



Evaluation of Public Procurement Directives

Markt/2004/10/D

Executive Summary

**Europe Economics
Chancery House
53-64 Chancery Lane
London WC2A 1QU
Tel: (+44) (0) 20 7831 4717
Fax: (+44) (0) 20 7831 4515
www.europe-economics.com**

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Introduction

- 1 This report by Europe Economics is the final output of project MARKET/2004/10/D, the purpose of which is to evaluate the effects in the 15 Member States that were subject to the EU Procurement Directives 1992–2003 of the introduction of those Directives. It is part of the European Commission's still relatively new policy of systematically evaluating the effects of its interventions in the EU economy, in order both to increase accountability and to help improve the basis for future policy-making.
- 2 The study commenced at the beginning of 2005. It required an economic analysis of the ways in which the Directives are likely to have affected the markets for procurement goods and services, and involved a legal review of the implementation of the Directives and new empirical research comprising 100 in-depth interviews of awarding authorities and suppliers and an electronic survey administered by the Commission Services.
- 3 Although one could argue that 100 in-depth interviews are not nearly enough to cover the full range of different conditions of awarding authorities and suppliers in 15 Member States, we believe that the results of this interview series nonetheless provide a valid basis for evaluation. Each Interview was conducted by a highly trained economist fully briefed on the legal background and using a carefully prepared interview structure. We obtained an excellent level of response in the interviews. The results fitted into a coherent pattern, as the report will discuss.
- 4 The results of the online surveys were not equally satisfactory. Despite considerable efforts by ourselves and the Commission services it did not prove possible to obtain an equally representative email address list for all Member States. Moreover the response rate as is common in online surveys was small as a percentage of emails sent out and not evenly balanced between Member States. On the other hand those who did respond were able to provide some detailed and specific information. The results have been interpreted in the light of these factors.
- 5 The new empirical research reported here has significantly added to the knowledge previously available on the effects of the EU public procurement Directives. .

10 Key Questions

Question 1: Compliance

How have contracting entities in the Member States complied with the administrative procedures laid down by the Directives?

- 6 The data basis for an assessment of compliance is incomplete and the scope of the present study did not allow for the creation of a new primary dataset which might have made it possible for firm conclusions to be drawn. However, a number of observations can be made:



(a) Overall compliance has improved significantly. In 1995 only 8 per cent of total public procurement (including procurement not subject to the Directives) was published in the OJEU, while in recent years the fraction was between 16 and 17 per cent (and even 20 per cent in the year 2003).

(b) On the other hand we think (even if we cannot prove it) that a significant amount of non-compliance still remains and is not uniform over the different Member States. The publication rate (and hence compliance) may be worse than average in the Netherlands (where a study had found that in 2002, authorities subject to the Directives publish only one third of the amount they should have published – although in fairness one should mention that the Netherlands are the only Member State to have provided an apparently reliable database on which to judge compliance) and in Germany where publication rates appear similarly low. Countries with better compliance rates probably include Spain, the UK and with some caveats Greece.¹

(c) We found that countries with a national legal system that is well integrated with the Directives have higher and more strongly growing publication rates than others.

Question 2: Costs of Compliance

What are the actual operational costs of complying with the Directives, for awarding authorities and suppliers respectively, compared with the cost of complying with other national legislation applicable in individual Member States, (for below threshold contracts for example)?

7 We found that as a result of the Directives the administrative costs of the tendering process have increased for awarding authorities and also that suppliers' costs of bidding have increased.

(a) For awarding authorities the factors increasing costs include the legal rights for bidders that were introduced by the Directives. The authorities subject to the Directives are obliged significantly to increase the accuracy and volume of their documentation and the formality of the process (for example, spelling out their specifications in more detail) in order to reduce the risk of legal challenge. There are indeed complaints that in order to comply with the Directives the authorities have to follow certain procedures even in cases where they believe that the procedures are not efficient. Overall the administrative costs for awarding authorities have gone up by 20-40 per cent (on average in our sample by 35 per cent). The additional cost is a substantial burden in relation to small contracts but a modest additional cost for middle sized and large contracts (meaning for contracts above the thresholds). For these contracts we estimate that overall the Directives have added to the administrative costs of the authorities by an amount equivalent to about 0.2 per cent of the contract values.

