of a definitive architectural project, with an in-depth analysis of a technical and economic feasibility project for the structural part and plant engineering in the second phase; 4) competition of single-stage ideas, for the purchase of notional proposals to be subsequently developed with the three levels of design; 5) competition of two-phase ideas, aimed first at the purchase of notional proposals to be selected for admission to the second phase, which instead aims at the purchase of a definitive project at an architectural level, with an in-depth analysis of a project's technical and economic used for the structural and plant engineering stage.

The Regional rules also distinguish between the services of architecture and engineering for less than 40 thousand euros, the direct assignment may be used. For the award of services contracts with an amount between 40,000 – 100,000 euros, the negotiated procedure is allowed. For services contracts of an amount exceeding 100,000 euros, an open or restricted procedure is required.(19)

To avoid overlapping between similar procedures, the Sicily Region developed three standard models of contract notice, consisting of an outline for the selection criteria to be used, depending on the procedure, in ideas and contest.

For the architectural and engineering services, nine models have been developed to be used as an exploratory notice or invitation letter based on the amounts of the contracts to be awarded.

Sicily's decree also elaborates on the guidelines on the application of standard contract documents. Chapter 1 identifies the main preparatory activities for a design contest and competitions for ideas or an award of architectural and engineering services. In chapters 2 and 3, the insolvency procedures are described. Chapter 4 contains the complete standard contract documents and references to the current legislation and of information useful to the public officials in charge of the award procedure.(20)

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(18) As stated in Decr. No. 30 of 2018.

(19) Decr. No. 30 of 2018.

(20) The aforementioned notices have been published, in editable format, on the home-page of the Web site of the Regional Technical Department of Infrastructures and Mobility of the Sicilian Region – Section 'Gare', which calls for Services in Architecture and Engineering. The Regional Technical

Calls for tenders refer to the aforementioned guidelines of the Italian Anti-corruption Authority (ANAC).(21)

The Sicily Region launched the aforementioned standard contract documents for design contests and for architecture and engineering services in order to open the market, streamline the procedures for more transparency in the assignments, and restore centrality to the quality of the projects.

The standard contract documents of the Sicily Region provide a minimum imposition of economic-financial requirements. They replaced the old and excessive selection criteria requested for participating in a design contest (e.g. the economic and financial standing, a significant turnover of the employees of the professional structure, and the possession of a mandatory insurance).(22) This is one of the elements that was introduced by the standard contract notices to break down that wall, erected by previous rules that did not give due importance to the quality of the project, which progressively precluded the assignment of public contracts to small-medium professional firms (which in the country make up more than 90% of the market), reserving the procurement market only to economic operators already entrusted with large projects.

The novelty lies in the fact that in the standard contract documents approved by the Region, the goal is to open the competitions to new economic operators (even if they do not have large professional structures, with significant economic-financial and technical-organizational requirements) which may offer quality projects.

The standard contract documents adopted in Sicily rely on the assumption that the selection criteria can be demonstrated by the awardee, after the

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Department will constantly update the published standard notices, in relation to the evolution of the current regulatory framework. A Guide to the use of the standard tenders was also published, to be used for the estimated amount of the consideration and the procedures adopted, in compliance with the Italian Public Contracts Code, which is made up of four Chapters: – Chapter 1 identifies the main preparatory activities for a design or idea competition or an ordinary assignment of Architectural and Engineering Services; – Chapter 2 describes the bankruptcy procedures (referred to in Art. 152, 153, 154, 155, 156 Italian Public Contracts Code, Legis. Decr. No. 50 of 2016, Design and ideas competitions; – Chapter 3 describes the ordinary procedures of assignment (Referred to the Italian Code of public contracts, Legis. Decr. No. 50 of 2016, Art. 157, Assignment of architectural and engineering services). In Chapter 4 the Announcements of competitions are listed (with Models A1-C, A2-C and A3-C, depending on whether they are one-to-one or two-degree design competitions or one-level ideas competition) and the Type calls Services of Architecture and Engineering (Model from B1-SAI to B9-SAI, in relation to the estimated amount, which varies from an amount lower than 40,000 euros to an amount equal to or greater than 100,000 euros, and to the procedures adopted). It is also specified that the B1-SAI and B2-SAI models are used only in justified cases where the contracting authority can not resort to the Single Register, established at the Regional Technical Department, pursuant to Art. 12 L.R. Sicily No. 12 of 2011, while the B4-SAI model reproduces call for tender no.3 drafted by ANAC and approved by the same Authority with resolution of the ANAC No. 723 of 2018.

(21) Legis. Decr. No. 50 of 2016, Art. 3, par. 1.

(22) Presid. Decr. No. 137 of 2012.

award procedure.<sup>(23)</sup> This is an important step to refocus the award on quality and innovation of the project and no longer on turnover, thus re-launching the importance of assessing quality in the execution of public works. On the other hand, it is a clear sign of a reversal of the political tendency to centralize the organization of the public administration.

In this perspective, the public administration assumes the role of a control room for programming the efficient use of public funds aimed at financing and relaunching the assignment of architectural and engineering services to innovative economic operators. The role of public officials is enhanced because they take a central position in the planning and control of the entire public procurement works cycle, fighting corruption too.

### ***3. The Aggregation of Public Procurement in Sicily***

During recent years new organisational models for aggregation of purchases especially in the health sector have been settled. The aims are savings, improvement in the quality of the services and enhancement of innovation. The heterogeneity of the models implemented at the regional level is explained by the specific characteristics of the territory in which the different models of aggregation was experienced.

In a complex sector such as healthcare, the challenge is to improve the organization while recognizing the patient's centrality, and streamlining the bureaucratic-administrative processes to improve the effectiveness, efficiency and quality of service. The process of aggregation of purchases is identified as the first fundamental element of a wider project of re-organisation of the entire supply chain. The main advantages obtained with the reduction of the costs of the administrative staff (involved in the purchase process) and the reduction of the costs of acquisition and management of goods and services (if coordinated centrally) lead to the obvious goal of achieving efficiencies through economies of scale. It is believed that the centralization of purchases should trigger a virtuous circle aimed at changing the entire supply chain in order to unify warehouses, order offices, invoice settlement, and asset identification management, while avoiding the duplication of local activities and consequently reducing the costs of service.

Techniques and instruments for electronic procurement, aggregated procurement and the possibility of signing framework agreements were tools

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(23) Introduced by Art. 154 par. 5 of the Italian Public Contracts Code, Legis. Decr. No. 50 of 2016.

already provided by the EC 2004 Directive on public procurement.(24) Among these tools, aggregation of purchases and different models of joint procurement pointed out the best results in terms of efficiency.

The main goals of aggregation of purchases in the public sector are: 1) economies of scale for the reduction in the unit cost of purchase of goods or services achieved for significant savings on the basis of auctions, combined with a reduction of transaction costs, such as those related to publications, organization costs, etc. (economic-financial impact); 2) more efficient use of professionals resources of the public administrations (organizational impact); 3) streamlining the process to improve not only efficiency but also effectiveness (strategic impact).

