

BASIC OF PUBLIC CONTRACTS IN ITALY

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1. ADMINISTRATIVE ACTION BY CONTRACTS

Public administrations can conclude all the categories of contracts existing in the legal system. There is no general restriction to make contractual agreements, except for particular provisions concerning specific categories of public entities or specific subject matters. Furthermore, according to national courts (see Corte di Cassazione, II, no. 2624/1984; Consiglio di Stato, V, no. 4680/2001; Regional Administrative Court for the Region Liguria – TAR Liguria, no. 155/2005), also administrations apply the general provision of the Civil Code (CC), Art. 1322, which entitles the parties to bargain contracts not explicitly regulated by the Code itself.

Moreover, in the last years new rules on administrative action extended the entitlement of public bodies to use contractual instruments in a general way: symbolically, legislative policies stimulated administrations to pursue public interests by applying private law, with

the aim of streamlining and improving the efficiency of the whole system, whenever possible (i.e., when there is no mandatory rule compelling administrations to develop unilateral action by exercising administrative powers). In addition, Art. 11, L. no. 241/1990, entitles public bodies to conclude “administrative agreements” (so called “accordi integrativi o sostitutivi del provvedimento”) with private parties, with the aim of determining the contents of administrative (discretionary) measures or replacing them at all. In this case the principles of private law should apply only if they are consistent with the administrative procedure; nonetheless the actual implementation of this rule is troubled (except for urban planning agreements).

Even though private law entered the administrative action, administrations shall also apply specific public rules in bargaining public procurements, such as service, supply and work contracts, and in contracting out instrumental services in order to improve their efficiency. This means that even if contracts concluded by public bodies are essentially subject to the CC and, more generally, to private law – except for some particular cases (game and gambling contracts, loan contracts) – administrative law, especially after the adoption of the European Directives, provides rules which modify or supplement CC, in order to protect both the public interests in the development of the public contractual action - guaranteeing, in particular, the constitutional principle of impartiality (Art. 97 of the Constitution) and the maximization of economic advantages for public entities - and the European principles of freedom to provide services and of open and full competition. On these grounds, the procedures that public bodies should follow in bargaining (so called “procedura di evidenza pubblica”) should match both the principles and the rules of administrative law and the private law principle of fairness.

As a result, according to the phases of public contracting, a double standard system regulates “public contracts”: the selection of competitors follows public rules, whereas private law applies in the performance of the contract (once it has been awarded). This means that the choice of the private partner must be made in compliance with a competitive procedure and the whole contractual action must comply with the principle of good faith and of protection of legitimate expectations.

Furthermore, the double standard system exists also in the field of judicial protection, albeit with some recent innovations: following the general rule on judicial competence – which assigns to civil courts the protection of individual rights (“diritti soggettivi”) and to administrative courts the protection of legitimate interests (“interessi legittimi”) – bid protests are submitted to administrative courts, while contracts disputes refer to ordinary courts (Art. 133 (1), Code of Administrative Process - hereafter CAP). During the performance of a public contract, indeed, contractual parties have rights and obligations in an equal and synallagmatic relationship, whereas in the tendering procedure, the contracting administration exerts some authoritative powers over the competitors, whose legal position matches the notion of legitimate interest (as the Joint Divisions of “Corte di Cassazione” confirms, by judgment no. 27169/2007, administrative action by contract may be perfectly divided into two phases, the first one governed by administrative law, the second one by private law).

However, the distinction between private law and administrative law is not so sharp, because there are several interferences between the two legal frames: on one side, public administration may be sued by the winner of the competition for pre-contractual liability, if the awarded contract is not concluded by the end of the *standstill period* (that is a minimum period during which the signature of the contract in question is suspended); on the other side, public administration holds some powers of unilateral intervention during the performance of the contract, such as that one to terminate it for default or for convenience. In this legal framework, the intersections between public and private law must be verified case by case.

On these premises, this report aims at analysing the main characteristics of Italian contract law on public procurement.