¹ As explained in more detail in the report the data basis for Greece is not as reliable as in other Member States.



- (b) For suppliers administrative costs have also increased due to the higher formality of the process which increases the need for form filling and also requires more detailed proposals. Administrative costs for suppliers in our sample rose by 30-50 per cent (on average by 42 per cent). Administrative costs rose less than proportionally with contract size so that the extra burden is greatest for small contracts. Overall the Directives added to the administrative costs of the suppliers an amount equivalent to about 0.2 per cent of the average contract value. Moreover the implication of the numbers of tenders for each contract advertised is that suppliers have to bid more often for a more or less fixed sum of work (we have no reason to believe that the total amount of public procurement increased due to the Directives). These additional bidding costs may double the extra costs incurred to suppliers in relation to each successful bid.

Question 3: Benefits of compliance and balance of costs and benefits

What are the benefits of compliance? Are the costs outweighed by the benefits that compliance provides to the different parties involved? How are these costs and benefits distributed amongst the different parties involved?

8 We can attribute significant benefits to the Directives:

- (a) **Transparency:** Nearly all suppliers and authorities interviewed thought that transparency has increased due to the Directives. Companies that have tried to enter new markets commended the OJEU publications as a significant help in providing market information.
- (b) **Fairness:** Most suppliers say that the Directives have increased their expectations of a fair award procedure and that more authorities now award their contracts based on the published award criteria.
- (c) **Better procurement practices:** In the opinion of most suppliers and awarding authorities the Directives have helped to improve the professionalism of procedures in public procurement. Some procurement officials say that the Directives enable them to fend off political pressure and to concentrate on value for money. (On the other hand both authorities and suppliers complain that the Directives too often require procedures which have no additional value and which reduce efficiency.)
- (d) **Competition:** Overall most suppliers and authorities thought that the competitive pressure in procurement markets had increased. This impression was stronger in markets for the more homogenous and tradable goods and services.
- (e) **Prices:** We concluded from three different sources of information that the overall prices are lower than they would otherwise have been as a result of the Directives but not by a great margin. We estimate this effect to be between 2.5 and 10 per cent of the contract value by 2002.



- (f) **Quality:** Opinions were mixed on the impacts of the Directives on the quality of the goods and services purchased. For standardised products the general opinion was that the authorities now explain in more detail what they want and so receive better quality. For less standardised goods and services, however, negative opinions dominated as many suppliers thought that the technical knowledge of many authorities is not sufficient to achieve the desired quality.

Balance of costs and benefits

- 9 An exact calculus is not possible but we conclude that the balance of costs and benefits has been significantly positive. For the overall welfare calculation we have compared the compliance costs for awarding authorities and the enforcement costs with the price and quality gains resulting from increased competition. The net balance of benefits over costs is an approximation for the welfare gains to society (compliance costs for suppliers are included in the price developments as suppliers will include these in their calculations). We assume for the purpose of this calculation that price reductions mainly reflect increased efficiency rather than merely a transfer from producers to customers; and that savings by awarding authorities benefit those served by the authorities rather than being dissipated in internal inefficiencies. Overall we think that prices are lower than they would otherwise have been by more than 2.5 per cent (€6 billion) of contract value and that enforcement costs and compliance costs for awarding authorities are less than 0.7 per cent (€1.75 billion) of contract value. The overall welfare gain should therefore have been more than €4.25 billion a year by 2002.

Cost and benefits for the different parties

- 10 There appears to be a somewhat uneven distribution of costs and benefits.
- (a) The benefit of lower prices than would otherwise have been paid accrues to the awarding authorities (and as a result, presumably, to the taxpayer or those served by the awarding authority). These benefits outweigh the costs of compliance but the balance is least favourable for complex requirements, and least for small contracts.
- (b) Among the suppliers costs and benefits are unevenly distributed. While efficient and expanding suppliers have been able to use the increased transparency and fairness in order to win additional business, other suppliers suffer from this increased competition as well as from the increased administrative costs of compliance. In the longer term, suppliers as a whole may be said to benefit from becoming more efficient.

Question 4: Costs of Non-Compliance

What is the overall cost of non compliance? Is it possible to measure this cost accurately? Have the costs and benefits of compliance changed over time?

- 11 We define the cost of non compliance as the net benefit that could have been gained had there been full compliance.



