Cracking Down on Corrupt Companies

A Critical Analysis of the EC's Public Procurement Proposals

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Executive Summary

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Public procurement provides the main interface between the public and private sectors and is recognised as a major source of corruption. In recent years, tendering organisations have developed a raft of anti-corruption initiatives, including those aimed at deterring private companies from engaging in corruption. Whilst, current EU public procurement law makes no such provisions, the European Commission's proposals for a new public procurement Directive coordinating public *service* contracts, public *supply* contracts and public *works*, introduces the possibility of excluding companies found guilty of corruption from tendering for public procurement contracts in the EU.

The Commission's proposals have proved controversial for reasons economic, legal and political. Most importantly, the European Commission and European Council are in disagreement over the *level of discretion given to member states* in the implementation of the Directive, the *possibility for companies to be exempted from exclusion*, should the company show that it has removed *the cause of the conviction* and the *mechanics of the system for exchanging information on the criminal convictions of companies* between member states.

If the Commission's proposed anti-corruption measures are to have an impact on the behaviour of tendering companies across the EU, then they must: be underpinned by an effective information exchange system; provide for a high level of harmonisation between member states; and limit the possibilities for companies to escape being penalised. The following recommendations reflect these requirements, whilst taking on board - and seeking to bridge - the divergent positions of the respective decision-making bodies.

Recommendation 1: Application of minimum standards to all EU public procurement

The EU public procurement Directives apply to member states only. They do not govern public procurement of the EU institutions themselves – or the EU's external aid budget. The provisions of Article 46 for excluding corrupt companies should apply to procurement undertaken by the EU institutions themselves as well as its external aid budget (which already provides for exclusion under its 'ethics clauses').

Recommendation 2: The information exchange mechanism should be EU co-ordinated

The member state-led system that is currently under discussion suffers from fundamental weaknesses. The system to be adopted should be an *EU co-ordinated system*.

Recommendation 3: Introduction of mandatory limits for member states

The Directive should seek to limit the discretion given to member states so as to achieve a minimal degree of harmonisation. Specifically the Directive should set out mandatory limits for member states in relation to: *the minimum conviction level;* the *period of time between conviction and disqualification from tendering*; and guidance on the conditions under which *conviction of a natural person is deemed equivalent to the conviction of the economic operator*.

Recommendation 4: Introduction of 'due diligence' obligations on companies

The Directive should introduce a 'due diligence' obligation on companies in relation to provisions for exempting companies from the ban. This would shift the burden of proof on to the company, who would be required to show that despite a series of measures, it had failed to stop – for example - an employee engaging in bribery or corruption. This would serve to protect both employees and companies.

Recommendation 5: Provide for the exclusion of sub-contractors, associates and subsidiaries.

Recommendation 6: Obligatory application of the provisions of Article 46 of the single Directive to the utilities Directive.

Recommendation 7: Make reference to the study on *Procurement and Organised Crime: an EU-wide study*, White, S., 2000, Institute of Advanced Legal Studies.

1. Aims and structure

The overall aim of this briefing paper is to critically analyse the European Commission's proposals for new European Parliament and Council Directives in public procurement, together with the proposed amendments of the European Council and the European Parliament, from an anti-corruption perspective. It was published in September 2001 in preparation for the debate of the European Parliament in mid-September 2001.

The briefing paper is structured as follows:

- *Section 2* introduces procurement, corruption and the policy drivers;
- *Section 3* provides an overview of the existing public procurement Directives, together with the European Commission's proposals for two new Directives and the proposed amendments of the European Council and European Parliament;
- *Section 4* provides a critical analysis of these proposals and amendments;
- *Section 5* sets out recommendations on how the current proposals might be strengthened in order to combat corruption more effectively;
- *Annex 1* sets out the basic elements of the co-decision procedure – the legislative instrument which underpins the adoption of the public procurement directives;
- *Annex 2* provides a summary of the findings and recommendations of the recent EU-wide study on *Procurement and Organised Crime* and sets out the study's proposed criteria for the operation of an EU coordinated information register (White, S. 2000).

2. Procurement, corruption and the policy drivers

Public procurement provides the main interface between the public and private sectors – and is recognised as a major source of corruption. Evidence from within the EU and across the world shows that today's liberalisation agenda underpinned by a shift in the role of the state from *provider* to *enabler*, and leading to an increase in the 'contracting out' and privatisation of 'public services', is increasing both the *opportunities* and the *incentives* for the payment of bribes by private companies to government organisations.

Organisations such as the EU and the OECD have long recognised that bribes paid by companies to governments, not only distort markets and competition, but also undermine decision-making and democracy. Indeed, the OECD's Convention on the Bribery of Foreign Public Officials (1999), which requires members (including all EU member states) to enact legislation that criminalises the act of bribing foreign public officials, reflects these concerns.

However, today there is evidence that economically powerful Multinational Companies (MNCS) are engaging in a new form of corruption – *state capture* – using bribery to lever control over legislation, regulation and policy-making. Such 'state capture' significantly raises the stakes, increasing the policy imperative to combat corruption.

In recent years, organisations, ranging from the World Bank to EU national governments, have adopted a raft of anti-corruption initiatives, including those aimed at deterring private companies from engaging in corruption. These either seek to raise the costs of corruption – for example by excluding or 'black-listing' companies found guilty of engaging in corruption – or increase the incentives for engaging in non-corrupt behaviour - such as certification schemes or white lists.

Whilst, current EU public procurement law makes no provisions for anti-corruption measures, the European Commission's proposals for a new public procurement Directive coordinating public *service* contracts, public *supply* contracts and public *works* contracts, introduces the possibility of excluding companies found guilty of corruption from tendering for public procurement contracts in the EU.

The challenge of holding companies to account for their corrupt practices, however, should not be underestimated. In the past, companies have escaped penalty through, for example, the conviction of an employee. In 1994, a senior executive of Lyonnaise des Eaux was convicted and sentenced to prison after magistrates found that bribes of FF 19 million had been paid to the Mayor's electoral campaign in return for Grenoble's water privatisation contract. However, Lyonnaise des Eaux continues to tender for public procurement contracts – across the EU and across the world.