2. THE LEGAL FRAMEWORK ON PUBLIC CONTRACTS

Unlike French “droit administratif”, Italian administrative law does not recognise the category of “administrative contracts”, but since the beginning of Italian Kingdom some

acts have regulated specific categories of public contracts. The first and most important statute was L. no. 2248/1865, “Allegato F”, concerning public work procurement. Moreover, the 1923 regulation concerning the State budget and public expenditures (R.d. no. 2440/1923) provided a set of general rules about tenderer selection and contract award criteria, holding public auction as a general principle (with the exceptions indicated in the same statute and in some other special statutes) for contract award.

In this framework, EU law has deeply modified national contract regulation, by compelling public entities to implement new procedural rules aimed at guaranteeing an open and full competition among private undertakings in the EU internal market. Moreover, EU Directives oblige Italian legal system to recognise unsuccessful tenderers compensation for damages produced by infringements of European regulations (or national statutes implementing them), regardless of the nature of the affected private interest: this way, EU law has overcome the historical distinction in Italian system between “individual rights” and “legitimate interests”.

Since 2006 the Code of Public Contracts (CPC), concerning public works, public services and public supplies, has come in force (see D. Lgs. no. 163/2006). It transposes the Directives 2004/17/EC and 2004/18/EC, which regulate those public contracts with a significant impact (assessed on an economic threshold basis) on transactions between Member States; but it also regulates the same types of contracts (i.e., public procurements), which value is under the European economic thresholds.

Substantially, the CPC maintains the double standard system for contracts with public administrations, providing that what is not expressly regulated by the Code should comply with L. no. 241/1990 (Administrative Procedure Act) as it regards award procedures and other related administrative activities, and with CC as it concerns the contractual activity itself (Art. 2, CPC). Moreover, although the CPC is mainly a public law statute, it provides a number of references to private law, so that interferences between the two legal frames are continuous and relevant.

3. CONTRACT AWARD PROCEDURE

As a general principle, every public entity assigning benefits by contracts to private persons through the allocation of limited resources shall make a call for competition. Indeed, in accordance with the ancient idea laid down in the State budget and public expenditure statutes, tendering procedures have been deemed necessary to guarantee both best value for money and greater administrative advantages for the contracting authority, as well as to prevent public officers' misconducts and briberies. In this view, law aims at favouring public administrations' interests: e.g., the 1923 regulation has exempted the administration from the duty to give reasons, even in the case of exclusion of a tenderer from the contract awarding procedure.

However, EU law has introduced a new balance among the interests at stake, since it has stated that public tendering is deemed necessary in order to guarantee equal chances of the economic operators for public contract awarding and, more generally, whenever a public entity provides market players with an opportunity of profit (see Consiglio di Stato, VI, no. 362/2007). Pursuant to some rulings of the European Court of Justice (ECJ) on the correct interpretation of 2004 directives, competition has become a key principle in contract awarding, aimed at guaranteeing the transparent, equal and non-discriminatory conduct of contracting administrations regardless of the threshold criteria.

In the national system, the CPC has precisely implemented the cardinal rules of EU law, providing a unifying framework for the whole field of public procurements. So, the open, restricted and negotiated procedures shall apply not only to those public procurements with an amount exceeding the economic thresholds fixed by the European Directives, but also to the ones under that EU threshold (with the exception of specific cases – regulated in Art. 121, CPC – which aim at simplifying the typical constraints of formal tendering procedures, even though they comply with the fundamental principles of the EU regulation, mentioned by Art. 2. CPC). Moreover, the same principles also apply to the excluded contracts for procurement, such as contracts on a lot of public services, contracts on weapon production and trade and contracts awarded under international rules (Art. 27, CPC); Art. 30, CPC, also provides that the competitive selection for service concessions

“shall be conducted in compliance with principles derived by the Treaty and the general principles of public contracts”.

However, the implementation of EU principles concerning the awarding of local services of economic interest was more troubled, because of a strong tradition of in house providing by local authorities, formerly managed by special public utilities and lately managed by joint stock companies, wholly or partly owned by the local authorities. Recently, the recourse to in house providing has been reduced by administrative jurisprudence and by the legislator. On one hand, the Joint Chambers of the Council of the State (“Consiglio di Stato”) and other administrative courts applied in a strict way the in house providing criteria developed by the ECJ; on the other hand, statutes authorised the companies awarded without a competitive selection to operate only within more restricted functional and territorial limits and, finally, assessed the exceptionality of the direct awarding itself, recognising in the tendering procedure (“procedura competitiva ad evidenza pubblica”) the ordinary awarding of local utilities. But this rule applies in a different way if the company shares a mixed-ownership, composed by both local public authorities and the private parties chosen by a competitive procedure (see d.P.R. no. 168/2010).