- 12 It is not possible to measure this cost accurately or to know how the costs and benefits of compliance have changed over time as we have only incomplete information on the level of non-compliance, and we do not know whether the effects of compliance on those contracts not currently complying would be similar to the effects on the contracts that are compliant.
- 13 If one were to assume that a 25 per cent publication rate would constitute full compliance in the whole EU-15 (as was suggested by some estimates for the Netherlands), and also to assume that the effects on non-compliant contracts would be broadly similar to the compliant contracts, then the additional net benefit (or the cost of non-compliance) of full compliance in 2002 would have been more than €2 billion. However, for the reasons explained it is impossible to provide an accurate measure of this cost.

Question 5: Perceptions of costs and benefits

What have been the perceptions of costs and benefits by different parties?

- 14 We found perceptions on the costs and benefits of the Directives to be quite mixed. Many authorities and suppliers complained about the additional administrative burden, while on the other hand many recognised the additional possibilities provided by the Directives and the contribution they have made to improving procurement practices.

Question 6: Central Purchasing Bodies and Framework procurement practices

Are central purchasing bodies or framework procurement practices used in different ways in different Member States and what effect do they have on public procurement? What proportion of public procurement is conducted by these means and which sectors are most affected? Do they result in better value for money, compared to direct procurement by contracting authorities? Do they have a negative impact on the participation or success of small and medium sized enterprises in tendering procedures? Do they improve the overall level of compliance by aggregating what would otherwise consist of below threshold purchases?

- 15 Awarding authorities are using central purchasing bodies and framework contracts more frequently than before, for the following reasons:
 - (a) The facilitation of compliance was cited as the main reason for the use of central purchasing bodies and about half of the authorities also found them to provide better value for money.
 - (b) Both of these incentives were mentioned by the majority of the authorities as the reason for the use of framework contracts. An additional reason for greater use of framework agreements was the clarification of the law by the European Court of Justice and during negotiations over the new Directives.
- 16 The opinions of suppliers about both procedures are mixed:



- (a) Central purchasing bodies were found to be less transparent, less fair, and more bureaucratic than other public procurement bodies. Overall suppliers found central purchasing to be less efficient but more competitive.
- (b) Framework contracts were assessed as less transparent, less fair, and less competitive but slightly less bureaucratic. Overall framework contracts were found to be about as efficient as other public procurement.

Question 7: Effects on different sectors and authorities

Have there been significant differences in the effects on particular product or service sectors, or on particular categories of procuring entity? For example some services are not subject to the full provisions of the Directive. As they are not subject to the same competitive procedures, one might predict their prices relative to other services have increased. Is this so and are there reasons why they should still be considered less tradable?

- 17 The Directives were in general more positive for larger awarding authorities than for small. Compliance costs increased less in relation to the value of large contracts than for small contracts so the small authorities had to bear proportionately greater cost increases. Moreover, the burden of ensuring compliance also fell harder on smaller authorities than on larger authorities as their staff are less specialised and therefore have more difficulty in fully understanding the complex procedures and legal questions.
- 18 The Directives have increased the incentive of the authorities to increase average contract sizes, so small companies have now more problems in seeking to enter the public procurement markets. We found that small companies have on average more negative attitudes to the Directives.
- 19 The effects of the Directives on different sectors were strongly influenced by three characteristics:
 - (a) Complexity of specifications: In sectors where proposals contain a significant intellectual input and where proposals require correspondingly greater effort for their preparation, the attitudes towards the Directives were much more negative than elsewhere. Suppliers found that the authorities lack sufficient technical expertise to specify tenders adequately and that many of them are deterred by the Directives from seeking advice from suppliers before the tender is issued. In markets of this kind compliance costs have therefore risen by more than average and the benefits of competition have been smaller than average. Some suppliers in these markets think that the Directives have on balance made the market less competitive.
 - (b) Tradability of good/service: Additional competition rose most strongly in markets where no local presence is needed to conduct the contract (e.g. homogenous or standardised supplies and bulk goods) as companies did not have to change their company organisation or structure in order to compete.