Overall, the number of exclusions of companies from public procurement tendering is low. Even the World Bank, which has pledged to ban companies found to be engaged in corrupt practices on World Bank funded projects[1], has so far failed to bar any MNC from tendering for its projects. The outcome of the long-running trial of the *Lesotho Highlands Water Project,* in which a number of western construction companies is accused of paying bribes, will provide a test of the Bank's resolve.

The Commission's proposals potentially represent a major step forward in curbing corruption. The threat of being excluded from tendering for public procurement contracts across the EU provides a powerful deterrent. However, the extent to which these proposals prevail over the undoubted legal, economic and practical challenges will be determined by – and testimony to - the political will of the member states.

3. The EU public procurement Directives

3.1. The Existing Public Procurement Directives

The basis of the existing public procurement directives can be traced back to 1971 when a Directive relating to *public works* came into force. Since then, directives on *public supply* and *public service* contracts have been adopted, as well as directives for the *utilities* sector. Whilst there have been several amendments over the years, the basis of the Directives has remained unchanged.

The existing Directives governing public procurement in the EU are:

[1] http://www.worldbank.org/html/opr/procure/debarr.html.

- The '*Classics'* Directives
  - 92/50/EEC relating to the coordination of procedures for the award of *public service* contracts[2]
  - 93/36/EEC coordinating procedures for the award of *public supply* contracts[3]
  - 93/37EEC concerning the coordination of procedures for the award of *public works* contracts (works)[4]
- The '*Utilities'* Directive
  - 93/38/EEC coordinating the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors[5]

The existing public procurement Directives do not explicitly address corruption, although the three 'classics' directives enable tenderers to exclude on the grounds of; *bankruptcy, professional misconduct, non-payment of social security and tax* and *misrepresentation* (see BOX 1).

BOX 1: Articles 29, 20 and 24 of the Classics Directive

Chpt.2 Criteria for Qualitative Selection, (92/50/EEC: Art.29, 93/36/EEC; Art 20 93/37/EEC Art24):
1. Any (supplier, contractor, provider) may be excluded from participation in the contract who:
(a) is bankrupt or is being wound up, whose affairs are being administered by the court, who has entered into an arrangement with creditors, who has suspended business activities or who is any analogous situation arising from a similar procedure under national laws and regulations;
(b) is the subject of proceedings for a declaration of bankruptcy, for an order for compulsory winding up or administration by the court or for an arrangement with creditors or of any other similar proceedings under national laws and regulations;
(c) has been convicted of an offence concerning his professional conduct by a judgment, which has the force of res judicata;
(d) has been guilty of grave professional misconduct proven by any means which the contracting authorities can justify;
(e) has not fulfilled obligations relating to the payment of social security contributions in accordance with the legal provisions of the country in which he is established or with those of the country of the contracting authority;
(f) has not fulfilled obligations relating to the payment of taxes in accordance with the legal provisions of the country in which he is established or those of the country of the contracting authority;
(g) is guilty of serious misrepresentation in supplying the information required under this Chapter.

3.2. The European Commission's Proposed New Public Procurement Directives

In 1996, the European Commission published and consulted on its Green Paper, '*Public Procurement in the European Union: Exploring the Way Forward'*, the findings of which highlighted the need to simplify and clarify the existing legal framework. This marked the beginning of the overhaul of the public procurement Directives.

[2] as amended by 97/52/EC, 13 October 1997
[3] as amended by 97/52/EC, 13 October 1997
[4] (as amended by 97/52/EC, 13 October 1997
[5] as amended by Directive 94/22/EC of 30 May 1994 and Directive 98/4/EC of 16 February 1998

In May 2000, the European Commission adopted proposals for two public procurement Directives:

- the first concerns the co-ordination of the procedures for the award of public *service* contracts, public *supply* contracts and public *works* contracts and consolidates the existing three 'classics' directives into one single text (COM(2000)275[6]);
- the second concerns procurement procedures of entities operating in the water, energy and transport sectors: COM(2000)276 final[7] - the former 'utilities' directive.

These have been the subject of discussion (under the co-decision procedure – see Annex 1) of the European Council's *Consultative Committee on Public Procurement*, as well as various European Parliamentary Committees, including the *Committee on Legal Affairs and the Internal Market* – which is the responsible committee. The Commission's proposals, together with the proposed amendments, are due to be discussed in the European Parliament in Autumn 2001.

3.2.1 Public Service, Public Supply and Public Works

The Commission's proposal for a new single directive covering public *services, supply* and *works* introduces new anti-corruption measures under Article 46.

Article 46

Art.46 paragraph 1 (BOX 2) introduces a new obligation to exclude any tenderer who has been the subject of a *final* judgment for *membership of a criminal organisation*, for *corruption* or for *fraud.*

BOX 2: Personal Situation of the Candidate - Article 46: Paragraph 1

1. Any economic operator shall be excluded from participation in the contract who at any time during a five-year period preceding the start of the contract award procedure, has been convicted by definitive judgment:

(a) of having committed a serious offence by participating in the activities of a criminal organisation, defined as a structured association established over a period of time and operating in a concerted manner to achieve financial advantage and, where appropriate, to influence unduly the functioning of public authorities;
(b) of corruption, that is to say, of having promised, offered or given, whether directly or via third parties, a benefit of whatever kind to a civil servant or public agent of a Member State, a third country or an international organisation or to any person for the benefit of that person or a third party, with the intention that such person will carry out or refrain from carrying out any act in breach of his professional obligations;
(c) of fraud within the meaning of Article 1 of the Convention relating to the protection of the financial interests of the European Communities established by the Council Act of 26 July 1995

[6] A corrigendum was published on the 30th August 2000 (COM(2000)275 final/2)

[7] A corrigendum was published on 31st August 2001 COM(2000)276 final/2)

Article 46 paragraph 2 point (h) (BOX 3), provides for the possible exclusion of any economic operator who has been sentenced, *whether or not by final judgment*, on grounds of fraud or of any other illegal activity. Paragraph 2 (c) also extends the right to exclude participants for offences concerning their professional conduct to cases of *non-final judgements.*

BOX 3: Article 46: Paragraph 2.

