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EXECUTIVE SUMMARY

Concepts and research questions

The goal of this deliverable is to provide an assessment of the impact of corruption on development by focusing on infrastructure through a survey of EU-funded infrastructure projects in selected countries.

The reports on public procurement in this work package were meant to advance the understanding of government favouritism and state capture by using public procurement data. **We define government favouritism as the process whereby a government agent treats certain economic actors in a preferential manner against others of similar background. We define state capture as the situation when a government agency acts systematically for the benefit of a specific interest group or company instead of autonomously pursuing its public goal for broader social benefit as defined in either law or policy. We define as corrupt the situation when the particularistic distribution of public funds can be associated with evidence of reciprocation - profit (of any kind) for the individuals or parties enjoying authority who decide over preferential social allocation from the recipients of their favour or their associates. We seek to understand the rules of the game in the governance of public resources, especially whether the dominant norm is particularism (transaction explained by the presence of a particular connection or identifier) or universalism (transaction identical for the whole category of non-state actors). Particularism on behalf of the government towards non-state actors (individuals, organizations or companies) can result in two situations. In the case of favourable treatment we speak of favouritism. In the case of unfavourable treatment we speak of discrimination.**

Our reports focus on the construction sector because this sector is indicated by nearly every source as the highest public investment and top risk area in nearly all the countries. We differ from most of the literature on procurement which is focused on regulations, loopholes and potential risks, as we ask the following research questions:

1. ***What is the norm in the public resource distribution*** in the area of construction? In the case of a modern and non-corrupt government we would expect that the government acts to maximize social welfare (outcome is beneficial for most people), treating every actor (for instance, companies which bid for tenders) in a non-preferential and impersonal manner (process is fair and impartial) by pursuing values such as ethical universalism (everyone treated equally and fairly) and seeking maximum return for public investment (value for money). Can we estimate how many transactions from the total in our area of study come close to this benchmark? Is there enough transparency to assess if the norm is universalism or rather particularism/favouritism? Are corrupt exceptions known and controlled adequately? Is the situation different for EU funds compared to national funds?
2. The second research question, once we establish if most transactions are particular rather than universal, is ***what is the nature of the particularistic link***. Why is government treating preferentially some private actors? Is there evidence of

profit reciprocation, and if not, is this due to absence of data and lack of adequate investigations, or other factors?

3. If we find evidence of systematic government favouritism and state capture, *what is the impact of this for the market and society?* Do we find evidence of market or political distortion (e.g. through party financing)?

Indicators and case selection

To answer these questions our research teams set to collect these indicators:

1. **Indicators on transparency of government transactions in the area of procurement and public-private partnership in infrastructure.** These were basically collected from the process of retrieving data, based not only on online accessibility but also to the responsiveness of national authorities to disclose the data needed to document this report.
2. **Indicators on the material stake of procurement in the budget and construction sector** at least from 2008 to the last available year, as follows:
 - National level data:
 - Share of total procurement volume in GDP (%), if possible, breakdown to national vs. local level
 - Share of construction sector in GDP and in total public expenditures (%)
 - Share of construction spending in total procurement (%)
 - Share of EU-funded projects in total construction sector (%)
 - Firm level data:
 - Mean/median market share of the companies that *participate* in all (relevant) public procurement in construction sector and EU funded projects separated between domestic and international companies
 - Mean/median share of public procurement income in total income of these companies (%)
3. Indicators on **national procurement legislation and practice:**
 - What are the national peculiarities in procurement legislation? Are there substantial differences between national and EU procurement rules?
 - How have the national rules changed over time? Were there any changes after elections / government changes?
 - How are members of procurement award boards appointed? Are they bureaucrats or mostly politicians? Again, is there a systematic turnover after elections / government changes?
 - Do national laws, courts and/or political decisions indicate any systematic pattern for a particularistic distribution of resources? If yes, what is the nature of the particularistic link? Is there important contestation, and where does it come from?
4. Indicators on government favouritism and corruption **in public procurement**, as follows:
 - Outcome indicators. Non-random patterns after data mining of public procurement indicating some companies win disproportionately a large number of contracts or some agencies grant most of their budget to certain companies

- Process indicators. Number and relative share of single bidding in the tendering process, as well as of other frequent tendering irregularities
- Indicators of profit for the awarding public authority. Individual or party donors to electoral campaigns and any other financial contributions to political parties (financial ties to politicians).

The countries selected for this study changed slightly compared to the project document. The original case selection included an EU old member state, at least one new post-communist member state, one accession state and one neighbouring country. The latter was supposed to be Ukraine, which was discarded due to beginning of the war there and the difficulty of retrieving data. The final case selection included thus four new member countries with four different accession dates (Hungary - 2004; Romania and Bulgaria - 2007; Croatia - 2014), an accession country (Turkey) and an old member state (Germany). Greece was discussed in the context, but discarded due to difficulty of data gathering and lack of variation in the panel, which missed a country with good control of corruption perception. With the inclusion of Germany, the resulting panel varies sufficiently both in terms of EU membership and the level of control of corruption reported.