The Sicilian provisions identified the organizational model for the Sicilian Regional Health System, which included planning the purchases of goods and services and developing and rationalizing hospitals' activities within the network.(25) This includes the aggregation of Healthcare Facilities in two territorial areas, western and eastern, and the identification of a management body for each area, called the Committee, composed by the general managers of the Health Authorities of each area. The strategy adopted by the Sicily Region consisted of identifying a leading public entity for each sector, according to the 'lead buying group' methodology, based on a logic of specialization on specific macro-categories of primarily identified goods. The award procedure was carried out on a regional level for products with a high degree of standardization (drugs, vaccines, insurance services) of the goods/services.

The 2016 IPCC is intended to pursue the rationalisation of costs and human resources involved in procurement activities and to improve professionalisation through the qualification of the contracting authorities and the reduction of their numbers.

According to these policies, in 2018, the Italian Anticorruption Authority approved a list of special central purchasing bodies (CPBs).(26) For the Sicily Region, the Single Central Regional Commission was included in the list.

Such Sicilian central purchasing body is in charge of procurement also for other contracting authorities in the sector defined by a Ministerial Decree.(27)

(24) Implemented in the Italian legal framework with the Legis. Decr. No. 163 of 2006.

(25) Region. Law No. 5 of 14 April 2009.

(26) Italian Anticorruption Authority – ANAC, Resol. No. 31 of 17 January 2018; Prime Min. Decr. of 11 November 2014, Art. 3, 4 and 5.

(27) The categories of goods and services currently in charge of aggregators are the following: 1) Needles and syringes; 2) Defibrillators; 3) Facility management properties; 4) Drugs; 5) Guardia; 6) Property maintenance and plants; 7) General medications; 8) Pace maker; 9) Hip replacement; 10) Building cleaning; 11) Assistive products for incontinence; 12) Cleaning, Laundry and Catering Services for National Health Service Agencies; 13) Sanitary waste disposal services; 14) Integrated

For the aforementioned categories and for the thresholds indicated by the national provisions, the Italian Anticorruption Authority does not release the required identification code (CIG) for the traceability of the award procedure to contracting, so it is not possible to purchase in a different way.(28)

The qualification of contracting authorities is based on the territorial areas of activity, the type and amount of the contract. In the absence of the qualification requirements, the contracting authorities make their purchases through qualified CPBs or by aggregating with other qualified contracting authorities.

The Italian case law specified that these special CPBs (in Italian *soggetti aggregatori*) are different from the central purchasing bodies constituted by Municipalities.(29) However, they can be established as simple CPBs or as a ‘Single Contracting Authority’ (in Italian *Stazione Unica Appaltante – SUA*) on the basis of Italian Antimafia provisions.(30)

The Sicily Region is operating with two Central Purchasing Bodies on its territory: the Single Central Commission of the Sicilian Region – CUCRS and the Metropolitan City of Catania. The CUCRS is primarily focused on the expenditures related to regional authorities and health authorities of the SSR, while the Metropolitan City of Catania is focused on the expenditures made by local authorities. The CUCRS provides for the procurement of goods and services.(31) While still in the start-up phase, the Metropolitan City resorts to the services provided by Consip, the national CPB.

In this context, the objective is to centralise and speed up the award of contracts of works, services and goods in the relevant sectors concerned. This means: (1) promoting the emergence of an aggregate demand for innovation and a more widespread collaboration between companies and the research system. The objectives are to finance the development of new technologies, goods and services, and to promote the technological development of economic operators, including through the support of pilot lines and actions for the early validation of goods and demonstration on a large scale; (2) supporting the purchase of services for technological, strategic, organizational and commercial innovation of companies, aimed at micro, small and medium-sized enterprises; (3) supporting economic development

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services for management of electromedical equipment; 15) Stent; 16) Vaccines; 17) Armed surveillance. Contained in the DPCM 24 December 2015 and updated with DPCM 11 July 2018.

(28) DPCM 11 July 2018.

(29) TAR Lazio, section II, 24 May 2018, No. 5781.

(30) Law 13 August 2010, No. 136, Art. 13, enforced by DPCM 30 June 2011; entities of large area according to the law of 7 April 2014, No. 56 and Legis. Dece. No. 50 of 2016, Art. 37, par. 4.

(31) Region. Law No. 9/2015, Art. 55.

of innovative solutions in processes, products and organizational formulas, and the financing of the industrialization of research results; and, supporting the technological advancement of companies through the funding of pilot projects and actions for the early validation of products and demonstration on a large scale, by companies, individually or in partnership with universities, public and private research entities, and technology districts.(4)

#### 4. Final Considerations

The 1990s Italian legislation had the aim of fighting corruption with administrative and procedural methods such as increasing transparency and reducing administrative discretionary power.(32) The introduction of the IPCCs in 2006 and 2016 did not fully solve some of the critical issues raised by the previous legislation, such as the costs arising from the rigid procedural schemes (*i.e.*, costs incurred by the private sector when using the traditional long-term procedures for award in our country). The problems encountered by some institutions that were established for pro-competitive purposes in using the said procedural schemes to promote speed and efficiency remain. These issues can be amplified by individuals who are engaged in opportunistic behavior, thereby increasing the corruption risks in public contracts(33).

The ‘qualification’ system for contracting authorities allows a reduction in the number of autonomous award procedures and encourages the monitoring activity on procurement procedures; furthermore, the professionalization of specialized and well-trained procurement officials can favor efficiency in contracting activity.

The efficient design of certain rules and the strengthening of the monitoring, activity contribute to a significant improvement pursuit of best value for money, assuring, impartiality and efficiency, favouring the participation (especially of SMEs) as well as – not to be underestimated – the fight against corruption.

The Italian legal system has introduced some instruments aimed at achieving the specific goal of public procurement rules (*i.e.* an open and

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(32) See G. M. RACCA, “De la autoridad sobre los contratos públicos a la autoridad anticorrupción: un cambio de sistema”, in *Revista Digital de Derecho Administrativo*, 181-220; G.M. RACCA, “Dall’Autorità sui contratti pubblici all’Autorità Nazionale Anticorruzione: il cambiamento del sistema”, *Dir. Amm.*, 2015, pp. 345-387; G.M. RACCA and S. PONZIO, “The new discipline on public contracts and the fight against corruption”, in *Corruption and criminal infiltrations in public procurement. Prevention and contrast tools* (L. SCOMPARIN eds), Turin, Giappichelli, 2016, pp. 109-144.

(33) Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally (G. M. Racca and C. R. Yukins eds), in *Droit Administratif/ Administrative Law Collection* (J.-B. Auby dir.), Bruxelles, Bruylant, 2014.

effective competition). The path, however, is not yet complete, as some of these instruments have to be enforced, while others are still to be implemented.

Cooperation among contracting authorities and networks of central purchasing bodies can enhance integrity, efficiency and innovation in public contracts.

**CHAPTER 23**  
**Innovation in the Public Procurement**  
**Process in Armenia:**  
**A Strategy for EU Integration**

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**1. Introduction**

The ‘2018 Armenian Revolution’(1) marked a dramatic change in the political system of Armenia with a new Government that came into power through a democratic and peaceful (non-violent)(2) revolution, and, thereafter, proclaimed the launch of wide-ranging fundamental reforms. As a major step in Armenia’s history towards a more democratic society, this revolution created a favorable atmosphere that gave fresh impetus to reforms and provided momentum for drastic transformations. The enhancement of democracy, efficient and effective governance, an increased level of transparency and accountability in public governance, the fight against corruption, free economic competition, protection of investors’ rights, and the rule of law and human rights all became high priorities of the new Government. All in all, the aim was to achieve real changes that would ensure freedom, happiness and prosperity for the citizens of Armenia.

