Integrity and efficiency in sustainable public contracts

Corruption, conflicts of interest, favoritism and inclusion of non-economic criteria in the award and execution of public contracts

Turin, June 8, 2012

Introduction

The workshop on "Integrity and efficiency in sustainable public contracts", organized and directed by Gabriella Racca (University of Turin) and Christopher R. Yukins (George Washington University), was held in the general framework of the scientific cooperation within the international research network "Public Contracts in Legal Globalization" (PCLG, www.public-contracts.net), that has been organizing collective research on all sort of questions linked to public contracts since 2007. Yet as Gabriella Racca pointed out during her introduction, the PCLG-network is not the only inter- and transnational network that gathers practical and academic reflections and know-how about public contracts, public procurement and, more broadly, public and administrative law. Indeed, there is also the "Procurement Law Academic Network" (PLAN, www.planpublicprocurement.org), that focuses on public procurement law, the "Ius Publicum Network Review" (www.ius-publicum.com), that clusters some of the most important public law reviews and provides information and contributions on the most relevant and topical public law subjects in an international and comparative way, and the Research network on EU Administrative Law (ReNEUAL, www.reneual.eu), that works on principles and rules on sound administrative procedure for the proper administration of the EU institutions – to cite only the most important international networks and without speaking about the national networks that work on related topics. In the light of this, Prof. Racca advanced the idea of finding a way to link and bundle all these reflections and this know-how, so as to allow for even more fruitful exchange, render these researches even more effective and create synergies between them. Following Prof. Racca, an Internet blog would be an appropriate tool to do so, as it would allow putting up documents and papers for discussion, posting comments and making available links to all the involved networks' websites and news. To launch and explore the process, a blog has been created under www.integrityinpubliccontracts.blogspot.it.

Public procurement and contracts indeed seem to be a very suitable topic for international and comparative exchange and research, because of the cross-border implications of procurement

rules and processes and international, regional and European common rules on public procurement. Yet the research accomplished by the aforementioned networks has shown that international and comparative research on public procurement also is a good basis for and, even more, calls for research on broader questions in the field of public and administrative law. Thus, public procurement is only one of the about twenty topics treated on the website of the "Ius Publicum Network Review"
(see http://www.ius-publicum.com/pagina.php?lang=de&pag=news-doc).

Prof. Yukins supports the idea of such an exchange also from his experience in the USA. In the framework of the government procurement law program at George Washington University Law School, international exchange is currently practiced with Canadian colleagues, turning out an interesting tool to share experiences and best practices. Furthermore, as Prof. Yukins pointed out, international harmonization of public procurement rules is also an objective supported by public policy makers, as differentiation in procurement rules creates barriers between markets. Thus, Prof. Yukins and his American colleagues are also involved in policy making and lobbying, an experience that could be reiterated with the EU institutions by European colleagues. On this point, Prof. Racca made mention of her experience with the answer to the recent green paper on public procurement of the EU Commission produced by herself and several colleagues from Turin. According to Prof. Racca, an international, collective academic effort to produce a common answer to this kind of consultation would assure even more impact and visibility.

The Turin workshop aimed to have a first brainstorming discussion on the subject of "Integrity and efficiency in sustainable public contracts", triggered by the presentation of the different papers, so to prepare the outline of the collective book the scientific directors and participants aim to produce.

Concerning the general setting of academic work on public procurement today, Prof. Yukins outlined that there are three "generations" in the academic analysis of procurement law. The first one established the link between procurement law and general administrative and administrative procedure law, the second one focused on the critical analysis of the existing legal provisions so to improve them, and the third generation today has to link critical legal analysis of procurement law with economic analysis, which was one of the aims of the Turin workshop. Prof. Racca stressed the importance of the procedural component of the procurement process put forward in their approach to the workshop's topic. Thus, the procedure has to assure objectivity to grant the respect of the principles of fairness and equal

treatment. Yet the necessity to grant objectivity does not only concern the contract award but also the execution; in the line of the Pressetext case law, material changes of the contract have to be severely controlled, because they can, inter alia, constitute an open gateway for corruption. Another aspect of integrity in public contracts is the link between anti-corruption and anti-trust law; indeed, there is not only a risk of illegal arrangements between the private contractor and the public entity, but also between private bidders.