The universe of transactions was established as contracts in the field of public infrastructure (construction) of over 1 million euros starting in 2008, so to cover at least two electoral cycle and two governments. We decided that EU funded projects will be discussed within the framework of nationally funded projects, so whenever possible teams were instructed not to make a selection but draw on all possible existing data.

Due to varying access to data in these countries, our research teams were encouraged to use a mix of methods most suited to their respective data availability. All teams engaged in data mining on different numbers of transactions to spot non-random distribution patterns and investigated particularistic links with party financing and other potential causes. Teams also searched for distortions by market analysis of the construction sector and by analysing the provenance of fortunes of top businessmen. Teams which managed to extract big data made extensive use of descriptive and inferential statistics to establish the significance of non-random distribution and connect it with potential causes.

Results

Data availability varied even more significantly than we expected. Data was denied to teams in Bulgaria and Turkey despite being officially requested (it is not available online). Online available procurement contracts in Romania proved not to be in open data format, so most of the resources of the team were spent on manually copying the data and building a database. Croatia and Hungary managed to retrieve the data. The latter three countries had therefore a large N to work with. Germany was a surprise due to poor availability of data (there are no legal requirements to even store it), so only data in the European Tender Electronic Data (TED) as well as German audits could be used. While comparable and addressing similar research questions, reports vary in terms of capacity to answer these questions. Bulgaria, for example, uses a selection of top 40 construction companies for an in-depth analysis, while Turkey opted for public-private partnership (PPP) projects.

Indicator collection proved relevant as to the material stake (high in all the countries, though affected by crisis everywhere except in Germany), sector analysis (the crisis made firms even more dependent on public funds for their survival), market distortion and patterns of distribution. We recommend that total value of procurement should be monitored by year and sector by all the countries, as well as the percentage of competitive procurement from the total. Presently in both allegedly corrupt countries (such as Bulgaria) or non-corrupt (such as Germany) indicators suggest that public procurement is far less competitive than previously thought, in any event far from OECD guidelines¹.

Main diagnosis was however possible drawing on this variety of sources. Government favouritism and state capture were identified across very different contexts. The report on Turkey draws on quite complex analysis to identify the public-private partnerships and concessions as the main means to achieve favouritism, for instance, which would not be possible in the context of EU legislation. The existence of private favourite firms with political connections is confirmed for Hungary, Romania, Bulgaria and Turkey. Some state agencies seem entirely captured, with all over 50% of their budget going to such firms. In Croatia state-owned companies are the most favoured, but their management is entirely politicized, so the research team argues that private profit exists (for the appointing party). The Hungarian report found EU funds a liability especially since the 2010 government change. In the case of Romania, national funds, as compared to EU funds, are more susceptible to procedural irregularities as evidenced by the larger share of contracts won by a single bidder. However, politically well-connected companies are winning not just national Romanian contracts but are also winning more EU funded contracts. The indicators on market concentration are more ambiguous and difficult to interpret, but there seems to be less distortion than hypothesized. The main impact is on public funds and democracy, as procurement seems an important means to fund politics. Particularism seems an important presence and part of the rules of game, even in Germany, despite insufficient evidence indicators exist to suggest that ethical universalism is far from being the general norm and many informal practices still persist. The impact on society is however highest in new democracies such as Romania, where most of the top fortunes in construction and most other areas are actually made from public contracts, not the private market. Similarly in Hungary, the most rapid wealth accumulation can be directly traced to procurement contracts awarded to companies with direct links to the top leadership of the right-wing government.

Each country report contains recommendations which can be grouped in three main areas: improvement of transparency, training of administrators, and monitoring. Indeed most of the problems found reflect rules of the game that are perceived by the population of these countries and which could be avoided by prevention, consisting of full transparency, training, and monitoring. More detailed recommendations will follow in the next WP8 policy report, in WP 10, as well as the Anticorruption Report volume 3, due this fall.

¹ <http://www.oecd.org/gov/41760991.pdf>



ABSTRACT

The Bulgarian public procurement market constituted 9% of national GDP on average from 2009 – 2013, which is lower than the EU average. Public procurement has been particularly important for the construction sector in the country, with approximately a third of total sector turnover deriving from public procurement in 2013. Since the onset of the economic crisis in 2008 the survival of the construction sector in Bulgaria has essentially hinged on public procurement, coming mostly from EU funds. This concentration of market power in the hands of the public administration, coupled with a history of lack of effectiveness, integrity and control, and persistent structural governance deficiencies imply significant corruption risks. Although the legal framework has continuously improved, it is subject to too frequent changes to ensure proper implementation.