- (c) Market share of public sector: In sectors where a local presence is needed the Directives have only increased competition when the market share of the public sector is big enough.
 - (d) As a result of these factors we found that compliance cost increases were much higher in relation to contract value in service contracts than in other contracts and that competition has increased most in supply contracts. Thus the overall balance was less positive in services than in supply.
- 20 It did not prove possible to conduct a price comparison between exempted sectors and other sectors as most exempted sectors cannot provide sufficiently standardised goods and services to allow prices to be compared.
- 21 We conducted an analysis of the exempted sectors that showed from a cost benefit point of view, that some of the sectors (military supplies, rail transport, water transport services) offer arguments for an inclusion into the Directives as they are tradable, some of the tenders are not especially complex, and the average contract size is big. If the Commission and Member States wish to pursue these possibilities, an ex ante impact assessment would be appropriate.

Question 8: Comparisons with private procurement

Has there been a significant difference between the behaviour of public and private institutions in some specific sectors, or between public institutions in different Member States where comparable data may be readily available across a range of relatively standardised products or services? For example hospital purchases or school meals provide a readily understood and easily identifiable purchase, which might none the less show significant variation across the EU or between public and private purchasers.

- 22 We were unable to find data which could sufficiently accurately measure price differences between privately and publicly bought goods and services.
- 23 The interviews nonetheless provided some insights into differences between public and private sector procurement:
- (a) The Directives prescribe that contracts have to be awarded following a rational assessment essentially designed to help to achieve value for money. Some authorities stated that this legal obligation has on occasion helped them to fend off political pressure. So in this respect the Directives have helped to make public procurement more similar to private procurement.
 - (b) In other respects, the Directives have made public procurement less similar to private procurement where rules are designed to be fit for the purpose and flexible, whereas public procurement officials have to follow the prescribed procedures in order not to risk litigation.



- 24 Most suppliers find private procurement more transparent, fairer, more competitive and less bureaucratic than public procurement, even though the OJEU contracts are regarded as better on these criteria than other public procurement.

Question 9: Impacts on Member States and over time

Have there been significant differences in any of these impacts on individual Member States, or over time?

- 25 The way in which the Directives affected the various Member States depends on the nature of their procurement arrangements :
- (a) Member States with strongly centralised procurement functions (like the UK or Portugal) could realise more benefits as their large contracts induced strong competition and relatively less costs. The gains appeared less in Germany and the Netherlands where procurement functions are more decentralised.
 - (b) On the other hand authorities in Member States with relatively informal procurement legislation before the Directives had more problems with compliance and more compliance costs. Examples are again Germany and the Netherlands, and Denmark.
 - (c) Publication rates tended to increase most strongly in countries where with the introduction of the Directives a new national public procurement framework was created which incorporated the Directives (like Austria, Sweden, Finland and France). In other countries where the Directives were implemented on top of the national law and not sufficiently integrated into it, authorities had more problems with compliance and faced higher compliance costs.
 - (d) Member States that undertook particular efforts to increase the professionalism of their public procurement officials (e.g. Sweden, Finland, Ireland and the UK) tended to reap more benefits from the Directives.
- 26 As the number of users in the OJEU grows only with the number of ITTs published in it, the first authorities publishing might not have achieved much more competition from their publication. Over time the suppliers are able to adapt to the additional information available and change their bidding behaviour and perhaps their company structure in order to compete.
- 27 Many authorities and suppliers told us that the effects of the Directives were not significant say 10 years ago but had become more important in the last five years. Our conclusion is that the cost/benefit ratio is more favourable today than it was 10 years ago.

Question 10: Value for money and level playing field

Have the Directives met their objective of allowing contracting entities to get best value for money from their procurement? Is there a level playing field in public procurement? Have the Directives had any unexpected effects (either good or bad)?