Armenia is now in the process of designing the ‘Armenia Development Strategy 2030’ (ADS)(3) as an overarching strategy for growth of employment, development of human capital, improvement of social protection systems and institutional modernization of the public administration and governance.

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(1) The 2018 Armenian revolution (most commonly known in Armenia as #MerzhirSerzhin (Armenian: ՄերժիրՍերժին, meaning “#RejectSerzh”) was a series of anti-government protests in Armenia from April to May 2018 staged by various political and civil groups led by member of Parliament Nikol Pashinyan (head of the Civil Contract party). Protests and marches took place initially in response to Serzh Sargsyan’s third term as the prime minister of Armenia and later against the Republican Party-controlled government in general. Pashinyan declared it a Velvet Revolution (*Թաւելոյան հեղափոխություն*).

(2) A non-violent revolution is a revolution using mostly campaigns with civil resistance, including various forms of non-violent protest, to bring about the departure of governments seen as entrenched and authoritarian.

(3) [policy.asiapacificenergy.org/node/1492](http://policy.asiapacificenergy.org/node/1492).

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Through ADS, Armenia plans to provide a comprehensive set of targets and indicators that are necessary for the effective planning and monitoring of its development objectives in various areas such as economic development, culture and national identity, environmental protection and natural resources, *public and territorial administration*, education, science and innovation, human rights, rule of law and justice, defense and security, infrastructure, and social services.

This paper focuses on ADS institutional reforms in public administration, more particularly, in its attempt to exceed the 2006 benchmarks of the European countries and Baltic States, *i.e.*, the Estonian Model,(4) by the year 2012. In doing so, this paper evaluates the structural and functional reforms in Armenia's public administration system, and, identifies significant progress on transparency, accountability and efficiency in its procurement legislation. It is worth noting that the Armenian procurement legislation has been largely revised to adapt to the European Union standards.(5)

## ***2. Public Procurement System of Armenia in the context of Eurasian Economic Union***

### **2.1. Public Procurement System of Soviet Armenia**

The Union of Soviet Socialist Republics (USSR) (Russian: экономика Советского Союза),(6) commonly known as the Soviet Union, was a socialist State in Eurasia that existed from 30 December 1922 to 26 December 1991.(7) Its economy was based on a system of State ownership of the means of production, collective farming, industrial manufacturing *and* centralized admini-

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(4) The Estonian model of e-procurement might serve as one of several possible examples. Estonia has been moving towards a fully electronic public procurement environment since 2001, with 92% of procurement procedures conducted electronically in 2016. *See* chapter 18 by M. BORODINA in this book.

(5) [ec.europa.eu/growth/single-market/public-procurement\\_en](http://ec.europa.eu/growth/single-market/public-procurement_en).

(6) As part of the Soviet Union, the Armenian SSR transformed from a largely agricultural hinterland to an important industrial production center, while its population almost quadrupled from around 880,000 in 1926 to 3.3 million in 1989 due to natural growth and large-scale influx of Armenian Genocide survivors and their descendants. On 23 August 1990, it was renamed the Republic of Armenia after its sovereignty was declared, but it remained in the Soviet Union until its official proclamation of independence on 21 September 1991.

(7) The countries forming the USSR were Armenia, Azerbaijan Byelorussia, Estonia, Georgia, Kazakhstan, Kirghizia, Latvia, Lithuania, Moldavia, Russian SFSR, Tajikistan, Turkmenia, Ukraine, Uzbekistan. The Armenian Soviet Socialist Republic, also commonly referred to as Soviet Armenia, was one of the constituent republics of the Soviet Union in December 1922 located in the South Caucasus region of Eurasia. It was established in December 1920, when the Soviets took over control of the short-lived First Republic of Armenia, and lasted until 1991. It is sometimes called the Second Republic of Armenia, following the First Republic of Armenia's demise.

strative planning. State control of investment, public ownership of industrial assets, macroeconomic stability, negligible unemployment and high(8) job security characterized the Soviet Union economy.

After gaining independence,(9) Armenia ‘inherited’ an absolutely unviable economy from the Soviet system and found itself in the most difficult situation of all the countries of Transcaucasia. From the agrarian-industrial country with developed metal working, mechanical engineering, chemical, light, and food-processing industries, Armenia turned into a small state which could boast neither rich natural resources nor a favorable geographical position(10) or fertile soils.

*Until 20 years ago, Armenia’s economy was centrally planned.* It was planned in relation to the requirements of the constellation of regions and semi-autonomous Republics that made up the Soviet Union. *Armenia was an important supplier of manufactured inputs – notably machine tools – to the rest of the Soviet bloc economy and particularly to Russia itself.* This market disappeared overnight, both because the absence of competition had left key parts of what was essentially a highly protected manufacturing economy chronically unable to compete in suddenly liberalized markets, and because the precipitous decline of the Russian economy had significantly reduced the demand side of the market.(11)

*State procurement was performed by direct financing of public entities without competitive bidding, and the levels of fraud and corruption were extremely high.* (12) In 1992, the Presidential Decree “on measures for the formation of the Federal contracting system” initiated the establishment of the procurement process on a competitive basis.(13) In 1997, the next Presidential Decree on the “urgent measures to eliminate corruption and budget cuts in the organization of the

(8) H. PHILIP, *The Rise and Fall of the Soviet Economy*, London, Routledge, 2003, pp. 1-8.

(9) On 23 August 1990, it was renamed the Republic of Armenia after its sovereignty was declared, but remained in the Soviet Union until its official proclamation of independence on 21 September 1991. Its independence was recognized on 26 December 1991 when the Soviet Union ceased to exist. After the dissolution of the Soviet Union, the state of the post-Soviet Republic of Armenia existed until the adoption of the new constitution in 1995.

(10) For much of its history, Armenia has been a prisoner of its difficult geography. Situated at a strategic crossroads, it has lost out in competition with much larger regional powers and empires, and was the victim of the first genocide of the 20<sup>th</sup> century. Armenia is now at a crucial political crossroads yet again, this time with the fate of the country’s strategic orientation and domestic stability in the balance. The challenges facing Armenia are daunting, and go well beyond its dangerous over-dependence on Russia, the burden of the unresolved Nagorno-Karabakh conflict, and the enduring legacy of the Genocide. In fact, the most serious threat to Armenia is not just external but domestic. Entrenched corruption and the democratic deficit impede sustainable economic policy and sound political reform. This means that the solution is also less external, and must address deeper domestic deficiencies.

(11) UNCTAD, “Voluntary peer review of competition policy: Armenia”, United Nations, New York/Geneva, 2010.

(12) N. PAKHARUKOVA, *Public procurement system in Russia in the process of transition: Guidelines for EU suppliers*, Helsinki, Metropolis, 2014.