2. Any economic operator may be excluded from participation in the contract who:

(a) is bankrupt or is being wound up, whose affairs are being administered by the court, who has entered into an arrangement with creditors, who has suspended business activities or who is in any analogous situation arising from a similar procedure under national laws and regulations;
(b) is the subject of proceedings for a declaration of bankruptcy, for an order for compulsory winding up or administration by the court or for composition with creditors or of any other similar proceedings under national laws and regulations;
(c) has been convicted by a judgment of any offence concerning his professional conduct;
(d) has been guilty of grave professional misconduct proven by any means which the contracting authorities can demonstrate;
(e) has not fulfilled obligations relating to the payment of social security contributions in accordance with the legal provisions of the country in which he is established or with those of the country of the contracting authority;
(f) has not fulfilled obligations relating to the payment of taxes in accordance with the legal provisions of countries concerned;
(g) is guilty of serious misrepresentation in supplying the information required under this Section;
(h) has been convicted by a judgement of a fraud or any other illegal activity within the meaning of Article 280 of the Treaty, other than those within point (c)of paragraph 1 of this Article

Sub-contractors

Article 26[8] of the Commission's proposal gives contracting authorities the *possibility* of asking the tenderer to indicate who the designated subcontractors are. However, no provision is made for the exclusion of sub-contractors or of tenderers using convicted sub-contractors.

BOX 4: Article 26 (Consolidated Directive) and Article 37 (Utilities Directive)

Article 26: Subcontracting
In the contract documents, the contracting authority may ask the tenderer to indicate in his tender any share of the contract he may intend to subcontract to third parties and any designated sub-contractors. This indication shall be without prejudice to the question of the principal economic operator's liability.
Article 37: Subcontracting
In the specifications, the contracting authority may ask the tenderer to indicate in his tender any share of the contract he may intend to subcontract to third parties and any designated sub-contractors. This indication shall be without prejudice to the question of the principal economic operator's liability.

[8] which corresponds to the provisions of the current Article 25 of Directive 92/50/EEC, Article 17 of Directive 93/36/EEC, and Article 20 of Directive 93/37/EEC

Information Exchange Between Member States

Effective implementation of Article 46 depends on a mechanism being in place that gives tendering authorities access to information about the criminal convictions of companies from other member states.

The Commission's current proposal does not contain any description of such a mechanism. However, the issue has been extensively discussed by the *Working Group on Organised Crime and Public Procurement*, which is made up of independent experts. Whilst no formal information is available on the Working Group's discussions – and the issue is still open to agreement - it seems likely that the Commission will propose the following system. Each member state will be required to assign responsibility to a central authority to answer enquiries made by tendering authorities from other member states on whether companies have any convictions under the three points of Article 46. The responsible authority is required simply to provide a 'yes' or 'no' answer. This means that there is no actual exchange of information on a company's criminal records.

In addition, the Commission must decide whether to incorporate a description of the proposed information exchange mechanism into the current Directive, or to have a separate legal instrument. At this stage it seems likely that the proposed format of the information exchange mechanism will be the subject of a subsequent legal instrument.

3.2.2 The Proposed Utilities Directive: Water, Energy, and Transport

The Commission's proposal on procurement procedures of entities operating in the water, energy and transport sectors does not explicitly address corruption. However, Article 53 point 4 (see BOX 5) provides that the selection criteria and rules to be used '*may include the exclusion criteria listed in Article 46'*.

The Commission's proposal provides that the telecommunications sector is exempted from the scope of the Directive. This will apply simultaneously in all member states and reflect the state of liberalisation of the sector. The proposal introduces a new mechanism, whereby purchases in the remaining water, energy and transport sectors will be exempted from the scope of the Directive, once the sector is judged to be fully liberalised. Exemptions will not be automatic as sectors and member states will be assessed on a case-by-case basis. Exemptions will not apply to activities carried out by the public authorities.

Sub-contractors

Article 37 of the Commission's proposal gives contracting authorities the possibility of asking the tenderer to indicate who the designated subcontractors are. However, as is the case for the single, consolidated Directive, no provision is made for the exclusion of sub-contractors (see BOX 4).

BOX 5 Article 53: Criteria for Qualitative Selection (Chapter VII, Section I)

1. Contracting entities which establish selection criteria in an open procedure shall do so in accordance with objective rules and criteria which are available to economic operators.
2. Contracting entities which select candidates for restricted or negotiated procedures shall do so according to objective criteria and rules which they have laid down and which are available to interested economic operators.
3. In restricted or negotiated procedures, the criteria may be based on the objective need of the contracting entity to reduce the number of candidates to a level which is justified by the need to balance the particular characteristics of the procurement procedure with the resources required to conduct it. The number of candidates selected shall, however, take account of the need to ensure adequate competition.
4. The criteria set out in paragraphs 1 and 2 **may include the exclusion criteria listed in Article 46** of Directive 2000/./EC [on the coordination of procedures for the award of public supply contracts, public service contracts and public works contracts].

3.3. Amendments to the European Commission's Proposed New Directives

Article 46 has proved to be highly controversial and has met with resistance from the Council and the Member States for reasons legal, political and economic:

- *Practicalities of implementation*; member states have highlighted the difficulties of implementing Article 46 across the member states, given the interpretive problems of definition and regulation across national criminal law systems;
- *Disagreement over the appropriate legal mechanism*: the 'exclusion of tenderers' straddles two distinct areas of European law - internal market and criminal law which are governed by different legislative processes based on different legislative instruments and which assign different powers to the three decision-making bodies (the Commission, the Council and the Parliament);
- Conflict between the dual objectives of *creating and protecting the internal market.* A number of member states, including the United Kingdom, holds the position that corruption issues - along with other labour, social and environmental standards - should not be '*the tail that wags the public procurement dog*'.