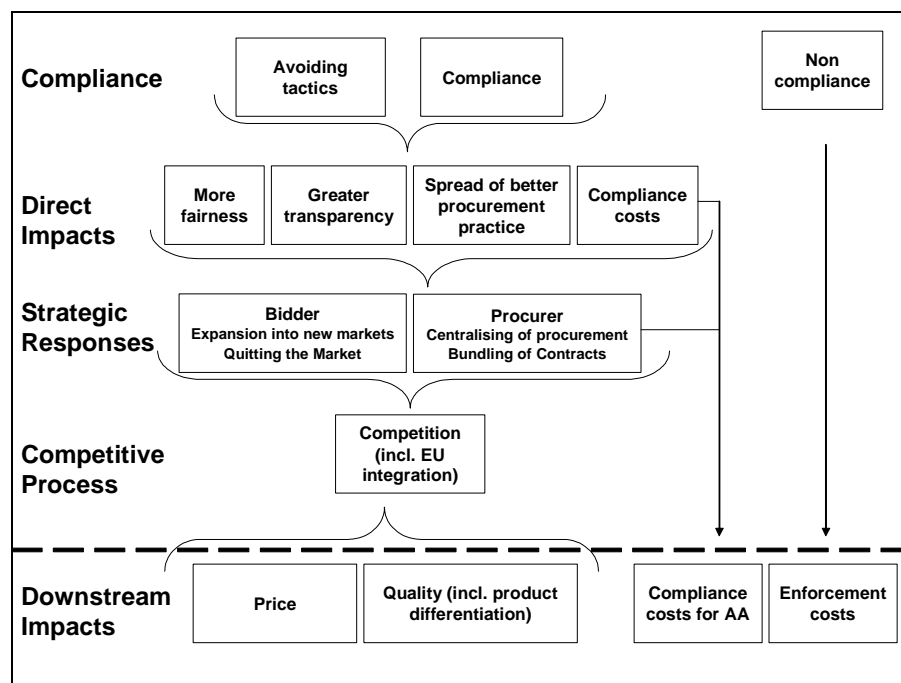
- 28 As mentioned previously we have concluded that overall the Directives have helped the authorities to get better value for money (see Question 2: Benefits of compliance)
- 29 We conducted an analysis of the input-output tables of eight of the EU-15 Member States and found that import penetration in the public sector has risen more strongly in the majority of countries than the import penetration in the private sector between the years 1995 and 2000.
- 30 Moreover, the overall import penetration rate of the public sector in most of the eight countries is now nearly as high (and in some even higher) than that of the private sector if adjusted for sectoral differences of purchases. (If not adjusted the private sector import penetration rate stays higher due to the fact that the public sector buys less tradable goods and services.) This is indication of a reasonably level playing field.
- 31 Most suppliers thought that success rates in foreign countries are much lower than in the home country. This is not surprising if one takes into account that in many public purchasing markets a local presence is necessary for the efficient performance of contracts.
- 32 By formalising the procurement procedures the Directives have increased the demands on the professionalism of the public procurement official. Officials have to be more technically adept (as they have to specify the product more closely) and at the same time legally competent (to avoid legal challenges). Consequently, the Directives have contributed to significant changes in the sector regarding staffing and organisation of public procurement departments. They have also increased the emphasis on the legal aspects of procurement relative to its economic purpose. This may be regarded as an unintended, or negative, effect.
- 33 One source of criticism was the prohibition of using the experience of prior working relationships between awarding authority and supplier as an award criterion. Authorities complained that they could neither favour an incumbent (because they found his experience so valuable) nor discriminate against him (if they wanted to ensure future competition).
- 34 Another negative and presumably unintended consequence is that it has become harder for some smaller suppliers to enter procurement markets.

Structure and Conclusions of the Report

- 35 The order followed in the research, and hence in the report, uses the analytical framework on which the evaluation was based. This framework begins with a categorisation of different types of effect, as illustrated below. Thus we first sought to understand the ways in which awarding authorities and suppliers complied with the new requirements (or failed to do so); then moved on to an assessment of the direct effects on equity, transparency, procurement practice, and compliance costs. The third step was to investigate the strategic responses made by players in the procurement markets; and the fourth, the effects of those new strategies on the competitive process. Finally, we address the question of likely impacts on welfare.



The Relationship between Different Impacts of the Directives



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- 36 In all cases, the impact of the Directives is defined as the difference between the actual situation and that which would have prevailed in the absence of the Directives (referred to as the counterfactual). The counterfactual differs from country to country, from period to period, and from type of procurement to type of procurement. Detailed accounts of the legal frameworks in each Member State on which assessments of the counterfactual drew were part of the study, and were provided in the interim report.
- 37 The main conclusions reached about the impacts of the Directives may be briefly stated as follows:
- Compliance has increased over time and is now substantial, but the available information suggests that there is still significant non-compliance.
 - Positive direct impacts were achieved. Transparency has increased; there is a more level playing field, and better procurement practices have been encouraged (though comparisons with the efficiency of private sector procurement remain favourable to the private sector). However, many suppliers emphasized that some authorities focus too much on legal compliance and not enough on an efficient procurement process to gain value for money. The effect on compliance costs was moreover significantly adverse for both awarding authorities and suppliers.
 - The main strategic response of awarding authorities was to endorse the principles on which the Directives were based, and to accept that less close continuing relationships with incumbent suppliers was a price probably worth paying. Increasing