(13) Decr. 826 from 7 August 1992.

procurement of products for State needs,” (which was based on UNCITRAL principles) was issued.(14)

## 2.2. Innovations in Public Procurement System of Post-Soviet Armenia

The Republic of Armenia is a sovereign, democratic, social, and rule of law State. Since the breakup of the Soviet Union in 1991, Armenia has made great progress towards the liberalisation of its economy.(15) Armenia has been one of approximately 80 nations that has launched its competition systems since 2000,(16) although it remains strongly dependent on the economic health of *the Russian economy and of the EU*.(17)

To date, Armenia’s economy is characterized by a high level of market concentration, most probably due to the limited points of entry and exit for the import and export of goods, which is accompanied by *a weak customs service that leads to a significant underreporting of trade*. The geopolitical tensions have already closed two of landlocked Armenia’s most likely routes to the sea, namely, the borders with Turkey and Azerbaijan. Thus, Armenia has only one reliable and economically viable route to the sea, that is, through its border with Georgia. In addition, Armenia struggles with what is called the ‘shadow economy’,(18) which is predominantly controlled by unreported informal sector activities, most of which are done through traders or producers that are trying to evade payment of taxes and import duties.

(14) Decr. 305 from 8 April 1997.

(15) The economy of Armenia is based on 5 regions which differ in natural and economic-geographical conditions and industrial specializations. Ararat (electric power, mechanical engineering, chemical industries, manufacture of building materials, and agriculture), Shirak (textile industry, mechanical engineering; livestock), Pridebed (copper, chemical industry; agriculture, mechanical engineering), Sevan-Agstevi (electric power, livestock, grains and tobacco), and Syunig (mining industry, agriculture, hydroelectric power industry and mechanical engineering). The main industrial centre of Armenia is Yerevan, followed by Gyumri and Vanadzor.

(16) The Law of the Republic of Armenia on Protection of Economic Competition (‘the Act’) was passed on 6 November 2000. On 13 January of the following year, the State Commission for the Protection of Economic Competition of the Republic of Armenia (SCPEC) was established.

(17) Several critical background facts and circumstances affect every aspect of Armenian life. Each significantly influences the character and practice of competition law and policy and the challenges to be confronted. There are two fundamental facts of Armenia’s economic and political life. The first is its status for approximately 70 years as a Republic of the former Soviet Union. The second fundamental feature underpinning Armenia’s political and economic life is the geopolitical situation in the South Caucasus region, specifically the conflict-ridden relationship between Armenia and its eastern neighbour, Azerbaijan, and between Armenia and its western neighbour, Turkey.

(18) ‘Shadow economy’, also known as ‘informal sector’, ‘black economy’, ‘underground economy’, or ‘gray economy’, refers to activities and business transactions that occur ‘below the radar’ or economic activities that are not recorded; hence, no taxes were collected from these activities. When economists calculate the GDP (gross domestic product) of a country, they do not include the value of the transactions in the shadow economy. See, e.g. B. TUNYAN, “The Shadow Economy of Armenia: Size, Causes and Consequences”, Working Paper No. 05/02, Armenian International Policy Research Group, 2005.

Armenia's procurement legislation<sup>(19)</sup> consists of the 2005 Constitution, as amended by a 2015 referendum,<sup>(20)</sup> the 1998 Civil Code,<sup>(21)</sup> the public procurement law and other legal acts. Interestingly, public procurement in Armenia is *decentralized*, that is, the procurement of goods, works and services is delegated to procuring entities at the central, the provincial, and the local levels of government.

In 1991, Armenia had independently launched its public procurement system with transition from a centralized to a market economy. After the adoption of its new Law on Procurement (LoP),<sup>(22)</sup> *Armenia has transferred its semi-centralized procurement system<sup>(23)</sup> into a decentralized one.*<sup>(24)</sup> At the same time, Armenia has adopted a strategy of developing a unified Armenian Electronic Procurement System (ARMEPS).<sup>(25)</sup> The creation of possibilities for electronic administration,<sup>(26)</sup> particularly electronic document circulation and exchange, significantly decreases the paperwork load and saves working hours, optimizes the number of public servants and enhances their qualifications. The e-procurement system of Armenia, the 'Armenian Electronic

(19) Law on procurement RA, 16 December 2016, Art. 3, Purpose and scope of the law. "1. The purpose of the law is to ensure: a) organization of competitive, efficient, transparent, open and indiscriminate procurement process; b) formulation of unified rules for the procurement process and legal grounds for the supervision of application thereof; c) regulation and cooperation of the procurement process; d) equal rights for any person, regardless of his being a foreign physical person, organization or stateless person to participate in the procurement process, except in cases prescribed by law. e) broadening of the circle of participants and encouragement of competition between them for the purpose of signing a procurement contract. 2. The scope of this law extends to procurements made in the RA by the procuring entity. The procurement procedure outside of the RA is formulated by the RA government".

(20) Adopted through a referendum on 5 July 1995. Amendments to the Constitution of the Republic of Armenia were introduced through a referendum on 27 November 2005. Amendments to the Constitution of the Republic of Armenia were introduced through a referendum on 6 December 2015.

(21) Adopted by the National Assembly on 5 May 1998. The civil legislation of the Republic of Armenia consists of this Code and other laws containing norms of civil law. Norms of civil law contained in other laws must comply with this Code.

(22) Adopted on 22 December 2010 and effective from 1 January 2011.

(23) Per the old LoP only State government bodies or community institutions had the ability to participate in the centralized procurement system.

(24) The decentralization of procurement has substantially increased the number of stakeholders in public procurement. The private sector has continued to grow. Small, medium and large enterprises have been participating in providing thousands of items of goods, works and services under government procurement contracts.

(25) Armenia: Case Study on e-Government Procurement Development, ADB Technical Assistance consultant's report, May 2011.

(26) Armenia reported numerous e-portals introduced since the last monitoring round, including: e-civil system; e-petition; e-bankruptcy; www.azdarar.am; e-court; e-hotline; www.e-license.am; e-penitentiary; e-visa; e-consul; e-request.am; e-drafts and others. Most of these Web sites are linked to the e-government Web site e-gov.am. In addition, as discussed below, most of the tax services have been digitalized and the same process is ongoing for customs. See OECD report on 4th round of monitoring of the Istanbul Anti-Corruption Action Plan, *Anti-corruption reforms in Armenia*, pp. 91-93.

Procurement System (ARMEPS) is an affiliated system with the Ministry of Finance (MOF).(27)

The introduction of an electronic system for services provided by the State has improved the openness, accountability and transparency of the activities of the public system, while reducing the corruption risks(28) through a significant reduction of direct and personal contacts between public servants and economic operators. As a result, administration operations become more controllable by citizens, as e-procurement creates the opportunity for citizens to participate in the administration process. *The announcements on international tenders can be found on the central procurement website by following the appropriate prompts.*(29)

Despite the significant progress recorded in the sphere of electronic administration, Armenia is still far behind the European Union countries with respect to public electronic services.(30) In 2013, Armenia adopted the proposed roadmap provided in the EBRD-UNCITRAL Initiative's "Road Map for Finalizing e-Procurement Reform in the Republic of Armenia 2013-2015".(31) The purpose of the roadmap was to achieve full implementation of e-GP in Armenia by 2015. Four years thereafter, the roadmap has yet to achieve its full realization. Updates are being made from time to time.

*Considerable work has been done to bring the procurement legislation of Armenia in conformity with the UNCITRAL Model Law, GPA (WTO General Procurement Agreement) and EC Public Procurement Directives.* Despite the solid steps towards the modernization of the procurement legislation and public administration system, there are still many gaps to identify and resolve. The obvious problems, for example, which need to be primarily addressed are: *foreign bidders' lack of participation in Government tenders,* (32) *capacity building strategies,* (33) *and appli-*

(27) The PSC supports the ARMEPS functionally; and EKENG CJSC (e-Governance Infrastructure Implementation Unit) supports it technically.