Therefore, the CPC implements the principles of non-discrimination, equal treatment and transparency, laid down in the EU Treaties, in order to ensure open and full competition among the economic operators of all the Member States in the field of public procurements. However, the transparency principle is generally observed throughout the whole administrative action by contract, at least in its elementary components, such as the provision of appropriate advertising forms and the setting of suitable deadlines for the presentation of candidatures and tenders. In order to achieve a minimum standard of competition, the Code itself provides a simplified application of these rules also to the under-threshold contracts and to the excluded contracts (see Articles 27, 30, 110, 125, CPC).

Especially, as a relevant component of the transparency principle the Code charges the contracting authority with the legal burden to provide in a proper notice the requirements

for presentation of candidatures and tenders, the contract award criteria, and the specifications of the subject matter of the contract itself, even in cases of direct bargaining. This general rule has been developed by administrative courts over time: for instance, the TAR Piemonte, no. 1524/2002, has upheld that the call for an informal tender creates for the contracting administration an implicit commitment to the principles of transparency and “par condicio”; therefore, the authority itself cannot modify the conditions of the subject matter by the beginning of the procedure and the preparing of tenders. This way, transparency meets the requirements of equal treatment and non-discrimination in order to level playing field.

Eventually, the CPC provisions maintain an old feature of Italian law in this field, quite strengthened in the '90s: precautions against “opportunistic behaviours” of the parties. This is the reason why provisions about negotiated procedures are more restrictive than in the European law, national rules preferring anonymous candidates and secret tenders. This fact contributes to the peculiar complexity of regulation, which is scantily oriented to flexibility and mildly interested in the optimisation of joined welfare (and the Code has not expressively repealed the 1923 regulation in the part relating to contracts).

However, this over-structured system has not prevented public entities from enjoying a substantial contractual freedom: sometimes, *against the law*, as demonstrated by the impressive case-law of both administrative and ordinary courts, as well as by some judgments of the ECJ on actions brought by the EU Commission against Italy for infringements of EU law by State, regional or local authorities; sometimes, *beyond the law*, as the extensive use of contractual schemes as invented in business practice by public bodies demonstrates.

Therefore, public administrations have been condemned and their contract award decisions have been quashed on the ground of the lack of any competitive tendering procedure or the abuse of negotiated procedures (see, respectively, ECJ, 2008, C-337/05 and TAR Lazio, II, no. 3886/2008); or on the ground that, when proceeding by a public notice, the contracting party cannot ask further participatory requirements than those laid down by the law, if they are disproportionate with the value of the contract at stake or they

are irrelevant for the subject matter. Furthermore, another ground for annulment is the rejection of an abnormally low tender, without verifying in detail the justifications given by the competitor about the seriousness and reliability of the tender itself (see, respectively, Consiglio di Stato, V, no. 426/2010, and TAR Puglia, I, no. 3541/2006).

On the other side, public entities can also conclude some kinds of contracts (or combinations of them) created in the business practice by private operators (especially in the experience of multinational companies), such as factoring, insurance brokering, engineering, global service, performance bond, project financing, leasing option, sponsorship. All of those contracts can be included in the framework of *public-private partnership* rules provided by the CPC and in some cases specifically regulated by CPC itself.

4. PERFORMANCE OF PUBLIC CONTRACTS

Administrative and financial controls have always been among the most characteristic elements in the procedure of “evidenza pubblica”. Articles 11-12, CPC, provide that the final award decision does not produce binding effects on the contracting administration, until its approval by the competent controlling body of the same administration (*id est*, a senior civil servant). Moreover, the decree approving the contracts concluded by the State administrations must also be submitted to the Court of Auditors (“Corte dei Conti”) for external control on administrative and financial regularity, when they involve incomes to the contracting administration or they concern public works above the EU threshold or their amount exceeds one tenth of the EU value (Art. 3, L. no. 20/1994). It should be noted that Art. 19 of the 1923 Regulation laid down similar provisions, establishing that all final award decisions and all contracts did not bind the contracting administration, until they were approved by the minister or by a delegated authority, and could be executed only after this approval; and that the decrees approving the contracts should be controlled by the “Corte dei conti”.