The European Council, as well as various European Parliamentary Committees, have discussed the European Commission's proposals and produced a number of written amendments. The following are examined in more detail below:

- **Working Document of the European Council** (May 31 2001) sets out amendments to the Commission's proposal on the coordination of procedures for the award of *public supply contracts, public services contracts and public works contracts*;
- **Draft Report of the European Parliament's Committee on Legal Affairs and the Internal Market (June 2001):** on the Commission's proposals for the award of public supply contracts, public service contracts and public work contracts;
- **Draft Report of the European Parliament's Committee on Legal Affairs and the Internal Market (June 2001):** on the Commission's proposals for a directive on coordinating the procurement procedures of entities operating in the water, energy and transport sectors.

3.3.1 The European Council's Proposed Amendments to the Commission's Proposals

The Council's proposed amendments to the Commission's proposals moves away from mandatory terms and gives greater discretion and 'room for manoeuvre' to both member states and companies:

- *minimum conviction level*; the Commission's original proposal made no reference to a "minimum conviction level". However, the Council's proposed amendments give member states the responsibility for determining the "minimum conviction level"(this is not defined but this report interprets it as being the level of seriousness of the offence);
- *period of time between conviction and disqualification from tendering:* the Commission's original proposal stated that "*any economic operator shall be excluded from participation in the contract who at any time during a five-year period preceding the start of the contract award procedure, has been convicted by definitive judgment*" The Council's amendments specify that the member states should determine the time period with reference to their own national law;
- *the definition of responsibility of a natural person versus economic operator*: the Commission's proposal made no reference to the conditions under which conviction of a natural person responsible for or managing an economic operator shall be deemed equivalent to conviction of that economic operator were it to have legal personality. The Council's proposed amendment give responsibility to the member states;
- *exclusion from the ban:* the Commission's proposals did not provide any conditions under which the economic operator could be exempted from a ban. The Council's proposals provide that an economic operator may be exempted from exclusion if it has removed the cause of the conviction. This includes penalising an employee who may have engaged in corrupt practices without the company's knowledge.

BOX 6: Article 46: The European Council's Proposed Amendments to Paragraph 1.

1.Any economic operator shall be excluded from participation in the contract **who has been convicted by definitive** judgment under national law on the following grounds:

a) participation in a criminal organisation, as defined in Article 2(1) of the Joint Action of 21 December 1998;

b) corruption, as defined in Article 3 of the Council Act of 26 May 1997 and Article 3(1) of the Joint Action of 22 December 1998 respectively;

c) fraud within the meaning of Article 1 of the Convention relating to the protection of the financial interests of the European Communities established by the Council Act of 26 July 1995.

For the purposes of this paragraph Member States, referring to their national law, shall specify a

- minimum conviction level;

- maximum length of time for the period prior to the start of the contract award procedure during which account must be taken of the conviction;

- the conditions under which conviction of a natural person responsible for or managing an economic operator shall be deemed equivalent to conviction of that economic operator were it to have legal personality.

An economic operator may be exempted from the exclusion requirement provided for in this paragraph if it proves that it has removed the a cause of the conviction, for instance by penalising an employee having committed one of the acts in (a) to (c) without that operator's knowledge.

BOX 7: Article 46: The European Council's Proposed Amendments to Paragraph 2

2. Any economic operator may be excluded from participation in the contract who:
(a) is bankrupt or is being wound up, whose affairs are being administered by the court, who has entered into an arrangement with creditors, who has suspended business activities or who is in any analogous situation arising from a similar procedure under national laws and regulations;
(b) is the subject of proceedings for a declaration of bankruptcy, for an order for compulsory winding up or administration by the court or for composition with creditors or of any other similar proceedings under national laws and regulations;
(c) **has been convicted by a judgment which has the force of res judicata in accordance with the legal provisions of the country concerned of any offence concerning his professional conduct;**
(d) has been guilty of grave professional misconduct proven by any means which the contracting authorities can demonstrate;
(e)has not fulfilled obligations relating to the payment of social security contributions in accordance with the legal provisions of the country in which he is established or with those of the country of the contracting authority;
(f) has not fulfilled obligations relating to the payment of taxes in accordance with the legal provisions of the country in which he is established **or with those of the country of the contracting authority;**
(g)is guilty of serious misrepresentation in supplying the information required under this Section or has not supplied such information;
(h)has been convicted, **by a judgment which has the force of res judicata in accordance with the legal provisions of the country concerned,** of fraud or any other illegal activity affecting the financial interests of the Community within the meaning of Article 280 of the Treaty.

The Council's amendments introduce definitions for both participation in a criminal organisation and corruption (see BOX 7). They also seek to reverse the Commission's proposals of *Article 46 paragraph 2* point (h) (see BOX 3), that provides for the exclusion of any economic operator who has been sentenced, *whether or not by final judgement*, on grounds of fraud or of any other illegal activity and point 2(c) which extends the right to exclude to cases of non-final judgements. Rather than allowing non-final judgements, the Council is proposing that the judgement should have the force of *res judicata* – i.e. that the judgement should be final and beyond further litigation.

3.3.2 The EP Committee on Legal Affairs and the Internal Market's Proposed Amendments

In June 2001, the European Parliament's Committee on *Legal Affairs and the Internal Market* produced two draft reports on the Commission's proposals for two Directives on public procurement.

In relation to Article 46 of the Commission's proposal for a directive on the co-ordination of procedures for the award of public *supply, services* and *works* contracts, the Committee on Legal Affairs and the Internal Market, like the Council, seeks to amend paragraph to 1a) and introduces the definition of criminal organisation used in Article 2(1) of the Joint Action of 21 December 1998 (see BOX 10) in order to *'avoid pointless disparities and ensure maximum clarity'*. The Committee's reports also amends paragraph 1c) to add new clauses relating to *money laundering, drugs related offences* and the offence of *fraudulent or unfair ant-competitive behaviour* (see BOX 8).