The firm-level analysis of the public procurement contracts awarded to the top 40 construction companies included in the paper, confirms the trend of concentration of the construction sector. The data does not confidently detect a specific type of favouritism but corruption risks are detected in specific cases, especially involving large-scale construction projects in the infrastructure and energy sectors. Anecdotal evidence abounds that powerful private operators exert pressure on the public administration to channel public procurement to major companies, linked either legally and/or through circles of influence to them.

ACCRONYMS

CF	Cohesion Fund
CPV	Common Procurement Vocabulary
CSD	Center for the Study of Democracy
EC	European Commission
EPC	Engineering, Procurement and Construction
ESIF	European Structural and Investments Funds
EU	European Union
GBS	Glavbolgarstroy (large Bulgarian construction firm)
GDP	Gross Domestic Product
GVA	Gross Value Added
HPP	Hydro Power Plant
LPP	Law on Public Procurement
MA	Managing Authorities
NAO	National Audit Office
NPP	Nuclear Power Plant
NSI	National Statistical Institute
OP	Operational Programme
PFIA	Public Financial Inspection Agency
PHARE	Programme of Community aid to the countries of Central and Eastern Europe
PP	Public procurement
PPA	Bulgarian Public Procurement Agency
PPR	Public Procurement Registry
RIA	Road Infrastructure Agency
RSPP	Regulation on Small-Scale Public Procurement
SAPARD	Special accession programme for agriculture and rural development

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I. INTRODUCTION

Bulgaria has been repeatedly defined as a high corruption risk country, in which the resources and opportunities for corruption are high, while deterrents and constraints remain low (Mungiu-Pippidi, et. al, 2011, pp. 40-41). Its governance regime has been described as moving gradually from patrimonialism to open access order, with most of its features still in the competitive particularism stage (Mungiu-Pippidi, et.al. 2014, p. 25). Hence, if the normative ideal of good governance is equated with open access order,¹ Bulgaria is still far from achieving good governance. Widespread corruption persists in the country (CSD, 2014), and the allocation of public resources remains particularistic and unpredictable, though EU membership has produced more transparency and accountability. As one of the main channels for transferring public resources to the private sector, studying the functioning of the public procurement market in Bulgaria and focusing on construction can provide important insights into the opportunities and constraints to corruption or favouritism in Bulgaria.

II. MATERIAL STAKE: THE BULGARIAN PUBLIC PROCUREMENT MARKET

1. General public procurement market

In order to assess the corruption risk in this sphere, the term “public procurement market” is defined in this paper as the supply of goods, services and construction works² for the public sector and the utilities, for which the legislation prescribes following specific procurement procedures. This definition excludes the supply of goods, services, and works below certain (minimum) threshold values³, which according to Bulgarian laws do not require such specific procedures. In this context, the public procurement market includes most of the current and investment consumption of the central and local government bodies and institutions, as well as the legal entities they finance and/or manage. These are the so-called “conventional” contracting authorities in the public procurement sphere. The public procurement market also covers current and investment consumption of the so-called “sectoral” contracting authorities. These are the network suppliers of public services or utilities in the energy sector, water supply, transportation, and postal services. Regardless of whether they are publicly or privately owned, due to being natural monopolies and due to the fact that their (in)efficiency is of high importance for society

¹ For a detailed discussion on how good governance relates to a taxonomy of governance regimes and to corruption and anti-corruption, please see Mungiu-Pippidi, et.al. (2011), *Contextual Choices in Fighting Corruption: Lessons Learnt*, Hertie School of Governance and NORAD, Berlin, 2011.