The key aspect in the regulation of the procurement and the contract implementation processes is the apprehension, by the regulators, of the exercise of discretion by contracting authorities. As Prof. Yukins pointed out, the EU Commission is aware of the fact that only a small percentage of contracts is awarded to operators from other Member States and that the contracting authorities often have the feeling that the EU rules are superimposed from the top. Hence, to grant them too much discretion is seen as dangerous, as they are deemed reluctant to implement EU regulation properly. Prof. Yukins stated that this approach reminds the one of World Bank officials, who tend to block competitive dialogue because they are afraid of corruption. From the American perspective however, this seems bizarre because discretion granted to procurement officials is seen as necessary to allow them to achieve good technical solutions. The point seems to be that outside regulators often overreact concerning corruption.

Prof. Racca then presented the paper she wrote together with Prof. Cavallo Perin about *Reputation risk as a deterrent to unfaithfulness of the citizen*. Since the mechanical application of law procedures is not sufficient anymore, she suggests a new design of legal rules in such a way as to provide "correct" incentives towards integrity, pursuing in that effort a multidisciplinary approach: new emphasis on individual responsibility, organizational design and economic incentives play a role in preventing corruption, with special regard on civil servants' ethical obligations.

On the same time, Prof. Cavallo Perin and Prof. Racca focus their attention on the ways to prevent corruption through sanctions on individual acting on the organizations' behalf, but especially through sanctions that affect reputation.

In such a perspective corruption may be seen as an act of unfaithfulness to the State. In Italy the Constitution requires every citizen not only to respect the Constitution and the law, but also to be faithful to the Republic, that is a further obligation. Such unfaithfulness does not only regard the corruptor and the person corrupted, but has general effects, as distrust of institutions: in that way corruption weakens the confidence of citizens in the impartiality, effectiveness and efficiency of institutions. The lack of faithfulness represented by corruption

is a disruptive element of every organization that must be repressed by depriving citizens of the benefits related to their citizenship in proportion to the gravity of unfaithful behavior. The sanction for that unfaithfulness shall not be a fine, but the inability to benefit from privileges of citizenship, for some time. It is important to underline that the essential element of the sanction is not so much the inconvenience it can cause, but the impairment and compromising of the reputation of the person in the social group, with a strong deterrent effect.

Finally, a first structure of the collection of papers has been presented: the final book shall be divided in two main parts, following the same structure as the seminar.

A first part shall focus on the award phase, to investigate the concept of fairness and integrity during the selection of the bidder, as the second part shall be focus on the ways to obtain the top performance during the post-selection stage, since execution is a central topic in fighting corruption.

Presentations

- *Gian Luigi Albano (Consip s.p.a.): Objective vs. Subjective Awarding Criteria: On the (Im)Possibility of preventing both Collusion and Corruption in Public Procurement*

By way of introduction, Gian Luigi Albano mentioned several barriers that hamper the exchange on best procurement practices, such as the separation between practitioners and academics or the fact that in the academic world legal scholars and economists do not communicate. Dr. Albano insisted on the importance of the use of plain English as a common language and the need of a common dictionary and a common set of concepts. The object of his presentation thus would be to show how economists approach collusion and corruption.

Collusion is considered by economists a “contract” in the sense of a tacit, self-enforcing agreement that is “concluded” between two or more firms, mostly in the framework of a long-term relationship. The objective of procurement policy thus has to be to make the enforcement of this tacit agreement as difficult as possible. Public procurement markets possess pro-collusive features because of the predictability and relatively high stability of the public demand. A very objective way of evaluating tenderers makes the choice even more predictable; granting more discretion to procurement officials thus makes the choice more subjective and triggers unpredictability from the firms’ viewpoint – but opens the door for corruption, because it sets incentives to interfere with the procurement process. Dr. Albano

discussed the question of how to find a system that balances these two antagonist risks at the same time.

Furthermore, he put in evidence one of the main risks of collusion and corruption: as corruption can be fundamentally described as a self-enforcing (unlawful) contract hinging on a repeated interaction among involved parties, he highlighted the three effective strategies to contrast corruption: to get this target it is essential to make it difficult for the parties 1. to coordinate on how to split the illegal gains; 2. to monitor each other's actions; and 3. to enforce punishment on deviant behavior.

Prof. Yukins commented that there are more cartel cases in public procurement markets because public procurement is linked to the question of legitimacy of the public authorities and also because data are more easily available and public authorities are less incline to accept settlements in litigation.

- *Antonio Romano – Tassone (University of Messina): Prevention of corruption and efficiency in public procurement.*

Prof. Romano – Tassone could not be present in Turin, so Prof. Racca shortly presented his paper.

