

The impact of public procurement on EU structural support absorption rates and efficiency

Summary

The aim of this assessment is to improve the use of EU structural support by evaluating the impact of public procurement on EU structural support absorption rates and efficiency. From the point of view of management, the *effectiveness* of public procurement and the results of the public procurement aimed at are defined as the acquisition of goods, works or services meeting the needs of a client supplied for a reasonable price at the required time with the best possible use of human resources. The following factors determine the accomplishment of these results: legal regulation of public procurement, the practice of applying legal regulations, the capabilities of purchasing organisations and the control system and control procedures of public procurement. The assessment is based on the results of analysis of different information sources: regulating documents, statistical data on Lithuanian public procurement carried out in 2009-2011, surveys of purchasing organisations (hereinafter referred to as the “POs”) and employees of institutions controlling public procurement, public procurement documents (case studies), interviews, other publicly available secondary sources of information.

Impact of applying public procurement procedures on the speed and effectiveness of absorption of EU support.

Meeting the needs of a client. The results of surveys on the POs show that the POs most often procure the objects meeting their needs; nevertheless, they face the problem that the goods procured are of inferior quality. Around 48% of the TOP 100 POs and about 50% of non-TOP 100 PO group respondents have faced situations when they were not satisfied with the quality of goods, works or services procured, and approximately 18% of TOP 100 PO respondents and 9% of respondents not belonging to this group indicated this problem as systematic and recurring. Among the possible reasons for these problems the following were mentioned: the prevalence of the criterion of the lowest price, and insufficient use of possibilities provided for in regulations, etc.

Duration of procurement. Around one third of respondents pointed out that they often faced, and about half of them have at least several times faced situations when the procurement procedures financed by the EU took too long and the implementation of EU-financed projects fell behind schedule. Statistical analysis has proved that the source of financing (EU support funds) influences the duration of procedures. The trend noticed is that procurement financed by EU funds takes longer. Procurement financed by EU funds takes longer than non-EU-financed procurement due to their specificity: they are usually of higher value; larger share of international procurement; more claims are submitted; the criterion of economic benefit is applied more often; higher number of higher value procurements, the duration of which is longer, etc. When assessing all these factors together, the statistical analysis shows that the main factors determining the duration of a procurement procedure are: the type of procurement procedure (international/simplified) and exertion of legal disputes during the procurement procedure. Although the number of public procurements during which a claim was submitted is relatively small, the impact is high as it is likely that a high-value procurement financed by EU funds would be trapped, which would negatively impact the tempo of assimilating the EU support. Therefore, the suggestions provided are related to the possible use of simplified procurement (by increasing the limit of the procurement price taking into consideration the practice applied by foreign countries, and the increase of effectiveness of investigating claims.

When assessing the total duration of procedures and impact on effectiveness, attention should be paid to the preparatory stage for the implementation of project. Case studies have shown that smaller POs pay insufficient attention to the preparatory stage for the implementation of a project. By carrying out more detailed analyses of the market before the procurement, the POs would be more capable of choosing the right procurement procedure. The general duration of procedures in procurement financed by EU funds is also prolonged by the administrative system of the EU support (procurements are controlled more strictly and the control procedures prolong the general duration).

Rationality of the usage of funds. We identified the main factors that might increase the value of procurement financed by the EU funds. The EU support administrative procedures do not encourage the project implementers to make economic use of the funds of a project financed by the EU (the approved budgets, the aim to assimilate the funds). In addition, indirect costs of a project (e.g. remuneration to the project team, rent of premises, other indirect costs) are related to the sum of

direct costs. If project implementers procure objects for less than planned for in the budget, with the corresponding decrease of costs for financing, the share of indirect costs decreases. An important factor determining the price is the level of competitiveness. The level of competitiveness in Lithuania is lower than the EU average, and 35% of procurements have only one supplier (2011).¹

Impact of type of procurement on the speed and effectiveness of absorption of the EU support.