(28) Introduction of the concept of beneficial ownership and registration of beneficial owners and restrictions imposed on the latter (unfortunately this concept is not extended to other areas, for example, tax and customs, which decreases the impact of its introduction) is one of the major novelties of the law. See OECD report on 3rd round of monitoring of the Istanbul Anti-Corruption Action Plan, *Armenia progress update*, pp. 88-98.

(29) [www.procurement.am/hy/page/otarerkraya\\_petutyunneri\\_koghmic\\_kazmakerpvogh\\_gnumner/](http://www.procurement.am/hy/page/otarerkraya_petutyunneri_koghmic_kazmakerpvogh_gnumner/).

(30) Armenia Development Strategy for 2014-2025 to RA Government Decree # 442 - N On 27 March 2014.

(31) [www.ppi-ebd-uncitral.com/images/stories/pdf/RA\\_Armenia\\_eGP\\_roadmap\\_6\\_March\\_2013.pdf](http://www.ppi-ebd-uncitral.com/images/stories/pdf/RA_Armenia_eGP_roadmap_6_March_2013.pdf).

(32) Recommendations: To ensure the availability of all the tender information and documents in English (tender notices, regulations, guidelines, award and etc.), keep the information updated on the official Web site.

(33) Recommendations: To create and adopt public procurement capacity building strategies by applying local resources. The adoption of the institutionalized and sustainable strategies (professional development programs, education and trainings) should start from the needs analysis,

*cation of e-procurement.*(34) The current procurement public awareness-raising and capacity-building arrangements are inadequate. Although some procurement manuals exist, they are not suitable for all procuring entities. There are a large number of procuring entities whose staff need to acquire procurement skills.(35)

SIGMA supports ongoing public administration reform in Armenia and is aimed at enhancing Armenia's capacities to comply with the requirements of EU integration and to effectively use EU support as a potential candidate(36) for EU membership.(37) The Armenian public procurement system is in the course of modernization and standardization in accordance with OECD principles. According to this vision, the main aspects of reform to be addressed are in transparency and accountability in public administration to avoid the risks of corruption and bid rigging.(38)

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identification of the targeted stakeholders, the reporting of the knowledge gap and mapping the skills needed.

(34) It is highly suggested to invest in creation and maintenance of procurement e-learning platforms aimed at enhancing the awareness of public procurement policies and procedures among all stakeholders, and improved procurement competencies of public officials. After the adoption of the strategies a comprehensive dissemination and awareness raising plan will be appropriate.

(35) The RA Government Decr. No. 99-N dated 12 February 2015 approved regulations for the qualification of procurement coordinators and continuous professional development of qualified procurement coordinators. It is envisaged that every procurement official should take the training at least once every three years. The head of the contracting authority should submit to the Procurement Support Center (PSC) a list of its employees who need to be trained. PSC then comprises groups and schedule for the trainings for that year. *See OECD report on the 3rd round of monitoring of the Istanbul Anti-Corruption Action Plan, Anti-corruption reforms in Armenia*, pp. 87-88.

(36) Despite the fact that Armenia has worked hard to improve its public procurement system there are still obvious problems which need to be addressed; without facing these core issues it will be impossible to prepare a healthy foundation for the system's reforms:

1. Design and launch capacity building programs for procurement specialists (training on legislation procedures and the donors IFIs guidelines, FIDIC procedures, contract negotiation and management, proposal writing);
2. Establish a network of professionals from different markets and different procuring entities; create a platform for data sharing, practice sharing, exchange of skills, training on case studies, interactive studies;
3. Raising awareness on EU Programmes (European Structural and Investment Funds and Horizon 2020) and offers of funding opportunities to promote joint innovation public procurement – including both Public Procurement of Innovation (PPI) and Pre-Commercial Procurement (PCP) through forums, seminars, media, etc.;
4. Design and launch procurement e-learning modules via establishing an electronic training center;
5. Identify the reasons for foreign bidders' lack of interest (such as difficulty of access to procurement documents in English) in government tenders and improve conditions for their participation;
6. Require procuring entities not to use price as the only selection criterion for standard procurement items (update the calculation methods to include both quality and price in the selection of consultants);
7. Establish off-line and on-line means to create a bridge between post-Soviet Union countries (mainly three post-Soviet countries; Georgia, Moldova and Ukraine can serve as a case study), and learn from their experience, share knowledge and skills.

(37) SIGMA and Armenia: [www.sigmaxweb.org/document/26/0,3746,en\\_33638100\\_33638200\\_44395930\\_1\\_1\\_1\\_1.00.html](http://www.sigmaxweb.org/document/26/0,3746,en_33638100_33638200_44395930_1_1_1_1.00.html).

(38) *See Recom. 17 from the Third Round of Monitoring on Armenia: Transparency and discretion in public administration*, OECD report, aforesaid, pp. 88-90.

### ***3. Capacity for Innovation in Armenian Procurement Processes through Strategic Application of Organizational Models***

#### **3.1. Trials for establishment of a partially centralized procurement system**

In February 2017, the then-Minister of Finance<sup>(39)</sup> presented to the government a program to establish a partially centralized procurement system for public procurement.<sup>(40)</sup> The Minister justified the necessity to adopt a “partially centralized procurement system” to enhance the delivery of electronic procurements and comply with the requirements on regional economic development.<sup>(41)</sup>

As already discussed, the current public procurement legislation supports a decentralized approach in public procurement;<sup>(42)</sup> that is, the procuring entities themselves arrange the procurement procedures. While the laws promote the use of the electronic procurement system, this does not include the process of contract execution as this is still done through the traditional paper-trail procurement system.

The proposed centralization encourages the use of framework agreements for goods and services with similar technical characteristics that are included in the approved list by the Government of the Republic of Armenia. The proposed centralized procurement will be done through either the Ministry of Finance or any of the State-owned institutions or a legal entity assigned by the Ministry of Finance in cooperation with all central executive bodies.<sup>(43)</sup> Like most framework agreements, the proposed framework agreement has a validity period that will be used as the basis for the determination of the prevailing market price for the goods and services covered therein. There will be a mechanism for reviewing and/or revising the active contract price to ensure that the determination of the cost estimates in the framework agreements has a positive impact in the budgets.

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(39) V. Aramyan appointed as Minister of Finance by president S. Sargsyan on 20 September 2016 in Yerevan.

(40) The Minister's speech available at <https://iravaban.net/152241.html>.

(41) Government's Resol. No. 110-A, “Action Plan for the Improvement of Armenia's Business Environment in 2016”, 11 February 2016.

(42) Art. 17 of the Law of RA on Public Procurement: Implementation of centralized procurement for the needs of customers or their separate groups may be carried out in a centralized manner according to the prescribed rules by the Government of the Republic of Armenia. Purchases by a centralized manner shall be made by the entity or legal body assigned by the Government of the Republic of Armenia, [www.arlis.am/documentview.aspx?docID=110820](http://www.arlis.am/documentview.aspx?docID=110820).

(43) According to the RA Government executive order N526 Chapter XV the organization of the procedure of the centralized procurement could be done for the needs of the State and Non-Commercial Communities, state (communal) non-commercial organizations and organizations with more than 15% of the state (ownerships are to be included) in a centralized procurement plan.