On the contrary, basically the performance of public contracts has always belonged to the realm of ordinary law and EU law has not provided relevant transformation on this side of the regulation yet. Therefore, public contracts are generally subjected to CC rules on invalidity, remedies in case of breach and the consequent contractual liability, and enforcement of the contract by judgment of civil courts. However, public entities being endowed with some special powers, the CPC contains eight provisions which establish specific “principles on the performance of the contract”.

Broadly speaking, Art. 1372, CC, provides two fundamental principles on contractual relationships: the duration of the synallagmatic obligations (and of their binding effects) as long as established in the contractual regulation; and the impossibility to modify contractual terms and to cancel the contract by one of the parties. Both these principles enforce the ancient rule “pacta sunt servanda”. Therefore, by applying this provision (sometimes reminded in the case-law), on one hand, the contractual freedom of public administrations in acting for the best care of public interests is recognised; and, on the other hand, the same capability of such public entities to modify the content of the contract, as determined by agreement, by exercising their special powers, is limited.

However, both the CC and the statutes governing private contractual relationships have some exceptions as it regards the possibility of modifying and cancelling the contract, thus impairing the traditional image of the sanctity of the contract itself. This way, private law tackles the problems connected with the occurrence of unexpected events, from which frustration, impossibility or impracticability of contract may derive; but the presence of a public entity in the contractual relationship can certainly be a stimulus to break the equal positions of the parties and the contractual balance, which is linked to the resulting distribution of risks and benefits.

Furthermore, since the regulation on State expenditures, administrative law has entitled public administrations to lay down, by specific documents, detailed and technical rules for every type of contracts or for particular contracts (respectively called “capitolati generali” and “capitolati speciali”. See Art. 5 (7), CPC). On one hand, these specifications aim at integrating the contract notice drawn up by the contracting authorities for a tendering

procedure, working as “lex specialis” regulating the procedure itself, included the award criteria. Moreover, on the other hand, they determine the conditions of the contract performance, integrating the contract regulation after its awarding. In any case, they can advantage public bodies in the contract performance.

Academic literature and the case-law on public contracts have been debating a lot on the legal nature of such contract documents and at present it is a general opinion that the “capitolati generali” (at least that one on public works procurement used by government departments) have the same character of government regulations, while the “capitolati speciali” (at least as regarding the performance of the particular contract) are “general conditions of contract”, like in private contractual relationships, and therefore they are subjected to the rules of CC on unfair terms in consumer contracts (Consiglio di Stato, V, no. 6774/2005. Regarding CC, see Art. 1469-bis ff.).

Administrative law has traditionally assigned to contracting public entities the so called “jus variandi”, as a partial remedy to the bounded rationality of the administration itself and consistently with the nature of public works procurement as a long-term contract. In particular, Art. 11 of the 1923 regulation established that in the light of an increasing or a decreasing of works during the implementation of a contract, the private contractor is obliged to submit, under the same terms, up to the fifth of the contractual price; beyond this limit, he has the right to cancel the contract. This unilateral power of public administrations has a relevant correlation with the right guaranteed to private parties by Art. 1661, CC: both the provisions take into account the indispensability of the additional works, and consider the changed nature of the contract as the extreme limit to the modifications of the content.

Substantially CPC confirms this regulation, but Art. 132 refers not only to the modifications occurred during the execution of the designed works, but also to the risks in performing activity (such as the so called *geological surprise*). In particular, it provides an exhaustive list of the eligible modifications, due to their essential character and to their relation with the occurrence of unexpected events.

Furthermore, Art. 5, CPC, authorises the Government to adopt a regulation establishing the amount of penalties, consistently with the amount of contracts and the reasons of non-fulfilment, as well as the modalities for their enforcement; but also the CC provides the possibility of sanctions for the breach of contract or the fulfilment on late of the contractual obligations in the relationships between private operators (being there only the limit of their non-proportionate amount assessed as an unfair term).