Prof. Romano – Tassone's enquiry focuses on the plural aims of public procurement: to that extent discretion is a key issue also to get economical efficiency, since automatic systems of award are suitable to meet public interest only if the public administration can identify in advance, perfectly and exhaustively, the performance required. On the same time, discretion may be abused in corrupted practices that can be, or have been in the past, in some way accepted or tolerated in order to protect national, regional or local interest. Nonetheless corruption is, first of all, a criminal behavior and should be repressed.

- *Paula Faustino (University of Nottingham): Regulating discretion in public procurement: an anti-corruption tool?*

In her paper, Paula Faustino carried out a comparison of regulation of discretion in France, Portugal and the UK. She stated that award criteria are a key element concerning corruption, as they necessarily imply a certain degree of discretion. Since the legislator does not know at which moment of the procurement process corruption takes place, he tries to eliminate all discretion. Yet often the procurement process seems to be more an instance of misuse than of abuse of discretion. As Ms Faustino pointed out, discretion does not stop after the drafting of

the award criteria, because the application of these criteria implies still some discretionary power. Furthermore, over-regulation can also push procurement officers to try to circumvent the increasing quantity of rules. At the beginning of the drafting of the Portuguese code, the latter had 200 articles and procurement officers even asked for more detailed rules. In the UK, the perspective was at the opposite: the wish was to have the less rules possible. There is a lot of guidance provided by the government department, but most rules are not mandatory. On the EU level, the problem thus seems to be that the Commission does not give enough space to the national diversities – it would be desirable to differentiate more and to allow the exercise of discretion also by the national legislators to raise the acceptance of the EU rules by the national procurement bodies.

Prof. Racca agrees that minimum rules should be the target and that procurement should no longer be regulated by directives but by regulations who set up minimum rules and leave the rest to the discretion of the national rule makers. Thus, everybody would know that the basic rules are the same everywhere.

- *Albert Sánchez Graells (University of Hull): Prevention and deterrence of bid rigging: a look from the 2011 proposal for a new EU directive on public procurement*

Since Dr. Sanchez Graells could not take directly part in the workshop, Dr. Dario Casalini, lecturer of Public Law at the Faculty of Economics, University of Turin, presented his paper. He insisted on the importance of the structure of the market the authority is facing; procurement rules have to be seen as a tool to boost competition, not only to regulate proper spending of public money. The actual directive contains no rules against collusion, whereas the new proposal works with the concepts of fragmentation and exclusion. Dr. Casalini described the current situation, where bid rigging seems pervasive in public-buyer dominated industries (at least in the European Union) and then focused on some of the instruments and provisions designed to prevent and deter bid rigging that have been included in the December 2011 European Commission proposal for a new Directive on public procurement (replacing current Directive 2004/18). He particularly focused on the issues of contract division into lots and the rules controlling disqualification, suspension and debarment of competition law infringers, as two of the main tools that could effectively help prevent and deter collusion in the public procurement setting.

- *Anna Romeo (University of Messina): Requirements for economic operators*

Due to the many problems which arise in trying to identify the general requirements for participation in public tenders, the question has long concerned both doctrine and the law. Prof. Romeo explained that legislation was inspired by the idea of determining requirements necessary for the prior definition of traders who can participate in the bidding process. Also (or, perhaps, especially) from the European viewpoint, the clear and precise fixing of these requirements permits the setting up of a system of guarantee for traders because it is egalitarian and truly competitive. Certainly, the obligatory nature of the prediction of general requirements for economic operators does not exclude the discretionary power of the contracting authority in identifying the requirements for participation in contracts. Requirements of general nature can integrate the substantive requirements for participation or execution of the contract to the extent that they are not unreasonable, disproportionate, illogical and damaging for competition. Prof. Romeo then focused on two aspects in particular, the requirement given by the so-called "professional morality" and the requirement of regularity of deductions and amount of power of the contracting authority in order to ascertain and estimate the severity of the violation.