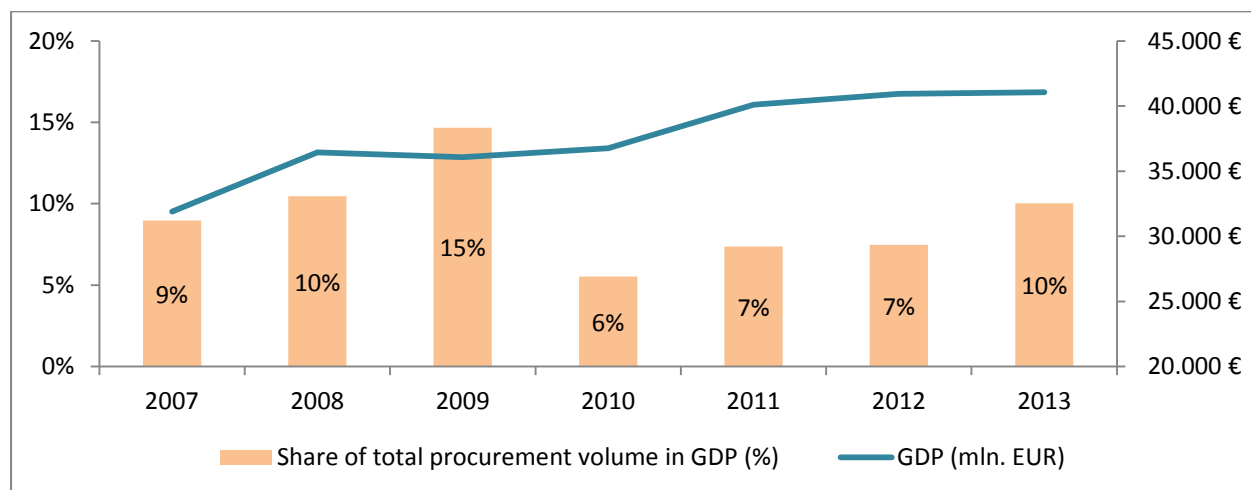
² There are different terms in the literature describing “construction works”, such as “public works” or just “works”. In this paper, we have chosen to use the term “construction works” as this is the term the Public Procurement Agency of Bulgaria uses, and it most closely describes the nature of the works carried out – construction and repairs. We have assumed that the construction sector has carried out the total value of the contracts under “construction works”.

³ As of January 2015 the minimum thresholds, under which the application of the public procurement procedures prescribed by the *Law on Public Procurement* is not obligatory, are: BGN 264,000 (approx. € 142,254) for works and BGN 66,000 (approx. € 35,564) for goods and services, exclusive of VAT. When the public procurement is carried out outside the country these thresholds are BGN 1,650,000, and BGN 132,000, respectively.

and the economy, their current and investment consumption is covered by the legal framework regulating public procurement.

On average, public procurement made up 9% of Bulgaria's gross domestic product (GDP) from 2007 – 2013 (Figure 1)⁴. While remaining small by EU standards, public procurement grew steadily from €1 billion in the early 2000s to a peak of just above €5 billion in 2009 before dropping to €3 billion in 2010 in the wake of the Eurozone economic crisis (Figure 2). It should be noted that both peak years of public procurement contracting since Bulgaria's EU accession – 2009 and 2013 coincided with parliamentary elections, which could be an indication of heightened risk of favouritism or corruption. The rise in public procurement contracts on an annual basis was not trivial and amounted to 5 percentage points of GDP in 2009 and 3 percentage points in 2013. Such increases in public procurement contracts in election years have been documented also before EU accession during the 2001 and 2005 parliamentary elections (CSD, 2006). This provides evidence that public procurement has been used by incumbent governments for winning electoral support in election years, which other things being equal, increases the risks of corruption.

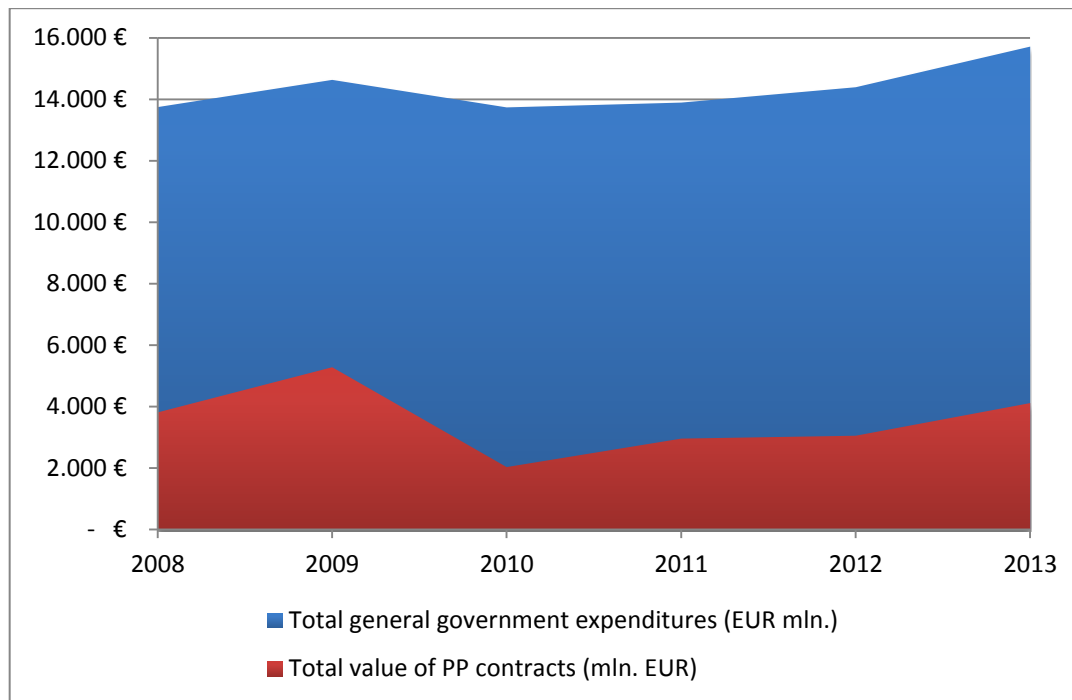
Figure 1. Share of total public procurement volume in GDP for the 2007 - 2013 period (%)