At the same time, the draft of the program suggests that in case of any procurement with an approximate value of up to 70 million drams, the 15% price preference for products from the Eurasian Economic Union will not apply due to its price implications, i.e., the procurement will have a relatively expensive price.<sup>(44)</sup> Nonetheless, the program recommends the promotion of domestic production by allowing the RA Prime Minister to authorize the adjustment of the technical specifications at the time of the procurement in order to give preference to local products.

According to the RA Government decision N526 made on May 2017, Chapter XIV on the Organization of centralized procurement for the State needs, the list of goods and services to be procured centrally is to be approved by the Government of the Republic of Armenia. Accordingly, the head of the body should approve the technical specifications, including the terms and conditions of the purchase, subject to centralized procurement, within 35 working days from the date of the formulation of the said conditions and before coordinating with all the republican executive bodies. In fact, the law likewise requires the formulation of an evaluation commission for every centralized procurement, composed of representatives from different contracting authorities that want to participate in the specific centralized procurement. The principal contract shall be valid for a period of six months, and all subsequent contracts shall be valid for a period of one year. The invitation to bid/tender must include a request to interested bidders to submit a statement declaring that they have properly executed at least one similar contract during the past three years.

In addition, decision N526 Chapter XV on the organization of the procedure for centralized procurement requires that procurements by State and Non-Commercial Communities States (communal), non-commercial organizations and organizations with more than fifty percent State ownership must be included in the centralized procurement plan.

Prior to November 1 of the preceding year, the head of the organization should submit to the authorized body (hereinafter referred to as the lead contracting authority), the purchase orders approved in accordance with the procedure defined in the technical specification of the subject matter, the maximum price per unit, the place and time of payment, the payment terms, and, where appropriate, the price to be supplied, the work to be performed, or the quality of the service to be provided and an expert opinion, including a written agreement authorizing the lead contracting authority to sign the contract award after the

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(44) According to the provisions of the Treaty on EAEU, the freedom of movement of goods, services, capital and labor, as well as implementation of coordinated or united policy in various branches of economy is provided within the Union. From 1 April 2015 in case of purchases with the volume up to 70 million AMD, the EAEU countries are given a 15% price preference while participating in public procurements of Armenia.

completion of the procurement process. The candidates for the composition of the evaluation committee must likewise be presented.

The lead contracting authority, on the basis of applications received by 1 December, prepares a procurement plan to be implemented in a centralized way. If there are five or more participating contracting authorities, each contracting authority must present one candidate in the evaluation committee, which is composed of candidates from the five organizations with the largest shares in the scope of the subject procurement. In case there are less than five participating organizations, each organization can nominate three candidates, and the evaluation committee must include candidates from all participating organizations subject to the restrictions on the maximum number of members for evaluation committee.

The representative of the organization with the largest share shall be appointed as the chairman of the evaluation committee.

Whenever possible, the procurement of goods, services and works of organizations in an administrative unit must be consolidated into a single lot, provided that all needs of the individual organizations are taken into account.

The selection of the procurement procedures shall be carried out by the lead contracting authority subject to compliance with procurement laws and procedures. In case of e-procurement, the procedures within the centralized procurement process must also be done through electronic system.

Contracts concluded as a result of centralized procurement can be found on the website of the Ministry of Labour and Social Issues of the Republic of Armenia (MLSA).(45) Currently the documents are available only in the Armenian language.

### 3.2. Possibilities for joint cross-border innovation and the EU-Armenia enhanced partnership and cooperation agreement

Taking into account Armenia's intention to accelerate its EU integration process, which in its turn includes also the current public procurement legislation and system revision, it is important to first of all analyse and evaluate the possibilities on how Armenia can benefit from the opportunities(46) on joint

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(45) Including information on the completed tenders.

(46) The main development in Armenia in the area of procurement was the adoption of the Law on Procurement (PPL) by the National Assembly of the Republic of Armenia (RA) in December 2016. The PPL is based on the UNCITRAL model law and had been drafted with the support of EU SIGMA and the European Bank for Reconstruction and Development (EBRD). According to the Government of Armenia and civil society representatives, NGOs (including Transparency International) were consulted during the drafting process and their comments were reflected in the PPL. Important features of the PPL were reviewed in the OECD report on 4th round of monitoring of the Istanbul Anti-Corruption Action Plan, Anti-corruption reforms in Armenia.

cross-border procurement under the EU 2014 Directives. The legal perspectives and Armenia's commitments and limitations as a member of the Eurasian Economic Union (EAEU) should be taken into account.

After Russia pressured Armenia to give up its potential Association Agreement and Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU in 2013, Armenia took a surprise decision to join the Eurasian Economic Union,<sup>(47)</sup> which put the relationship between the EU and Armenia into a period of 'strategic pause'. Since joining the Eurasian Economic Union, Armenia has steadily and stealthily sought to regain and restore relations with the EU, and to deepen its ties to the West more broadly. For example, the EU and Armenia re-opened negotiations on a revised and revamped EU-Armenia framework agreement in December 2015, after the launch of a so-called "scoping exercise" in October 2014 that sought to identify areas for such an agreement.<sup>(48)</sup>

The European Union's relations with Armenia are based on the EU-Armenia Partnership and Cooperation Agreement (1999), and moving forward on the new Comprehensive and Enhanced Partnership Agreement, completed in February 2017, which will create the framework for even stronger cooperation.<sup>(49)</sup> Launched in May 2009 in Prague, the Eastern Partnership (hereinafter EaP)<sup>(50)</sup> aimed at enhancing the relations between the European Union

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(47) The Eurasian Economic Union is an international organization of regional economic integration. It has an international legal personality and was established by the Treaty on the Eurasian Economic Union signed on 29 May 2014 in Astana. The Eurasian Economic Union was created on the basis of the Customs Union and the Common Economic Space of Belarus, Kazakhstan and Russia. The Customs Union has been launched since January 2010. A decision on entry into force of international agreements forming the Common Economic Space was made in December 2011. This defined the usage of the Agreements forming the Common Economic Space from January 2012 to 2015 targeting the creation of the Eurasian Economic Union. On 3 September 2013, the President of the Republic of Armenia Serzh Sargsyan declared the decision of the Republic of Armenia to join the Customs Union. The Republic of Armenia joined the Treaty on the Eurasian Economic Union signed on 10 October and the treaty entered into force on 2 January 2015.

(48) H. KOSTANYAN and R. GIRAGOSIAN, "EU-Armenian Relations: Seizing the Second Chance", CEPS Commentary Policy paper, 31 October 2016.

(49) The European Union is the leading trading partner of Armenia, with close to 30% of exports going to the EU, and is also the biggest donor in Armenia, providing an average €1 million per week, with the objective of having a clear impact on the life of citizens. Cooperation aims at supporting the country's resilience and economic development, strengthening good governance and the rule of law, improving Armenia's transport and energy links with the EU and the region, and developing stronger links between the labor market and the education system.

(50) The main goal of the EU was to create a stable, prosperous and secure eastern neighborhood, providing the eastern partners with the objective of political association and economic integration with the EU. Since the last Eastern Partnership (EaP) Summit, which took place in Riga in 2015, significant progress has been achieved in relations between the EU and its six partner countries. Association agreements, including Deep and Comprehensive Free Trade Areas with Georgia, Moldova and Ukraine, have now fully entered into force, opening new opportunities for closer cooperation on tackling key challenges, as well as economic integration and trade. Trade between the three associated partner countries and the EU has significantly increased. The implementation of these Agreements will be guided by the recently updated Association Agendas. Following a set of demanding reforms, visa-free travel to the Schengen

and the six countries participating in the initiative: Armenia, Azerbaijan, Belarus, Georgia, Republic of Moldova (hereinafter Moldova) and Ukraine.