Indeed, the powers to cancel the contract unilaterally have been deemed more relevant. In particular, Art. 134 and Art. 136 of the CPC provide public entities to withdraw existing contracts for convenience (“recesso dal contratto”) or for default (“risoluzione del contratto per grave inadempimento, grave irregolarità, grave ritardo”); Art. 135 adds the power to withdraw contracts for offences concerning the professional conduct of the economic operator concerned, condemned by a judgment having the force of “res judicata”, and for revocation of the certification of suitability by bodies established under public law. Moreover, a previous withdrawal for default by a public entity may be a condition for an order of exclusion from future competitive procedures developed by the same authority, on the ground that “the normal level” of confidence could be impaired (So, TAR Lazio, II, no. 5182/2000. See also Consiglio di Stato, V, no. 1500/2010, regarding a previous termination for default by another public administration).

However, some similar powers are also provided for the contractual relationships between private economic operators (Art. 1671 and Art. 1662, par. 2, CC), albeit in accordance with the framework of the Code itself (Art. 1218 and Art. 1375), as powers of “*private self-remedy*” (“autotutela privatistica” or “interna”). And then, the most insidious provisions for the equality of the contracting parties are the administrative prerogatives of “*public self-remedy*” (so called “autotutela pubblicistica” or “esterna”), which stem from the special capability of public administrations to pursue public interests. These powers allow the public party to set aside the award of a contract or quite the public notice itself and then the whole tendering procedure, at any time (Art. 11, CPC. See also Art. 6, D. Lgs. no. 53/2010, as amended by Art. 3(19), Annex 4, CAP), so that also during the performing phase, the contract can become ineffective.

The financial compensation for the private contracting party varies according to the reasons of the exercise of these unilateral powers by public entities. First of all, in case of modifications unilaterally charged on, the nature of the additional amount is assessed as a contractual payment (and not as compensatory damages). Secondly, the termination for convenience entitles the economic operator to the payment of the performed works and the value of the existing materials on site, in addition to the tenth of the amount of non-run. Thirdly, the termination for default too entitles the economic operator to the payment of the performed works; but the final settlement of the terminated contract establishes also the costs resulting from the award of a new contract to another economic operator to be charged on the defaulting contractor.

Moreover, in case of failure or not suitable performance, the suspension of the payment by the public entity is considered as a form of “*private self-remedy*” in accordance to Art. 1460, CC. On the contrary, the lawful exercise of the special powers included in “*public self-remedy*” may entitle the contracting partner only to claim a form of pre-contractual liability, while the wrongful exercise of the same powers entitles the economic operator, who has been awarded the contract, to the compensation for damages (which the administrative courts have been usually determining by the same flat-rate above mentioned).

The primacy of the position reserved to the public administration does not affect the private nature of the contract (especially, for public works); then performing it, the private partner is entitled to legal rights, with corresponding obligations on the public body (“Corte di Cassazione” – Joint Divisions, no. 10525/1996). Thus, the private partner may also sue in civil courts by the general action of termination of contract for breach of the public entity itself (Article 1453 of CC); however, the claimed breach should be reviewed as it regards the possible effect resulting from the lawful exercise of the special powers included in the “*public self-remedy*” (“Consiglio di Stato”, VI, no. 6275/2008).

As the breach of the economic balance of the contract is concerned, the CC provides some remedies in order to avoid the termination of the contract itself due to external

factors: to this end, Art. 1467 (3), CC, allows to the party to offer a fair change in the contractual conditions.

Furthermore, specific clauses about the recovery of the contract's economic balance (above all in case of new legislative or governmental regulations) may be included in the public notice and in the other contract documents for the tendering procedure, and then may be reproduced in the contractual regulation, so creating a real contractual obligation. More precisely, for long-term contractual relationship (such as the public works concession), Art. 143, CPC, provides that a restatement of new conditions of balance should be agreed, whenever new mechanisms or price conditions coming from new legislative and governmental regulations would affect the balance of the economic and financial plan of the activity awarded by the concession. The failure of this agreement can bring the economic operator to cancel the contract.