- *Loredana Giani (University of L'Aquila): Project Financing and health service. Criticality of an evolving model*

Prof. Giani stated that public-private participation is a phenomenon mainly driven by global financial institutions that has taken many forms over the years, adapting itself to the needs of promoters and partially adapting to the type of intervention to be implemented. The rapid emergence of project financing is undoubtedly influenced not only by pressures from the EU but more general by pressures of the market itself and international settings. As Prof. Giani explained, it must be taken into consideration that project financing – and more generally public-private partnerships – are an integral part of the programs for structural adjustment imposed by the IMF and the World Bank. In her presentation, Prof. Giani analysed this instrument with reference to the health sector. For this purpose, she examined the Italian and British experiences in this field, concluding that project financing, like any other instrument, is not good or bad in itself, but rather, because of its flexibility and versatility, lends itself to different uses and that, for these characteristics, it must be studied and thought through, especially if it is going to be applied in such a delicate area as the health system, to combine two opposite needs that in abstract are difficult to reconcile: the profitability of private investment and the satisfaction of the interest of the collective in the provision of a service

with high quality standards and the guarantee of universal access and, therefore, with a containment of costs for the users.

- *Peter McKeen (University of Virginia): The importance of a professional Public Procurement Workforce*

Prof. McKeen discussed the relationship between the public procurement workforce and broader efforts to promote an effective procurement system that maintains the public's trust. He argued that, when considering methods of enhancing the integrity and efficiency of public procurement, consideration must be given to the role of the procurement workforce in the overall contracting process, and advocated the need to further professionalize the public procurement workforce to deal with the increasing demands placed on procurement officials. Studies of public procurement systems consistently identify the procurement workforce as a "pillar" of the entire system, essential to assure the correct mechanism of the procurement process, also considering the increasing complexity of procurement legislation and the role of judgment and initiative laid down on individuals as key issue of efficiency in public contracts. Furthermore, he insisted on the fact that in addition to a more professional workforce, certain organizational changes could be made to provide individuals in the procurement workforce a greater stake in the process. Indeed, an acquisition workforce with a more comprehensive understanding of the overall process can promote better decision-making. Under the principal-agent theory, converging the interests of the agent and principal may foster actions by the agent (procurement official) that are more likely to be in the principal's (public authority's) interests. Prof. McKeen eventually presented the efforts made by U.S. government to improve the skills of professional procurement workforce, highlighting some of the challenges associated with the effective education of the workforce.

- *André Saddy (Instituto Brasileiro de Mercado de Capitais): Front-line public servants, discretion and corruption*

André Saddy explained that the primary objective of his research is to verify the relationship between bureaucracy, discretion and corruption exercised by front-line public servants and to understand the causes and impacts of corruption exercised by those public servants in various spheres and levels of activity, as well as the factors that facilitate resistance to corruption by citizens at individual and collective levels. According to Dr. Saddy, studying the characteristics of those characters (citizens and front-line public servants) is fundamental to understand this kind of threat to the rule of law and the corruption that is endemic to the

society we live in. Thus, doctrine normally effects those that work in the high levels of the administrative hierarchy, such as the administrative elites and the managers and supervisors, but not front-line public servants. This is the reason for proposing a sociological approach. In fact the doctrine already states that the more legal sociology advances, the more predictable the use of discretion becomes. Dr. Saddy focused on front-line public servants in two scenarios: those who work in the field or on the streets and those who work inside an office, explaining that his research does not attempt to quantify corruption, but to establish a correlation between the level of corruption, the bureaucracy and discretion of those servants who have contact with citizens in their normal routine work days.

- *Bushra Rahman – Eugene Schneller– Natalia Wilson (Arizona State University): Integrity and efficiency in collaborative purchasing*

Prof. Schneller, Rahman and Wilson could not be present in Turin. However their paper has been discussed, analyzed and presented by Dr. Manuela Consito, lecturer in Administrative Law at the University of Turin, Faculty of Political Science.

She explained that the presented chapter is a case study considering the evolution, implementation and success of a professional code of conduct for healthcare group purchasing organizations as they faced criticism and assault from government and other stakeholders in the health sector in the United States. The authors give attention to similar efforts, in other nations, to shape health purchasing behavior around social and business related considerations in procurement, provide a comparison of the GPO code to other codes and assess the key mechanisms developed for accountability to the code by GPOs. Their key sources include archival information from the Health Industry Group Purchasing Association (HIGPA) and the Health Industry Group Purchasing Initiative (HIGPII), references such as Gorlin's Codes of Professional Responsibility, the wide academic considerations of codes of conduct, other health industry responses including Kirk Hanson's assessment of GPO code criteria and the wide variety of popular press commentaries on this issue.