The type of procurement procedure (international/simplified) has a significant influence on the duration of the procedure. As for the simplified procedures, the Law on Public Procurement provides for shorter terms of public procurement procedures, and more flexible and simpler procedures of procurement. In some other countries (Ireland and Great Britain, Estonia, Latvia, Poland) regulation of simplified procurement is more liberal. Taking into consideration practices applied by other EU Member States, Lithuania could consider the following possibilities for regulating simplified procurement: to increase the limit of low-value procurement, to increase the existing sum of LTL 10,000 set by the Law on Public Procurement.

Ways of procurement. In most cases (both when procurements are financed with EU funds, and with funds from other sources) the simplest and theoretically shortest procedures applied in Lithuania are: open tender procedure/simplified procedures of open tender. No one of these is more effective than the other; however, only the best fitting one must be chosen for each procurement, i.e. the one that would ensure the highest effectiveness in a particular case. It would not be reasonable or effective to purchase uncomplicated objects, whose parameters are clearly defined and which are supplied under established conditions in the market in more flexible and at the same time more complex ways of procurement (negotiations, competitive dialogue). On the other hand, it would not be reasonable or effective to purchase complicated objects whose qualitative parameters and price may differ significantly, and whose supply conditions may not be defined in advance, following strictly defined means of procurement (open or restricted tender). In the context of the EU support, a series of complicated infrastructural projects are implemented which, in theory, should encourage the application of procurement procedures that are more flexible and therefore more suitable for the implementation of complex procurement; however, simpler procurement procedures are not often used. It is possible that the costs of skills, cost-effective examples and human resources and the risk of carrying out the procedures improperly, as well as the fear of incurring financial sanctions determine such practice.

Impact of assessment criteria (criterion of the lowest price/criterion of economic benefit) on the speed and effectiveness of the absorption of the EU support.

The results of POs survey show that in most cases the POs purchase the objects meeting their needs; however, sometimes they face the problem that the objects procured are of inferior quality. There may be many reasons for this (proper definition of the procurement object, selection of the means of procurement, control of contract implementation, etc.), however one of them is the prevalence of the lowest price criterion. When comparing Lithuanian and EU Member States practice, contrasting practices are noticed. Over 90% of procurements (according to number) in Lithuania are carried out according to the lowest price, meanwhile in the EU, on average only one third of procurements are implemented according to this criterion. The prevalence of the lowest price criterion does not ensure the quality of goods/works/services and the economy of costs that will be incurred during the entire life cycle of the object procured, which has a negative impact on the effectiveness of using the EU support and does not correspond to the principles of the policy of sustainable development.

On the one hand, the procedure of public procurement when the lowest price criterion is applied takes less time and requires fewer resources of the PO employees. On the other hand, assessment of proposals only according to the criterion of the lowest price is often unacceptable and inappropriate, especially when the quantitative parameters of goods, services of works need to be assessed. The European Commission “*Report on Modernisation of Public Procurement*“ (2011)² suggests that the criterion of the lowest price should not continue to be the determining factor for choosing the winner.

¹<http://www.vpt.lt/admin/uploaded/2012/VP%20Ataskaita%202012.pdf>

²<http://www.europarl.europa.eu/document/activities/cont/201110/20111025ATT30281/20111025ATT30281EN.pdf>

The impact of application of exceptions provided for in the Public Procurement Law on the speed and effectiveness of the absorption of the EU support.

The conclusion might be drawn that the application of exceptions has only limited influence on the tempo and effectiveness of absorbing the EU support, first of all for the reason that procurement procedures during which the exceptions provided for in the Public Procurement Law are applied are rather rare; therefore, the influence of such exceptions on the speed and effectiveness of using the EU support is not assessed as significant.

Control system of public procurement and control procedures of public procurement in the implementing institutions.

Control system of public procurement.