The 5th Eastern Partnership Summit<sup>(51)</sup> with the slogan “Stronger together” was a moment to celebrate the achievements of the last two years in the EU’s relationships with its six Eastern partners and to look forward to implementing 20 deliverables by 2020 that will bring tangible benefits to citizens. In the margins of the Summit, a number of agreements were taken forward, including a new bilateral agreement between the European Union and Armenia; a Common Aviation Area Agreement with Armenia; and the extension of the EU’s Trans-European Transport (TEN-T) network to Eastern partners. This new agreement will enable the European Union and Armenia to work more closely together in order to address the challenges faced and to make the most of the opportunities available.

Negotiations for Armenia’s participation in the EU’s biggest Research and Innovation Programme Horizon 2020 were concluded in 2015 and Armenia signed the Association Agreement in May 2016. Armenian legal entities can participate in all Horizon 2020 actions funded from the 2016 budget (calls for proposals, calls for tenders, contests, JRC activities etc.) with the status of entities from an Associated Country as of the entry into force of the Association Agreement. On 21 February 2018, the European Union and Armenia signed Partnership Priorities in Bruxelles. This sets the joint policy priorities for the coming years, in line with the new EU-Armenia Comprehensive and Enhanced Partnership Agreement. The four main areas of cooperation are: Strengthening institutions and good governance; Economic development and market opportunities; Connectivity, energy efficiency, environment and climate action; Mobility and people-to-people contacts.

#### ***4. What Armenia Can Learn from other Post-Soviet Union Countries***

##### **4.1. Innovations in Georgia’s public procurement system**

Since the first Law on Public Procurement was adopted in December 1998 (N1721), Georgia’s public procurement system and legislation have been continuously developing. The current public procurement framework – the Law on State Procurement (LSP) – was adopted in 2005 and came into force on 1 January 2006. Since its enactment, the LSP has been streamlined and has

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area was put in place for the biometric passport holders of Georgia and Ukraine, in addition to that with the Republic of Moldova, in place since 2014.

(51) Took place on 24 November, 2017 in Brussels.

undergone a series of amendments. The main aims of the LSP are to ensure the rational use of financial resources; develop healthy competition in the production of goods, supply of services and construction works necessary for the State's needs; ensure a fair and non-discriminatory approach towards participants in the procurement process; assure the publicity of the process; create a unified electronic system of public procurement, and build public confidence in it. The scope of the LSP covers purchases of goods and the supply of services and construction works by contracting authorities, using funds from the State, autonomous republics or local budgets, funds of public bodies and grants or loans guaranteed by the State. Substantial parts of the procurement process are regulated by secondary legislation. Provisions regarding avoidance of conflict of interest are stipulated in the LSP.

The main responsible agency is the State Procurement Agency (SPA), an independent legal entity under public law. Between 2012 and 2014, the SPA was merged with the Free Trade and Competition Agency, based on the Swedish model and with the assistance of Swedish experts, and was renamed the Competition and State Procurement Agency. Yet later (in 2014), this agency was split again into the Competition Agency and the SPA.

Up until the end of 2010, Georgia had a highly inefficient, bureaucratic and completely opaque procurement system and the public was not able to access any government procurement documents. This was mainly because in many cases, documents were not even properly archived. Today, Georgians and others interested in government procurement can find information online including tender documentation, documents submitted by bidders, participating bidders, their bids and all signed and amended contracts. Also included on the platform is information on all whitelisted companies that have been reliable in the past, and on those that have been blacklisted and barred from bidding for public contracts for a year. The website also allows interested bidders to request clarification on tender documents. These requests are usually answered by a procurement officer on the website before any bidding starts.

The introduction of e-procurement (October 2010) through the Georgian electronic Government Procurement (Ge-GP) system is a good example of how strong political will and commitment can be critical in the context of reforming public procurement. Within a year, the State Procurement Agency of Georgia (SPA) designed, developed, and tested the e-procurement system and eventually moved to the *mandatory use* of e-procurement, fully replacing paper-based tenders. The e-procurement system, which is broadly consistent with good public procurement practices, has increased competition among suppliers. In addition, by bringing processes online, it has made the procurement system more transparent, less bureaucratic, and less discriminatory. As a result, the

system has significantly minimized corruption risks and brought substantial savings to the government and Georgia's citizens. Now Georgia is one of the few countries in the world where the need for paper-based tenders has been fully eliminated, and 100% electronic tenders were introduced within less than one year.

The reform of e-procurement is clearly one of the most effective and efficient reforms undertaken in the last decade in Georgia. The remarkable achievements of SPA have been explicitly acknowledged by different international organizations<sup>(52)</sup> including the OECD, the United Nations and Transparency International, the latter ranking Georgia as the best country among the 19 countries of Eastern Europe and Central Asia in its 2014 Corruption Perceptions Index.<sup>(53)</sup>

Transparency International (TI)<sup>(54)</sup> Georgia also launched *tendermonitorge*, a new Web site which allows the public to search, explore and monitor public procurement, and which is based on electronic data from the electronic procurement platform of the Georgian Competition and State Procurement Agency (CSPA). Anybody who detects a potential violation of the law in an electronic tender process can file a direct complaint on the official procurement website, which is then reviewed by a Dispute Resolution Board, in which TI Georgia is represented, within ten working days. This online reporting mechanism is a very innovative approach that allows the public to scrutinize public contracts and to act to stop a process, if members of the public find violations of the law.<sup>(55)</sup>

#### 4.2. Georgia's successful example for EU integration

The Association Agreement (AA) between the European Union (EU) and Georgia is a comprehensive treaty covering Georgia's political and economic

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(52) The European Parliament welcomed Georgia's new procurement system, and noted that Georgia should also serve as an example for the EU Member States in this area – The e-Procurement system implemented in Georgia may serve as a good example for Asia and other Pacific countries. The countries, which have not yet introduced e-Procurement system, are particularly interested in the reforms implemented in Georgia as the ADB has noted. In 2012, the Ge – GP was awarded with the United Nations Public Service Award (UNPSA) in the category of "Preventing and Combating Corruption in Public Service". According to a recent survey published by the EBRD (EBRD 2012 Regional Public Procurement Legislation Self – assessment), the Ge – GP was recognized as the most advanced e – procurement platform among the Bank's 26 client countries.

(53) The World Bank, Georgia: An E-Procurement Success.

(54) A large amount of the taxpayers' money is spent on public procurement. Finances used for public procurement are in essence the taxpayers money spent on effective governance. Therefore, the system and policy for public procurement should be transparent, economically purposeful and efficient. As a result, they will provide high quality goods and services for effective functioning of State institutions, as Transparency International has noted.

(55) Georgia's E-procurement platform, 14 June 2013.

relationship with the EU. The trade-related content establishes a Deep and Comprehensive Free Trade Area (DCFTA), which is an important part of the overall Agreement.

The Agreement was signed on 27 June 2014, and has subsequently been ratified by Georgia, the European Parliament and all 28 EU Member States. While most of the economic content of the Agreement has been provisionally in force since 1 September 2014, its definitive and complete entry into force took place on 1 July 2016.