Source: NPA, NSI, 2014

⁴ The authors have taken all due care to ensure that the provided data is comparable across years. We have not detected any changes in the reporting system or legislation, which might bias the comparability of the data over time. If not mentioned otherwise explicitly all public procurement data in this paper refers to values exclusive of VAT.

Figure 2. Share of the total value of public procurement (PP) contracts in total general governmental expenditures (2008-2013)



Source: Eurostat, PPA, 2014

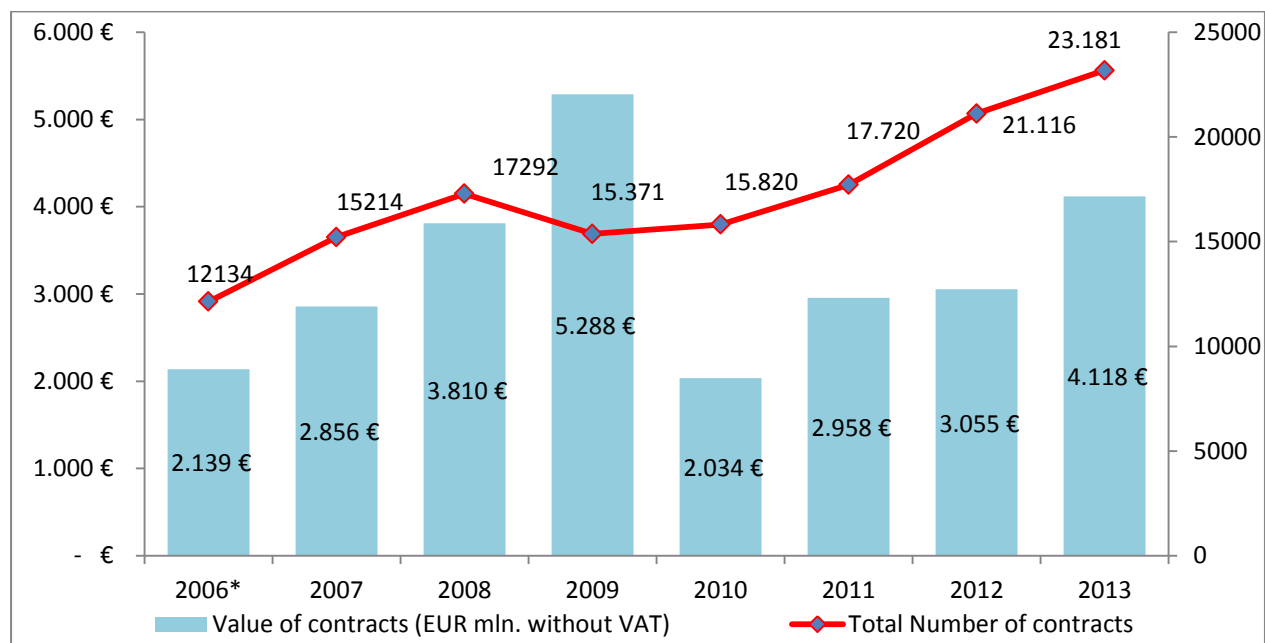
The lack of capacity on the part of the Bulgarian authorities to absorb European Structural and Investments Funds (ESIF), initially pre-accession and later on, has further contributed to the uneven dynamics of the Bulgarian public procurement market⁵. This has added pressure on the authorities to spend at any cost or decommission funds towards the end of the funds' contractual (2006 for pre-accession and 2013 for post-accession), and payment (2008 and 2015 respectively) periods⁶. The numerous irregularities in the management of the Programme of Community aid to the countries of Central and Eastern Europe (PHARE) and the Special accession programme for agriculture and rural development (SAPARD) pre-accession funds exposed by European Commission (EC) units, coupled with the lack of adequate systems of ex-ante (preliminary) and ex-post (follow-up) controls, and the tenuous response of the Bulgarian government to those findings, led to the forfeiture of EUR 220 million from the national PHARE programme, as well as to the freezing of EU funds earmarked for road infrastructure development in 2008 (Vachudova, 2009). Notably for the subject matter of this paper, the 2008 measures taken by the EC against Bulgaria were triggered by the uncovered blatant conflicts of interest in the road infrastructure fund, which had provided tenders to relatives of the then

⁵ Report from The Commission to the European Parliament and the Council On the Management of EU-funds in Bulgaria Brussels, 23.7.2008 COM(2008) 496 final.