The control system of public procurement is comprised of several levels. The main function of the Public Procurement Office is to monitor how the requirements of the provisions of the public procurement legislation are followed when implementing public procurement. The competence and authority of implementing institutions are related only to the administration of the EU support funds and the impact is related only to the recognition of project costs as appropriate to be financed, to awarding the financing and financing for applying financial corrections. The implementing institutions shall make sure that the costs were incurred without violating the provisions of legislation of the European Community and the Republic of Lithuania. The Department of State Control of the Republic of Lithuania carries out the function of an audit institution and implements the audit of costs declared to the European Commission and the audit of the EU support management and control system.

Taking into consideration the competencies and functions of the institutions participating in the procedures of public procurement and the procedures for administering EU support, it is considered that they [competencies and functions carried out by the mentioned institutions] have been coordinated since they focus on quantitatively different objects. Nevertheless, it should be noted that this does not mean that actions performed by the mentioned institutions do not overlap and that functions are carried out effectively. In addition, it is noticed that majority of institutions assess the security of conformity of procedures.

The presence of several levels of control in a system is not a bad thing as every level of control checks different aspects and controls the effectiveness of controls carried out by other levels. Yet, the participants of the system did not indicate that the controlling institutions assess the practice of application of public procurement differently; different institutions or different workers provide different interpretations of the Public Procurement Office and different conclusions or recommendations accordingly. This situation is probably caused by different specifics of the checks and functions of the controlling institutions.

Apart from the aforementioned, the duty of the implementing institutions to apply to the Public Procurement Office for the conclusion is not absolutely clear. In accordance with one legal act, an implementing institutions having suspicions about a violation of a public procurement procedure, must notify the Public Procurement Office of this. Meanwhile other legal acts establish the right for the implementing procedure to decide whether to apply to the Public Procurement Office. It should be noted that application to the Public Procurement Office for a conclusion always means that implementation of the project will take longer because it has the right to investigate violations of this kind for 20 working days (in some cases even 60 working days) from the date of receipt of all required documents and information. It is suggested to define the cases for application to the Public Procurement Office in the regulating documents.

Control procedures of public procurement in implementing institutions.

The analyses have shown that in spite of the fact that all implementing institutions carry out the same task of ensuring public procurement, they differ greatly in the principles of selection of their checks, the phases of the process, the questions of checks and the documents to be checked. Differences in the details of checks mean that both on the scale of the system of implementing institutions, and on the scale of institutions carrying out the control of public procurement in general, the "critical points of checks" which would allow effective optimisation of the control, are not coordinated. The survey of project managers in the implementing institutions who check public procurement has also revealed that the procedures are clear and comprehensible and applicable in practice, however, the

effectiveness of the procedures is assessed as weaker (proportion of time taken and the result achieved).

To ensure uniform practice and increase the effectiveness of checks, it is suggested to coordinate the check of the scope of procurement on the level of the EU support administration system by generally agreeing on common “critical points of control” and details of checks. In addition, accreditation/verification of check procedures and check sheets of the implementing institutions is suggested which would confirm that the procedures are sufficient to identify possible violations of the Law on Public Procurement (in the context of eligibility for financing by EU support and application of financial corrections).

Many implementing agencies apply a risk-based assessment by selecting the means of anticipatory and subsequent control of public procurement. Yet, the Rules on Project Administration and Financing provide that the selective check of public procurement may be applied only to procurement of low value. Therefore, the advantage of the opportunities of applying a risk-based approach on the scope of the entire system and decreasing the costs by checking the most risky fields in detail– and applying a representative check to the rest of the fields – is not taken. Modern theory pays increasing attention to the increase of effectiveness of control by applying the principles of risk management. It is suggested that all controlling institutions make a decision concerning the application of principles of the control system of public procurement based on risk management and the acceptability of such a system with regard to all controlling institutions. Having agreed on a risk-based model for the control system, it is suggested to fully apply it by checking the procurement financed by EU funds.

Skills of POs and controlling institutions

There are rather large quantitative differences in purchasing skills between separate POs. Larger POs or POs organising more procurement obviously have better skills and experience, therefore, the quality of procedures is considerably higher. The survey of POs and implementing institutions has shown the following: smaller POs face the problem of shortage of resources and skills. Around 43% of respondents (who do not belong to TOP 100 POs) pointed out that they do not have any public procurement specialists. But, it should be noted that apart from the lack of POs skills, the lack of interest and responsibility by project implementers to carry out public procurement in a timely manner and to adhere to deadlines also impede the absorption of EU support.