BOX 8: European Parliament Committee of Legal Affairs and the Internal Market
Proposed Amendments to Article 46: Paragraph 1

1. Any economic operator shall be excluded from participation in the contract who at any time during a five-year period preceding the start of the contract award procedure, has been convicted by definitive judgement:
(a) of having **committed the offence of participating as defined in Article 2(1) of Joint Action 98/733/JHA in a criminal organisation, defined in Article 1 of that Joint Action** as a structured association established over a period of time, **of more than two persons, acting in concert with a view to committing offence which are punishable by deprivation of liberty or a detention order of maximum of four years or a more serious penalty whether such offences are an end in themselves or a means of obtaining material benefits, and where appropriate, of improperly influencing the operation** of public authorities;
(b) of corruption, that is to say, of having promised, offered or given, whether directly or via third parties, a benefit of whatever kind to a civil servant or public agent of a Member State, a third country or an international organisation or to any person for the benefit of that person or a third party, with the intention that such person will carry out or refrain from carrying out any act in breach of his professional obligations;
(c) of fraud within the meaning of Article 1 of the Convention relating to the protection of the financial interests of the European Communities established by the Council Act of 26 July 1995.
ca)**of money laundering within the meaning of Article 1 of Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering**
cb) **of a drugs-related offence within the meaning of Article 3(1)(a) of the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances adopted on 19 December 1998 in Vienna**
cc) **of 'fraudulent or other unfair ant-competitive conduct in relation to the award of public contracts in the common market' as defined in the Council framework on criminal law.**

In relation to Article 46, paragraph 2, the Committee introduces the amendment that *'the judgement handed down be final'*. In this regard it amends paragraph 2c) (see BOX 9) and deletes point 2h) (see BOX 3) of the Commission's proposals.

BOX 9: European Parliament Committee of Legal Affairs and the Internal Market
Proposed Amendments to Article 46: Paragraph 2

2. Any economic operator may be excluded from participation in the contract who:

c) has been convicted by a **final judgement** pursuant to the law of the Member State in question, of any offence concerning his professional conduct;

Sub-contractors

Articles 26 and 37 of the Commission's respective proposals give contracting authorities the *possibility* of asking the tenderer to indicate who the designated subcontractors are, but make no provisions for excluding sub-contractors. The amendments proposed by the Committee on Legal Affairs and Internal Market for both Directives, however, do provide for the possibility excluding sub-contractors on the grounds of non-compliance with the provisions made in Articles 46 and 53 (see BOX 10).

BOX 10: European Parliament Committee of Legal Affairs and the Internal Market
Proposed Amendments to Articles 26 (Consolidated) and 37 (Utilities)

Article 26: Subcontracting – Proposed Amendments to the Consolidated Directive
In the contract documents the contracting authority **may not place any quantitative restrictions on the exercise by the undertakings of freedom of organisation of their own inputs. It** may ask the tenderer to indicate in his tender any share of the contract he may intend to subcontract to third parties and any designated sub-contractors. **The contracting authority may prohibit subcontracting to undertakings which are in the circumstances describes in Articles 46, 47, 48 or 49**…

Article 37: Subcontracting – Proposed Amendments to the Utilities Directive
In the specifications the contracting authority **may not place any quantitative restrictions on the exercise by the undertakings of freedom of organisation of their own inputs. It** may ask the tenderer to indicate in his tender any share of the contract he may intend to subcontract to third parties and any designated sub-contractors. **The contracting authority may prohibit subcontracting to undertakings which do not comply with the qualitative selection criteria laid down in Article 53…**

The European Parliament's Committee on Legal Affairs and the Internal Market also seeks to expand the award criteria listed in Article 53, which already cover economic and environmental criteria, to include employment conditions - specifically the *'integration of persons excluded from the labour markets*'.

4. Analysis

4.1. Article 46 of the Single Consolidated Directive on Supply, Services and Works

Article 46 potentially represents a major step forward in curbing corruption. The threat of being excluded from tendering for public procurement contracts across the EU, significantly increases the costs of corruption, thus providing a powerful deterrent. However, the actual impact of Article 46 in terms of changing business behaviour in practice will depend on:

- *the effectiveness of the information exchange system between member states on the criminal convictions of companies;*
- *the strength and level of harmonisation of legislation enacted at the member state level;*
- *the extent to which companies are able to use 'escape clauses' to avoid exclusion.*

4.1.1 Information Exchange System

The information exchange system which is likely to be proposed by the Commission - i.e. tendering authorities in member state X will be able to contact a central authority in member state Y, to find out whether company Z has criminal convictions in any of the 3 areas covered under Article 46 and be provided with a simple 'yes' or 'no' answer - suffers from a number of weaknesses:

- the system assumes that a central administration within the member state has access to criminal records. Yet a recent EU study (White, S., 2000) concluded that in most member states there is no specific system used to access criminal records. The study reports that, with the exception of Italy, there is a lack of access to, and sharing of, information between departments *within* member states. Indeed for Portugal it reported that "*only the criminal court has the full power to obtain data from all public, semi-public or private bodies*" (p. 23) and "*in the UK that public bodies are reluctant to exchange information for reasons of confidentiality*";
- there is a potential conflict of interest and thus a disincentive on the part of the member state to divulge information which will prevent its national companies from tendering from public procurement tenders in other member states This reflects a much wider tension between measures aimed at *protecting* the internal market - i.e. labour, social and environmental standards - and measures aimed at *facilitating* the internal market. The lack of political will, on the part of member states, to adopt a more integrated approach remains a fundamental problem;
- there is no obligation on the part of tendering authorities to contact the member state about its tendering companies. Moreover, the probable delays to the procurement process are likely to provide a significant source of disincentive to the tendering authority;
- the practical difficulties involved, even in the limited system that has been proposed, are likely to present significant barriers to the effective exchange of information and to greatly reduce the impact of Article 46. The EU study on Public Procurement and Organised Crime (2000) found that there is *no evidence of information sharing between* member states in relation to procurement and exclusion. Hence, despite the provisions of the current Directives, the study found that a natural company convicted, for example, of grave professional misconduct in one member state, is likely to be able to qualify as a tenderer in another member state. In addition, there are basic practical problems of language and the willingness of member states to provide a speedy response;
- the information exchange system as currently proposed is characterised by a lack of transparency. Increased transparency should be a cornerstone of all anti-corruption measures. It is unacceptable that this principle should be compromised;
- there is no reference to making use of other 'blacklists', such as the World Bank's, thus limiting the potential for exclusion to the criminal actions of companies within member states;
- there is no means of addressing the issue of corruption by subsidiaries (see discussion below).