⁶ EU Funds for catching up countries and regions are disbursed in 7 year budget cycles, with the current one encompassing 2014 – 2020, and the previous one – 2007 – 2013. The money designated for a particular budget cycle is spent under the so-called “n+2” rule, meaning that money has to be contracted at the latest by the year n (2013) and invoiced by the year n+2 (2015).

executive director⁷. Thus, the Bulgarian government was forced to spend the money designated for the years 2007 and 2008 in 2009 (an election year) (CSD, 2009). A similar or even higher peak of EU funds-related spending is expected to occur in 2014 – 2015, as funds have been frozen and unfrozen again in 2013 - 2014⁸, and 2015 is the last year, for which invoicing is allowed for the EU's 2007 – 2013 budget period.

Figure 3. Number and value of public procurement contracts in Bulgaria (2007-2013)



Source: PPA, 2014

The case of 2009 is of particular interest as the increase in volume has come on the backdrop of stagnant (and even declining from 2008 to 2009) numbers of public procurement contracts, indicating a rise in the value of individual public procurement contracts⁹ (Figure 3). Since then, the number of public procurement contracts has increased by some 50%, reaching 23,181 in 2013, which might signify some opening up of the market and stricter adherence to public procurement rules with the increase of the share of EU funds-related public procurement spending. EU funds have been playing an increasingly important role in the public procurement market, providing for roughly a quarter of all public procurement announcements¹⁰ in 2013 (Figure 4).

⁷ Mediapool.bg. (11 June 2014). *After five years of delays the case "Brother and Mate" is about to be solved (След пет години точене делото "Батко и братко" е на път да приключи)*. [WWW]. Available from: <http://www.mediapool.bg/sled-pet-godini-tochene-deloto-batko-i-bratko-e-na-pat-da-priklyuchi-news221362.html> [Accessed 21 March 2015].

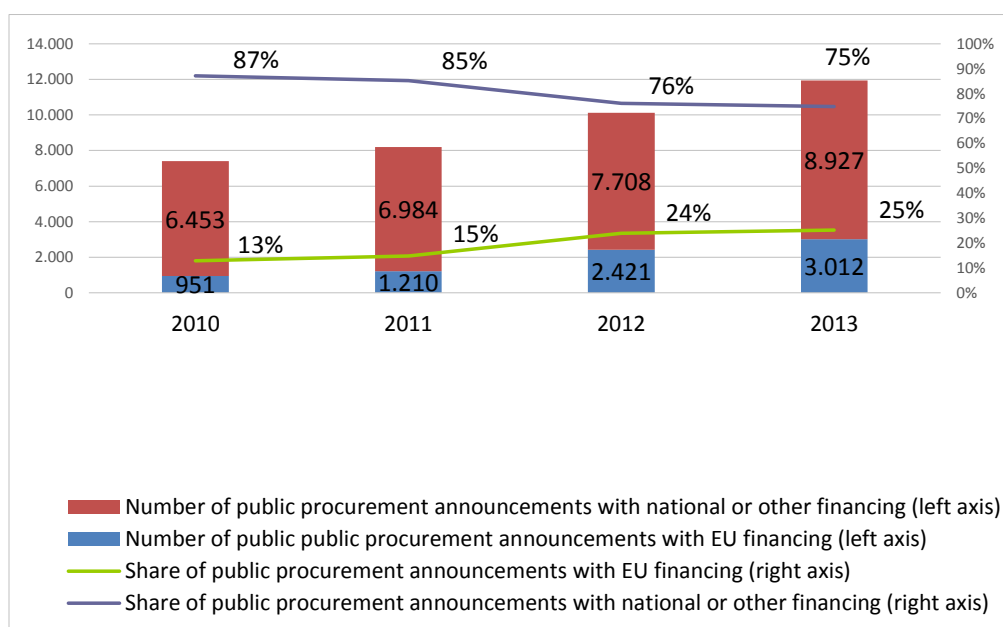
⁸ Novinite.com. (4 December 2014). *EU Unfreezes Bulgaria's Blocked Funds for Regional Development*, [WWW]. Available at: <http://www.novinite.com/articles/165213/EU+Unfreezes+Bulgaria%27s+Blocked+Funds+for+Regional+Development> [Accessed 20 March 2015].

⁹ The data refers to actual public procurement contracts and thus excludes the possibility of any increase or decreasing being the result of the signature of framework agreements. The latter are still very rarely used by the Bulgarian authorities.