use has been made of central purchasing, and of framework arrangements, as ways of both improving efficiency and facilitating compliance with the Directives. The strategic responses of suppliers included adaptation to a large EU market, with some greater emphasis on selling outside the home country, and some increase in specialisation. However, some smaller potential suppliers were deterred by the additional administrative burdens.

- (d) The result of these strategic responses and of the direct benefits has been a significant increase in the competition for many public procurement contracts.
- (e) The likely benefits in improved value for money, from lower price and better quality than would otherwise have been available, significantly outweigh the increases in compliance costs for awarding authorities, so that an overall improvement in welfare has almost certainly resulted from the Directives. (This is on the twin assumptions that the price reductions largely reflect improvements in efficiency and that consumers and taxpayers will benefit from reductions in the costs of public procurement.)

38 Thus, the overall evaluation has reached a significantly positive assessment of the effects of the Directives. We estimate the orders of magnitude as follows (the estimates are presented to decimal places in order to reflect the detailed calculations described in the text but are subject to considerable degrees of uncertainty, as the report explains) :

Overall Net Welfare Benefit of the Directives per year in 2002 (in €billion)

	Most estimate	negative	Most estimate	positive
Price decrease (including quality improvements)	6		24	
Compliance costs of awarding authorities	-0.75		-0.25	
Enforcement costs	-1.0		-0.35	
Net benefit of Directives	4.25		23.4	

Source: Estimates by Europe Economics

Recommendations

39 The research reported here leads us to suggest that the Commission consider the following recommendations which may increase the net benefit of the Directives, and which may reduce the burden of regulation as the nature of procurement changes.

- (a) *Improving the data available on public procurement.* The Commission Services should ask the Member State experts to reconcile their estimates with those of Eurostat. Depending on the results of this reconciliation, it may then be appropriate to conduct an analysis of authority accounts using a sample sufficient to give an accurate picture of procurement throughout the EU-25 and in every category of public procurement authority. In addition our analysis on public sector import penetration



could be repeated and extended as datasets from new countries or more recent years become available.

- (b) *Tailoring the provisions better to different cases:* The Commission could try to allow authorities to adapt the provisions more to the different types of awards. Possible areas for such a tailoring and increased flexibility could be time limits, information exchange between bidders and authorities, and thresholds (we would especially recommend that the Commission consider how the difference in the balance of costs and benefits for service contracts, as compared with supply contracts, could best be addressed). Some of these issues have been addressed in the 2004 Directives and the Commission should evaluate in how far the new Directives solve the identified problems.
- (c) *Promotion of better procurement practices:* The Commission could seek to support policies of Member States aiming at the improvement of the professionalism of public procurement officials.
- (d) *Encouraging a greater focus on economic as distinct from legal aspects of compliance.* This could be pursued through the promotion of better procurement practices, and by encouraging changes that would allow those involved in procurement greater scope to adopt methods best suited to different cases.
- (e) *Discussion with the Member States on national legal frameworks:* The Commission could discuss with some Member States how to improve the integration of the national legal framework with the Directives.
- (f) An important concern of both authorities and suppliers was the *system of remedies*. The Commission has worked in the last years to improve legal security and efficiency of remedies and should review whether this endeavour proves successful.
- (g) In some places the Directives may be reformulated to use *principles instead of prescriptions*. As procurement practices change, for example with “freedom of information” legislation and with increasing use of e-procurement, prescriptions which are now helpful may become unhelpful. Also as member countries revise their legislation to achieve the same ends as those of the Directives, exemptions could be issued to simplify the compliance required from authorities and suppliers within those countries.

40 In summary, it should not be concluded from the fact that the Directives have had a significantly beneficial net effect in the past that their scope should be extended or that they should be continued in force indefinitely. As circumstances change, the need for the prescriptive requirements of the Directives may reduce, and a more generally deregulatory approach may become more appropriate.