Given the status quo of negligible intra and inter member state information flows, combined with practical difficulties and a lack of political will on the part of many member states, it is difficult to see how Article 46 will fulfil its potential under the proposed member-state led system of information exchange.

Alternative options, including that of an EU blacklist, have been discussed by the European Commission's *Working Group on Organised Crime and Public Procurement.* Whilst no formal information is available on the Group's discussions, it is understood that it decided against the creation of an EU coordinated blacklist due to:

- data protection issues associated with the exchange of criminal data (what information, how long is it held, what right of appeal);

- the need for a legal system to underpin the passing of information on criminal records from one member state to another – no such basis currently exists;
- the fact that exchange of criminal records between member states as an issue reaches far beyond public procurement. The Commission is already looking at how to put such a system in place but does not wish to create a solution to fit the needs and time frame of Article 46;
- the ability of those black-listed companies to work behind 'fronts' or 'men of straw';

BOX 11: Alternative Information Exchange Systems

- Self-declaration systems (Finland, Austria) which are usually supplemented by checks with a range of authorities;
- Certification systems (France, Italy, Denmark);
- Central procurement register such that a public authority can check the self-declarations or the validity of documents with a central procurement register (Germany, Portugal, Spain);
- Black-list (Germany, Italy, World Bank);
- White List (see Annex 2).

Adapted from Procurement and Organised Crime: White, S. 2000

4.1.2 Strength and Level of Harmonisation of Member State Legislation

The Commission in its proposed text specifies the time period prior to the start of the contract award procedures during which convictions are to be taken into account. However, it does not provide any other mandatory levels.

The European Council's proposed amendments give discretion to the member states to determine levels in relation to the *minimum conviction level*; the *time period between the conviction and being able to register for a tender*; the *length of the ban*, the *conditions under which a natural person is deemed equivalent to the conviction of that economic operator*.

However, current national laws are far from harmonised. In relation to provisions for exclusion, the EU study on public procurement and organised crime (White, S., 2000) found that:

- *there is no consistency on the period of time for exclusion*. Some member states only allow exclusion from the current tender (Austria, Denmark, Finland, Ireland, the United Kingdom, the Netherlands and Sweden); others allowed for indefinite exclusion (France, Greece and Italy); whilst others for a set period of time (Belgium, Germany, Portugal, Spain and Luxembourg) but varying, for example, from 3-10 years in the case of Belgium to five years or less in the case of Spain;
- there *is no consistency on the length of time between the conviction and being able to register for a tender;*

- there is *no consistency on the approach to sub-contractors*. Whilst in some countries it is possible to exclude associates and other members of a consortium (Italy, Austria, Denmark, Finland, France and Germany), in others the possibility does not exist (Portugal, UK, The Netherlands).

Given this lack of consistency, allowing member states greater discretion in the implementation of the Directives, as proposed by the Council, will result in a 'bumpy' playing field, a distorted internal market and unequal provisions for exclusion on the basis of corruption. This is undesirable in terms of both the *completion* and the *protection* of the internal market.

4.1.3 Potential for Companies to Avoid Being Banned

In the Commission's original proposals there are two key loopholes through which companies can potentially avoid exclusion and therefore render Article 46 ineffective;

- the first relates to *subsidiaries:* the Commission's proposals do not address the issue of subsidiaries. In the context of multinational companies, this represents a significant weakness, particularly given increasing concern over the failure of MNCs to ensure that their subsidiaries and overseas affiliates adopt anything close to good practice in relation to labour, ethical and environmental standards;

- the second is *subcontracting:* in the Commission's proposals, Article 46 makes no reference to sub-contractors, although Article 26 does provide for tenderers to ask for information on sub-contractors. In relation to sub-contractors, the EU public procurement study (White, S., 2000) found that sub-contractors were rarely scrutinised as thoroughly as the main contractor and that "*in most member states it seems possible at present to circumvent the rules regarding exclusion by letting a 'clean' company apply for a tender'* (White, S. 2000, p.18). The study recommends that common rules be adopted for the exclusion of those who are either associated with the contractor or are sub-contractors. The Commission's proposals have not responded to this.

The Council's proposed amendments introduce a further potential escape clause. The provision that an economic operator may be exempted from the ban if it has '*removed the cause of the conviction'*, means that a company can continue to operate and tender for public procurement contracts if, for example, an employee is punished.

Whilst the clause is aimed at protecting companies from the actions of a rogue employee, it also potentially lets companies 'off the hook' completely, as companies found guilty of corruption can simply 'remove' an employee. The Council's proposed amendments mean that Article 46 could simply maintain the status quo, such that companies, which have been engaged in bribery and corruption, are still able to tender for public procurement contracts – across the EU and across the world.

5. Next Steps

The European Commission's proposals are due to be discussed before the European Parliament in September 2001, under the co-decision procedure. It is expected that:

- the European Commission will support its original proposals and in particular will be against the introduction of the clause that allows companies to be excluded from the ban should they, for example, take action against an employee;
- the Council will be seeking to introduce greater discretion to the Member States in Article 46, paragraph 1;
- the European Parliament may be looking for greater ambition – in particular in relation to the creation of a European co-ordinated register.

Given the level of disagreement, it seems likely that adoption of the new Directives will be a lengthy process and, under the co-decision procedure (see Annex 1), will go to Conciliation.