¹⁰ Public procurement announcements are fewer than the actual public procurement contracts signed as many announcements contain lots, each requiring the signing of contracts, and/or foresee a framework contract with more than one entity.

The substantial financial EU assistance to Bulgaria in the 2007 – 2013 period coupled with the increased social pressure on the national budget expenditures due to the economic crisis have made it critical to the Bulgarian government to do its best to spend the available EU funds in their entirety. However, as the budget cycle drew to an end in 2013, and financial penalties and corrections imposed by the European Commission started to increase, the government has resorted to two practices, which have increased corruption risks in this domain: covering withdrawn EU funds because of penalties and/or freezes, and over-contracting the available EU funds' budgets (Table 1). In this manner the government wants to guarantee that the whole amount of EU funds available to the country will be invoiced by 2015 even if some of the projects are not approved or delayed, or altogether scrapped by the EC (43rd National Assembly of the Republic of Bulgaria, 2014)¹¹. This practice puts additional discretionary power in the hands of the government and the public administration as they get to decide, which projects receive national budget funds replacement for lost EU subsidies, and which not. Other things being equal, this additional discretion increases corruption risks.

Figure 4. Number of public procurement announcements by source of financing: national vs. EU (2010-2013)



Source: PPA, 2014

¹¹ See also media reports in Bulgaria, such as: BGNES. (11 March 2015). *The risky Europrojects in ecology and road construction will be financed through national budget funds also in the new programming period* (Рисковите европроекти в екологията и пътищата ще се финансират със средства от бюджета и новия програмен период), Available from: <http://news.bgn.es.com/view/1220883> [Accessed March 20, 2015]

Table 1. EU Structural Funds (over)contracting¹² (December 2014)

Operational Programme	Programme budget		Contracted amount
	EU funding (EUR mln.)	Number of contracts	EU funding (EUR mln.)
OP Transport	1 624	116	1 628
OP Environment	1 466	524	2 322
OP Regional Development	1 361	1 187	1 421
OP Competitiveness	988	3 153	1 018
OP Technical Assistance	48	120	51
OP Human Resources	1 032	5 213	1 076
OP Administrative Capacity	154	1 446	175
TOTAL	6 674	11 759	7 692

Source: Information System for Management and Monitoring of EU Structural Instruments in Bulgaria - public module, December 2014

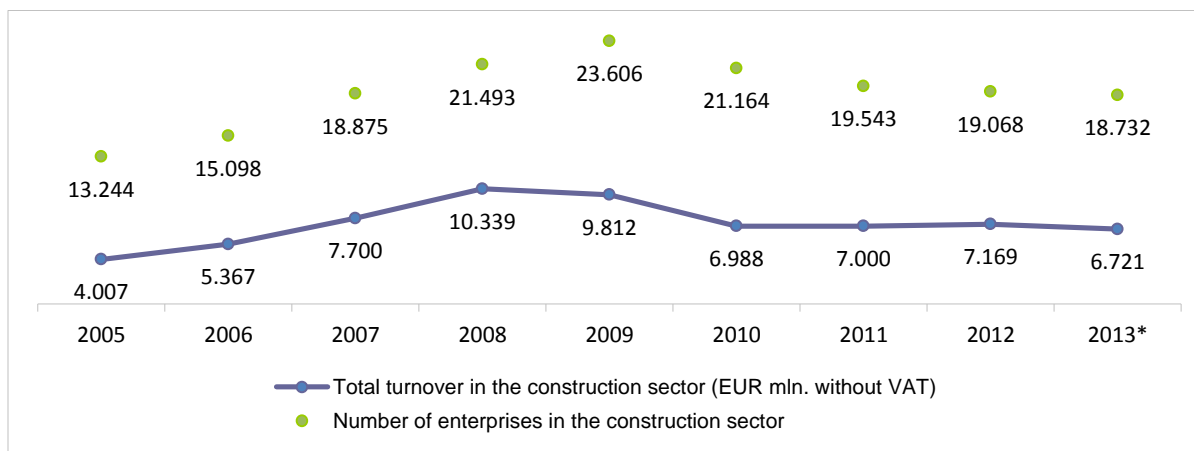
2. Key indicators of the Bulgarian construction sector

The share of the construction sector in the gross value added (GVA) of the Bulgarian economy amounted to an average of 7% in the 2007-2013 period. However, following the onset of the European economic crisis, its turnover has slumped by more than 30%, compared to its peak in 2008, reducing the share of the sector in total GVA to 5% in 2013.¹³ This has increased the dependence of construction companies, in particular larger ones, on public procurement contracts. Construction has been among the most affected sectors of the economy during the recent crisis following the bust of the real estate market in Bulgaria. By 2013 the number of active enterprises in the sector decreased by a fifth from its peak in 2009 (Figure 5).