- *Gabriella M. Racca – Roberto Cavallo Perin (University of Turin): Corruption as a violation of competition during the performance phase of public procurement*

Prof. Racca presented the paper she wrote with Prof. Cavallo Perin about corruption in the execution phase of public contracts. First, she pointed out that the procuring entity has chosen the most responsive tenderer according to public interest: contractual conditions represent a firm commitment and should not be substantially amended because every substantial change

or worsening of the quality during the execution phase determines an undue profit for the winner. It undermines competition because it changes the awarding conditions, disturbing the contractual equilibrium. Fair and open competition must be assured to every bidder, to get the evaluation of his offer in accordance with the award criteria. This right does not end with the award procedure but must be safeguarderd in the execution. Changing the award conditions in this latter phase makes the precautions of the precedent procedure useless. Unsuccesful bidders have the right to be sure that not only the winning bidder submitted a better offer, but that he also assures better performance. When this does not happen, the competition principle is undermined because the awardee's lower-than-promised performance makes it as if the procuring entity failed to choose the best tender. Such low quality performance can cover a corrupt agreement too. The role of the losing bidder can be fundamental in preventing corruption because of their deep knowledge of the object of the contract and of the winning conditions.

Allowing unsuccessful bidders to play an active role in contract execution could be an effective instrument to guarantee the winning bidder's compliance with contractual conditions. The focus on the execution could help to prevent corruption – because corruption may be the cause of material changes accepted during the performance phase thus undermining both competition and the integrity of the award procedure in connection with subsequent execution – with the proactive perspective to fight the win-win relationship between corruptor and corrupted through incentives or deterrents through the control of third parties in order to overcome the closure of the corrupt relationship during the perfomance phase.

- *Paolo Lazzara (Third University of Rome): Controlling compliance with contract performance clauses*

The presentation of Prof. Lazzara focused on the impact of modifications of contract provisions on the cost of public works and services. As he stated, the issue of variations is linked to the quest for the best reconciliation between the conservation of the binding constraint and the need (or opportunity) to adapt the performance to the provisions or circumstances occurring, or to change them in a way more satisfactory for the public authority. The statutory boundaries of the concept of variation mark the limits within which the modifications of the original object are still part of the performance. Nevertheless, contract modifications are a common mode of circumvention of European rules. Yet a ban or severe restrictions on variations might conflict with the nature of the contract which, in its

typical pattern, necessarily includes this possibility. It is also very difficult to monitor all the public contracts during the execution, mostly because the competitors no longer have any information about the correct fulfilment of the contract. Therefore, it is necessary to analyse the best practices to prevent that changes in contract execution consist in serious circumvention of rules and an easy opportunity for collusion. In this regard, useful information comes from statistics relating to variations during the execution of the contract and from the criminal law sector.

Other submitted papers/abstracts

The ideas of some other papers/abstracts have been discussed only in general, because of the lack of time:

- G. Edelstam (Sodertorn University): *Individual interest and public interest when the State or local governments buy goods or services*;
- F. J. Vazquez Matilla (Public University of Navarre and Pamplona City Council): *The modification of public contracts as an obstacle to transparency and efficiency*;
- I. Impastato (University of Palermo): *Subcontracting and corruption*;
- A. Gorczynska (University of Lodz): *The role of small and medium enterprises for sustainable public procurement systems*;
- K. Wauters (University of Louvain): *Social sustainability in public procurement: possible influence of a social Europe in progress.*

Conclusion

The papers presented during the workshop and the following discussions gave an overview of the wide range of topics related to the subject of integrity and efficiency in sustainable public contracts. In the edited collection that will follow, this overview will be completed by several other aspects treated by authors who could not be in Turin to present their papers. To further discuss the subject and to prepare the collective book, but also to present the work to the other members of the PCLG-network, the topic will again be on the agenda for the traditional December meeting of the network in Paris. Meanwhile, the blog presented in the introduction will allow for further exchange and discussion on the subject.

Participants and organizers thank Dr. Silvia Ponzio, Dr. Barbara Gagliardi, Stefano Osella, Marta Legnaioli, Matteo Pignatti, Dr. Maura Mattalia and Franco Peirone, who took part in

the scientific preparation of the seminar, working on the papers submitted but not discussed because of the impossibility of the authors to be present in Turin. Furthermore, the event would not have been possible without Dr. Silvia Ponzio and Ph.D. researcher Stefano Osella who managed the administrative organization, offering participants a warm as well as a very well organized welcome in Turin.

Report: Stefano Osella and Hanna Schröder