5.1. Recommendations

Recommendation 1: Application of minimum standards to all EU public procurement

The EU public procurement Directives apply to member states only. They do not govern public procurement of the EU institutions themselves – or the EU's external aid budget. The provisions of Article 46 should apply to procurement undertaken by the EU institutions themselves as well as its external aid budget. However, it is worth noting that the '*Manual of Instructions'* for procurement for Community Cooperation with Third Countries (SCR), already provides for exclusion in its 'Ethics Clauses', and is therefore much tougher on corruption than current internal market procurement rules. However, once adopted, the provisions of Article 46 should also be incorporated into the articles on the 'Grounds for Exclusion' to provide for a harmonisation of standards.

Recommendation 2: The information exchange mechanism should be EU co-ordinated

The member state-led system that is currently under discussion suffers from fundamental weaknesses - legal, practical and political. The system to be adopted should be an *EU co-ordinated system.*

Recommendation 3: Introduction of mandatory limits for member states

Given the large variation in provisions for exclusion in member state national laws (see White, S.,2000), it is recommended that the Commission issue guidance on:

- the *minimum conviction* level;
- *the time period prior to the start of the contract award procedures during which convictions are to be taken into account*;

- and the *conditions under which conviction of a natural person is deemed equivalent to the conviction of the economic operator*.

The Council's amendments should not be adopted in their current form. The effectiveness of Article 46 depends on some level of harmonisation of national law.

Recommendation 4: Introduction of 'due diligence' obligations on companies

The Council's amendments (see BOX 6) provide for companies to be exempt from exclusion if they *remove the cause of the conviction.* If introduced in its current form this would significantly *reduce* the costs of corruption, as the company has the possibility of being exempted from the ban.

It is recommended that the Council's amendment be strengthened by introducing a '*due diligence'* obligation on the company. This would have the effect of shifting the burden of proof on to the company who must show that, despite a series of measures, it failed to stop an employee engaging in bribery or corruption. This would significantly lessen the scope for companies to use an employee as a scapegoat, whilst at the same time providing protection for companies.

Recommendation 5: Provide for the exclusion of sub-contractors and subsidiaries

The Commission's proposals should not be adopted in their current form. It is vital that the provisions of Article 46 apply to sub-contractors, associates and subsidiaries. The amendments proposed by the European Parliament's Committee on *Legal Affairs and the Internal Market* addresses the issues to some extent (see BOX 10). However, any provision should be mandatory.

Recommendation 6: Application of Article 46 of the single Directive to the utilities Directive

It is recommended that the Commission introduces an *obligation* to apply the provisions made in Article 46 of the directive for the award of public *service* contracts, public *supply* contracts and public *works* contracts to the directive on the procurement procedures of entities operating in the water, energy and transport sectors (utilities).

Recommendation 7: Make reference to the study on *'Procurement and Organised Crime: an EU-wide study'*, White, S., 2000, Institute of Advanced Legal Studies

Reference should be made to the above study, which was commissioned by the Justice and Home Affairs Task Force of the European Commission. It explores the legal, administrative and practical realities of exclusion and procurement across the EU member states, covering areas of criminal, administrative, commercial and civil law. The report provides a synthesis of 15 national reports, as well as a set of recommendations (see also Annex 2).

ANNEX 1

The Co-Decision Procedure

1. Commission drafts the proposal for submission to the European Parliament (EP) and the Council of Ministers;
2. The EP may propose amendments;
3. The Council may adopt either the original or the amended proposal;
4. If the Council does not adopt the proposal it must adopt a common position, which it conveys to the EP;
5. The EP can then amend or reject the Council's common position;
6. If the EP proposes amendments to the Common position then the amended text must be sent to the Council and the Commission;
7. If the Council does not agree all amendments a Committee must be appointed comprising equal representation of the EC and the Council;
8. If the Committee cannot agree then the act is not adopted.

ANNEX 2

TABLE 1: Recommendations of the EU Study on Procurement and Organised Crime (Simon, W. 2000)

Recommendation	Justification
1. The conditions under which exclusions occur should be harmonised as much as possible	All member states make it possible to suspend applications from tenderers but only a few of them make it compulsory.
	All member states make it possible in practice to exclude tenderers from a specific tender, but some Member States make it possible to exclude them from a set period of time from all public tenders. Member States may wish to make this an option in EU law.
	Periods of exclusion vary in the member states. Member states may wish to consider whether these different approaches are likely to cause harm and whether they would like to legislate in order to harmonise periods of exclusion. Member states which only exclude on a case by case basis would then have the option of extending their system to excluding for a period of time in the future if they so wished
	Member States need to consider whether they wish a sentence pronounced by a judge for certain crimes and offences to include deprivation of the right to participate in the procurement process.
	All exclusions for a period of time are penalties within the meaning of ECHR and so should be appealable in a Court of Law.
	Member states should be reminded of their obligation under Article 3 of the Joint Action of 21 December 1998, requiring them to make legal entities criminally liable for organised crime offences.
	The vast majority of Member states do not suspend or exclude on suspicion alone and feel that this runs counter to the basic rights of tenderers. We recommend that member states be left to follow their own practices.
	We recommend that common rules be adopted regarding the exclusion of those who are associated to the main contractor in some way or are his sub-contractors.
	The concept of grave professional misconduct needs to be clarified as most member states authorities seem unclear as to what this might refer to.
	The member states should consider whether there should be a common approach to exclusion in cases where the tenderer fails to produce a crucial piece of evidence such as a criminal record.
	There needs to be a common approach to the period of time that is required before a natural or legal person who was convicted of organised crime offences is deemed to be rehabilitated and can tender again.
	At the moment the award of damages seems to pose little threat to public authorities. Member states may