The political and economic objectives of the Agreement are fundamental for the future of Georgia as an independent and secure European State.

The political purpose is to deepen the realisation of Georgia's 'European choice' and its relations with the EU. Membership in the EU is not pre-figured in the Agreement, but neither is it excluded in the longer run.

The EU-Georgia Association Agreement includes in Title IV a dedicated Chapter 8 on public procurement, comprising Articles 141-149 and an associated Annex XVI. Essentially, the Agreement provides for effective, reciprocal and gradual opening of the public procurement markets of the EU and of Georgia.

Public procurement in the EU and Georgia is of great economic importance. It accounts for around 18% of GDP in the EU and offers an enormous potential market for Georgian companies. The *Deep and Comprehensive Free Trade Areas (DCFTA)* (56) provides for the gradual and reciprocal liberalisation of the parties' public procurement markets under the strict condition that Georgia implement the EU's key public procurement rules. The EU and Georgia envisage mutual access to their respective public procurement markets on the basis of the principle of national treatment at the national, regional and local levels for public contracts and concessions in the traditional sectors as well as in the utilities sector.

Opening of public procurement markets is linked to gradual progress in the approximation of the Georgian public procurement legislation with the EU public procurement *acquis* accompanied by institutional reform and the creation of an efficient public procurement system based on the principles governing EU public procurement. The process of approximation includes methods and techniques for transposing the EU legislation into national law, its incorporation into the national legal system and the process of implementation.

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(56) The Deep and Comprehensive Free Trade Areas (DCFTA) are three free trade areas established between the European Union, and Georgia, Moldova and Ukraine respectively. The DCFTAs are part of each country's EU Association Agreement. They allow Georgia, Moldova and Ukraine access to the European Single Market in selected sectors and grant EU investors in those sectors the same regulatory environment in the associated country as in the EU.

The EU envisaged the ‘indicative time schedule’ for institutional reform, legislative approximation and market access. This time schedule foresees five phases for Georgia to implement the provisions of the EU’s public procurement directives, and the specific market access that Georgia and the EU will grant to each other. The market access provided in each phase will imply that the EU shall grant access to contract award procedures to Georgian companies – whether or not established in the EU – pursuant to EU public procurement rules under treatment no less favourable than that accorded to EU companies, and vice versa.

Although this schedule envisages a simultaneous market opening, it has to be noted that Georgia’s public procurement market was already open for EU companies before the DCFTA entered into force, and that EU companies can therefore already participate in Georgia’s procurement market.

On the EU’s side, the indicative time schedule foresees that each phase shall be evaluated by the Trade Committee and the EU’s market access will take place only after a positive assessment by this Committee, which will take into account the quality of Georgia’s legislation as well as its practical implementation.

Prior to the beginning of legislative approximation, Georgia must submit to the Trade Committee a comprehensive roadmap for the implementation of the requirements of the procurement chapter (hereafter referred to as the ‘public procurement roadmap’), covering all reforms in terms of legislative approximation and institutional capacity building.

The EU public procurement directives included in the DCFTA have meanwhile been replaced in the EU by a new legislative package. In 2011, the European Commission proposed the revision of Directive 2004/17/EC(57) and 2004/18/EC,(58) as well as the adoption of a directive on concession contracts. This legislative package was adopted in February 2014 and the Member States had to transpose the new rules into their national laws by April 2016 (Dir. 2014/24/EU(59) on public procurement; Dir. 2014/25/EU(60) on procurement by entities operating in the water, energy, transport and postal services sectors;

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(57) Dir. 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors.

(58) Dir. 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.

(59) Dir. 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Dir. 2004/18/EC Text with EEA relevance.

(60) Dir. 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 Dir. 2004/17/EC Text with EEA relevance.

Dir. 2014/23/EU(61) on the *award of concession contracts*). These new public procurement rules should also be covered in Georgia's public procurement roadmap. Whereas these new directives did not change the basic framework of the EU's public procurement system, which is mainly covered in phase 1 of the DCFTA's indicative time schedule, the numerous new elements need to be transposed into the DCFTA.

Phase 4 of the legislative approximation process will focus on: introduction of techniques and instruments for electronic and aggregated procurement including *framework agreements, dynamic purchasing systems, electronic auctions, electronic catalogues, occasional joint procurement*.<sup>(62)</sup> Introduction of occasional (*ad hoc*) joint procurement will result with more possibilities for co-ordination between contracting authorities; it could take many different forms – contracting authorities may jointly conduct one procurement procedure by acting together or by entrusting one contracting authority with the management of the procurement procedure on behalf of all contracting authorities.

## 5. Conclusions

Armenia has already demonstrated its willingness to implement innovative approaches in public procurement, *i.e.*, the establishment of a partially centralized procurement system. Its current law on public procurement has evolved to pave the way for the promotion of aggregation as a more efficient mechanism to address the common needs for goods and services by various government agencies. Like most countries that adhere to innovative measures, Armenia requires time to overcome uncertainties, estimate the risks and threats in establishing a fully centralized procurement system, one that continuously influences the current practices in its public procurement.

In doing so, Armenia can take advantage of the current opportunities provided by the EU-Armenia Partnership and Cooperation Agreement. While Armenia has not yet experienced joint cross-border procurement with the EU or participated in any PCP/PPI projects (*see* Horizon 2020 for details), its inclusion in the Horizon 2020 project can be a crucial step towards public procurement reforms that may eventually boost its on-going application for EU integration. Armenia's participation<sup>(63)</sup> in the above-mentioned PPI and

(61) Dir. 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts.

(62) Art. 33-36, 38, 50 of the Public-Sector Directive.

(63) Despite the fact that the participation requirements are a minimum of two public procurers from different EU Member States or countries associated to Horizon 2020, the results show less involvement and participation from associated countries. These results are the cause of many factors and barriers associated countries face. Among these factors, the strongest to be addressed first are: the visibility of

PPC projects can be a strong tool to unlock its potential for more innovation in public procurement, and maintain its compliance with rules for its membership in the Eurasian Economic Union.

Armenia's participation in EU-funded projects opens various opportunities for the improvement of its local innovation ecosystem that will promote a stronger local public-sector demand for innovative solutions, which will eventually attract additional financial investments, and, hopefully, encourage the relocation of innovative companies into the region. The government of Armenia has supported various initiatives for international public procurement participation. One of its recently announced initiatives is the call for tenders for the procurement of medical equipment in Armenia under the framework of the EU-CoE joint-project penitentiary reform – strengthening the health care and human rights protection in prisons in Armenia.

Armenia has been doing its part to facilitate its EU integration, and the EU should do the same by increasing its support by promoting its programs, projects and activities in Armenia. Moreover, the EU and EaP countries<sup>(64)</sup> should address the communication and visibility gap about the EaP countries within the EU itself. The examination of the EU tools and their impact in Armenia can help to further the policies, recommendations and strategies needed for efficient implementation.

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the programs and opportunities, the national professional capacities and lack of experience, and national laws, regulations and decentralized system.

(64) The Eastern Partnership (EaP) is a joint policy initiative which aims to deepen and strengthen relations between the European Union (EU), its Member States and its six Eastern neighbours: Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine.

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### **Part I. Crossborder Procurement and Innovation**

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