Moreover, Art. 133, CPC, referring to public works procurements, excludes the application of Art. 1664 (1), CC, which entitles both parties to seek review of contractual price whenever increases or decreases in the cost of materials or workmanship have been occurring for more than ten percent of the total price. This means that no price revision is allowed, being on the contrary applicable the criterion of fixed price. However, the price may be increased according to evolution in inflation by a rate established by a government decree, which may be further increased (but also decreased) in case of increases (or decreases) of the costs in construction materials due to exceptional circumstances. Furthermore, the revision possibly resulting from par. 2 of the 1664, CC, according to which economic operators can obtain a fair compensation for the occurrence of considerable difficulties in performing and the resulting modifications to the original design, is among the modifications of the contract included in the list provided by Art. 132, CPC.

On the contrary, according to Art. 115, CPC, all public services and public supplies procurements must hold a clause for price revision, without any reference to the occurrence of unforeseen conditions (differently from the CC). The different treatment of the categories of public procurements may be explained in the following way: because of the

greater onerousness of the performance in public works contracts, the purpose of containing the economic burden on public budgets has been prevailing, albeit without transforming the contract itself into an hazardous one, but using a sort of legal “value maintenance clause” rather than a “hardship clause” (differently also by works concession). And in order to meet the risks to the completion of works or to the quality of the performance, the national regulation on public contracts has opted for a system of insurances (Articles 75, 111, 113 and 129, CPC).

As the end of the public contracts is concerned, Art. 12 of the 1923 regulation established as a general rule that the definition of a certain term of the contractual relationship is mandatory for public bodies; moreover, ordinary expenses (like in the case of rent contracts) may not be exceeding a nine years time. Somehow, this rule is connected with Art. 57 (7), CPC, which forbids tacit renewals of public procurement contracts and sanctions the automatically renewed contract as void, even though this prohibition aims especially at guaranteeing an effective competition.

From the same point of view, CPC recognises the relevant role played by time in the regulation of public contracts: this is true in the case of additional deliveries by the original supplier, awarded by negotiated procedure without publication of a contract notice (the time-limit is three years); in the case of framework agreements (the time-limit is four years); and in the case of public works concessions (the time-limit is thirty years), where the contract duration may be extended with the aim to recover the contractual economic balance (Art. 57, Art. 59 and Art. 143, CPC).

Moreover, according with a consolidated case-laws (Consiglio di Stato, V, no. 6281/2002), modifications in the terms of the contract following a new direct bargaining are not allowed, because public entities must bargain by applying particular procedures (“procedura di evidenza pubblica”) even though they have contractual freedom. Therefore, the modifications to a contract should also be concluded by applying the same procedure.

As the contract completion is concerned, being the contracting partner generally chosen through a competitive procedure, public contracts should be implemented by the awarded

party. This protects administrations from the pressures of criminal organizations, which are always interested in assignment and subcontract of public contract (note that Art. 247, CPC, does not affect the controls provided by other statutes aimed at preventing criminal offences).

CPC confirms this general principle in Art. 118 (1), but it also provides some exceptions: Art. 116, CPC, regulates the modifications of the contract depending on subjective events of the contracting partner and Art. 117, CPC, affects the possibility of assigning the amount owed by public entities. Moreover, Art. 118 – as amended by D. Lgs. no. 152/2008 – authorises the awarded operator to subcontracting with quantitative limits (30% of the prevailing category of works, 30% of the whole amount of the contract in case of services and supplies) which should be defined time by time by the contracting authority in the public notice. Furthermore, competitors should indicate in their tenders the parts of the contract they are planning to subcontract and the contracting public entity retains the control on the suitability of the subcontractors, paying directly the amount owed for the performance to each subcontractor.

In conclusion, pressures, stemmed from both internal factors and the competitive market, have made the national regulation on the modifications of public contracts more restrictive than the EU law. At least with regard to subcontracting, which assures a wide discretion to the authorising public administration; and this is one of the general principles which applies also to excluded contracts (Art. 27, CPC). However, further limits to the possibility to renegotiate the contractual terms are going to be provided from the pro-competitive regulation applicable to public procurements, as in the case of the restricted use of the negotiated procedure for the awarding of additional works or deliveries to the contractual partner.

* Basically this report is based on the contribution by A. Massera in the volume edited by R. Noguellou and U. Stielkens, *Droit comparé des contrats publics*, Bruxelles, Bruylant, 2010. For a further analysis of the issues discussed due reference should be made to this essay