Recommendation	Justification
	consider setting up a tariff for the award of damages, failing which differences may have an impact on the Internal Market.
2. For the purpose of excluding tenderers on the grounds of organised crime the European Union should be treated as one area.	2.1 There are differences in the ways in which exclusion is interpreted in the Member States. It seems important that a common approach be agreed to avoid a distortion of the market and 'zones of leniency' within the European Union.
	2.2 Tax, duties and social contributions disqualifications should have a EU-wide effect: for example a tenderer who is established in Member State A and has failed to pay his taxes in Member State B should not be allowed to tender for lucrative state contracts in Member State C.
	There should be mutual recognition of professional bans/withdrawal of licenses.
3. Systems should be established to encourage a flow of information vertically (within member sates) and horizontally (between member states).	All Member States should consider centralising information exchange.
	3.2 The Member states should discuss adopting a common approach to the holding of data held centrally on excluded tenderers and in particular to the mechanisms for the correction of such data, when found to be inaccurate.
4. Purchasers should be given opportunities to develop sound practices in relation to organised crime	4.1 Purchasers have a key role to play. However, they often feel unsure as to what checks they can make and feel hindered because they have no powers of investigation. We recommend that purchasers be consulted as to the ways of making their role more transparent and more effective.
	4.2 Purchasers should be consulted on the role of future central agencies.
	4.3 Purchasers need to establish common approaches to anti-corruption in their own offices, with the help of the Falcone programme.
5. There should be a common approach to whistle-blowers.	5.1 Each central bureau in the member states should be responsible for receiving information and ensuring that allegations are investigated. At present it is unclear what happens to the information passed on by whistleblowers.
	5.2 The national procurement agencies could also have a 'hotline' for whistle-blowers and should be responsible for follow-up.
	5.3 A common standard of protection should be agreed for whistle-blowers who have chosen to give their

Recommendation	Justification
	names.
	5.4 A common approach to malicious reporting should be considered but as a low priority since Member States already punish this
6. Member states should consider developing systems to prevent organised crime and corruption.	6.1 We recommend that member states consider how far their existing arrangements allow for the prevention of bribery and organised crime and whether these structures could be amended to improve their prevention function.
	6.2 Member States may also wish to focus on the elements within the procurement process which prevent corruption and organised crime
	6.3 Member States may wish to look at existing mechanisms for administrative cooperation with the aim of improving horizontal and vertical co-operation
	6.4 Member states may wish to look at existing mechanisms for cooperating between administrative and prosecuting authorities with the aim of improving horizontal and vertical cooperation.
	6.5 The construction sector appears to be vulnerable to organised crime and special measures may be necessary throughout the EU. We recommend that this sector be singled out for attention throughout the EU.
7. In adopting a common approach, the member states should be mindful of the global dimensions of organised crime.	7.1 The accession countries should be involved in discussions on exclusions from the earliest practical opportunity.
	7.2 In the long term, exclusion arrangements for the Member States and the institutions of the EU will need to fit with wider arrangements under the auspices of the WTO. In the short term effective proportionate and appropriate action by the EU may help to give a lead to international action. Thus in developing proposals for action, consideration should be given to the wider international context.
8 The possibility of an EU-wide White List should be discussed. An EU White List could run alongside some	*8.1 Benefits* An EU White List would enable the EU to adopt a common approach on conditionality and to show what standards it is aspiring to in procurement. This would provide a list of tenderers who are reliable from the point of view of a) not being involved with organised crime and b) being reliable in some other notable respect… We believe that believe that these potential benefits are considerable and we therefore recommend that consideration should be given to setting up a European White List…

Recommendation	**Justification**
national/regional Black Lists	8.2 *Functioning of an EU White List* Member States would compile a list of tenderers (by sector) on the basis of positive checking. The tenderers would volunteer information showing that they meet EU-agreed criteria and they would agree to extensive checks being carried out by the national authorities in which they are established and that their particulars may be kept by the EU coordinating body. The national procurement agencies would be responsible for checking in accordance with the agreed EU White List criteria. Participation in an EU White List would be voluntary on the part of tenderers. However, being on the White List could be taken into account by public authorities not only in the Member States, which carried out the checks but also throughout the EU.
	8.3 *Preference* The European Institutions could consider giving an undertaking to give preference on the EU White List, since the latter would have been checked and found to meet some desirable criteria.
	8.4 Reasons Against an EU Black List An EU White List would complement existing Black List approaches in some Member States. An EU Black list could not and indeed should not become the main approach for three reasons. A) Blacklisting is a severe penalty (and raises the questions of proportionality), so it faces the practical limitation that authorities are very reluctant to apply B) Organised criminals operate behind fronts or 'men of straw' who by virtue of their good record do not get blacklisted, hence the measure may not be very effective. C) it is clear that black listing is unlikely to extend to all Member States at least in the foreseeable future. These disadvantages should be compared with the benefits of positive checking or white listing…
9. The action needed would be best deal with a combination of first and third pillar action	9.1 It seems essential that first and third pillars be coordinated and not seen as meeting different goals (opening of markets versus exclusion of tenderers…)

Source: Procurement and Organised Crime: An EU-wide study. Edited by Simone White, Institute for Advanced Legal Studies pp 28-33.

BOX 12: Mechanics of an EU White List

Narrow Version
- The tenderer volunteers to demonstrate or to have checks done to the effect that as far as the territory of the European Union is concerned:
- He has no unspent conviction for financial crimes or irregularities of any kind anywhere
- He has at no time been in breach of contract through the quality of his work
- He has at no time failed to pay social security contributions
- He has no outstanding tax or duties debt (over a certain thresh-hold to be determined)
- His associates/partners are also on the EU White List
- He is not blacklisted as a tenderer
- He agrees to his details being held by the EU coordinating body on procurement
- (Maybe) that he will only use sub-contractors, who are on, or a willing to apply for inclusion on the White list (see below, under the heading 'to be decided)

Wide Version
The above plus the following;
- He has never had a professional or other license withdrawn
- He has never been in breach of environmental rules
- He has never employed undeclared labour, or labour in breach of immigration rules

To be Decided
- The frequency of updating checks (three yearly?)
- The rehabilitation period after conviction and conditions for rehabilitation (see recommendation Annex 2 1.11)
- Whether tenderers on the EU White List should be asked to undertake to sub-contract to tenderers who are also on the list.

Source: EU Procurement and Organised Crime: p.34 White, S., 2000