In the survey of POs, the competence of institutions controlling public procurement was not assessed as the most significant factor in the system of public procurement (more significance was given to such aspects as the need for human resources and administrative burden, frequent change and complexity of regulations, shortage of skills in smaller POs). In general, during the survey the POs assessed the competence of controlling institutions as rather good. Nevertheless, one of the competence-related problems of the project managers of implementing institutions who check public procurement of projects is the wide range of their functions requiring managerial, legal, engineering and technological skills.

Regulation of public procurement

Regulation of public procurement on the EU level is an especially harmonised sphere. The Public Procurement Law provides for sufficient opportunities of flexibility, however, the factor that is important in seeking effectiveness in employing the opportunities provided and applying them in practice, which depends on the experience and skills of the PO.

Changes in the Public Procurement Law, impact on the speed and effectiveness of absorbing the funds of the EU structural support

When assessing formally, from the perspective of the stability of legal relations on public procurement, it is obvious that the Law on Public Procurement is amended too often. Yet, the amendments made with regard to the contents are significant and, in the opinion of the authors, needed. In the short-term perspective, such amendments could have negatively impacted the implementation of procedures (adaptation to the changes), in the long-term or system perspective, however, they were largely needed and allow for the increase of effectiveness. Taking advantage of the opportunities depends on the capabilities of participants, which are not always sufficient.

Conformity of the Public Procurement Law with the EU policies (sustainable development, environment protection, prompting innovations).

The Law on Public Procurement and post-legislation correspond to the relevant EU policies. The provisions of The Law on Public Procurement and post-legislation provide opportunities for innovative procurement that are not inferior to the ones provided in the rules applied by other EU Member States. Sustainability and other principles are also integrated in the Lithuanian system of public procurement (best value for money during the whole life cycle of a product may be ensured by using the criterion of the economically most beneficial tender; Part 3 of Article 24 of the Law on Public Procurement obliges the PO, in cases pointed out by the Government of the Republic of Lithuania, in the procurement documents to set the requirements and (or) other criteria for effectiveness of energy use and environment protection; the Public Procurement Law also provides for opportunities to integrate social aspects in the public procurement procedures).

Methodical documents regulating the application of the Public Procurement Law, their sufficiency and conformity.

When compared to the sample methodical documents provided by other EU Member States, the range of information provided by the Public Procurement Office is rather broad. According to the authors, information provided by the Public Procurement Office encompasses all fundamental issues on the regulation of procurement procedures; therefore, it is sufficient. Additionally, standard procurement documents designated for more complicated means of procurement could be drafted (negotiations, competitive dialogue, project tender, electronic auction, etc.). Besides, more user-friendly means for providing information could be sought for; examples of good practice, which could be followed by the POs, could be provided.

Dispute settlement mechanism.

At the moment Lithuania has a two-phase system of appealing against decisions taken during the procurement procedure: (i) pre-trial procedure of dispute settlement by means of investigating claims by PO and (ii) judicial procedure of dispute settlement. In practice, there are cases when the pre-trial phase of dispute settlement is employed improperly because the POs investigate the claims in a formal manner seeking to defend themselves, instead of resolving the issue in essence. Formal investigation of claims and reluctance to resolve the problems allow for further legal disputes, which in essence influences the deadlines of procurement implemented and its expedition.

Amendments of the Code of Civil Procedure approved in June 2011 provide that cases on public procurement shall be investigated in 60 days. Yet, taking into consideration the extremely busy schedule of courts, it is highly likely that cases on public procurement would not be investigated within the given period of time. Therefore, it is suggested that any changes are initiated gradually, first of all, after having assessed the impact of the amendments of the Code of Civil Procedure on the duration of the investigation of cases on public procurement.

Recommendations are provided in Chapter 6 of this Report