¹² Over-contracting occurs when the contracted amount is higher than the programmed budget.

¹³ Based on PPA and NSI data for the period 2007-2013

Figure 5. Total turnover and number of enterprises in the construction sector (2005-2013)



Source: Eurostat, 2014; *the number of enterprises for 2013 is provisional

The sector has developed dynamically with the top 100 construction companies¹⁴ concentrating on average 31%¹⁵ of the total turnover of the whole sector during the 2008-2013 period (Figure 6). Less than one percent of the construction companies in Bulgaria have a combined average turnover of EUR 2.5 billion¹⁶. The firm level analysis, based on a sample of the top 40 construction companies (see Methodological note, section 4.1), showed that they controlled 15% of the total turnover of the sector in 2013. While this does not seem like a high concentration rate, it certainly implies that there are not many construction companies in Bulgaria that can handle larger public procurement contracts. It should also be noted that the sector is highly regulated, with its main sub-industries having their own industrial associations, which lobby openly both for legislative changes and for specific construction projects. For example in 2014 the Bulgarian Construction Chamber and the Bulgarian Branch Chamber “Roads” opposed the decision of the Bulgarian government to build a 15 km tunnel on one of the EU transport corridors in Southwest Bulgaria, while the Bulgarian Association for Geotechnical and Tunnel Construction lobbied in favour of such a solution¹⁷.

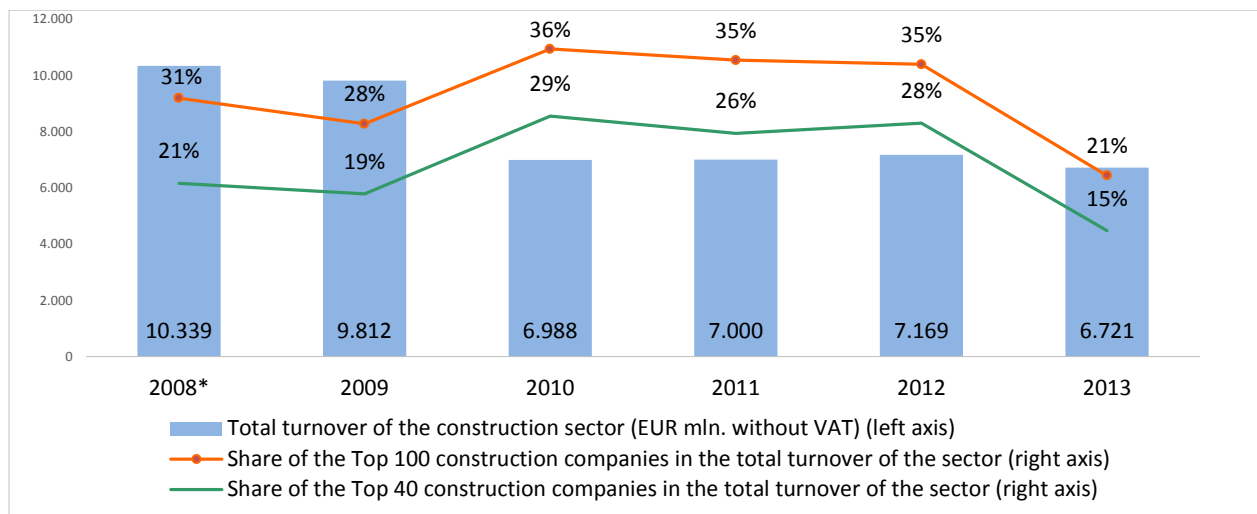
¹⁴ According to the official National Classification of Economic Activities

¹⁵ Excluding a single company which reported an annual turnover of EUR 1,731 million for 2008, with no reference values for 2009-2013

¹⁶ *ibid*

¹⁷ The Bulgarian Construction Chamber is by far the largest industrial association in the sector. It was created by a special law adopted on the last day before Bulgaria’s EU Accession (*Law on the Chamber of Construction Companies (Закон за камарата на строителството)*), promulgated in State Gazette 108/29.12.2006.). As of 2015 it assembles 1689 companies, 16 education organisations, and 7 non-governmental organisations. The chamber has 27 regional representations in the country. The chamber acts as a gatekeeper to the sector as it runs the Central Professional Registry. Among its main activities are: aiding the development of industry standards on health and safety; developing a Code of Professional Ethics; participating in the trilateral cooperation at branch and national level, and signs the collective labour contract; etc.

Figure 6. Share of the Top 100 and Top 40 construction companies by turnover in the total turnover of the construction sector (2008 - 2013)



Source: Eurostat, APIS, 2014; CSD calculations; *excluding a single company which mistakenly reported an annual turnover of EUR 1,731 million instead of 1.731 million for 2008.

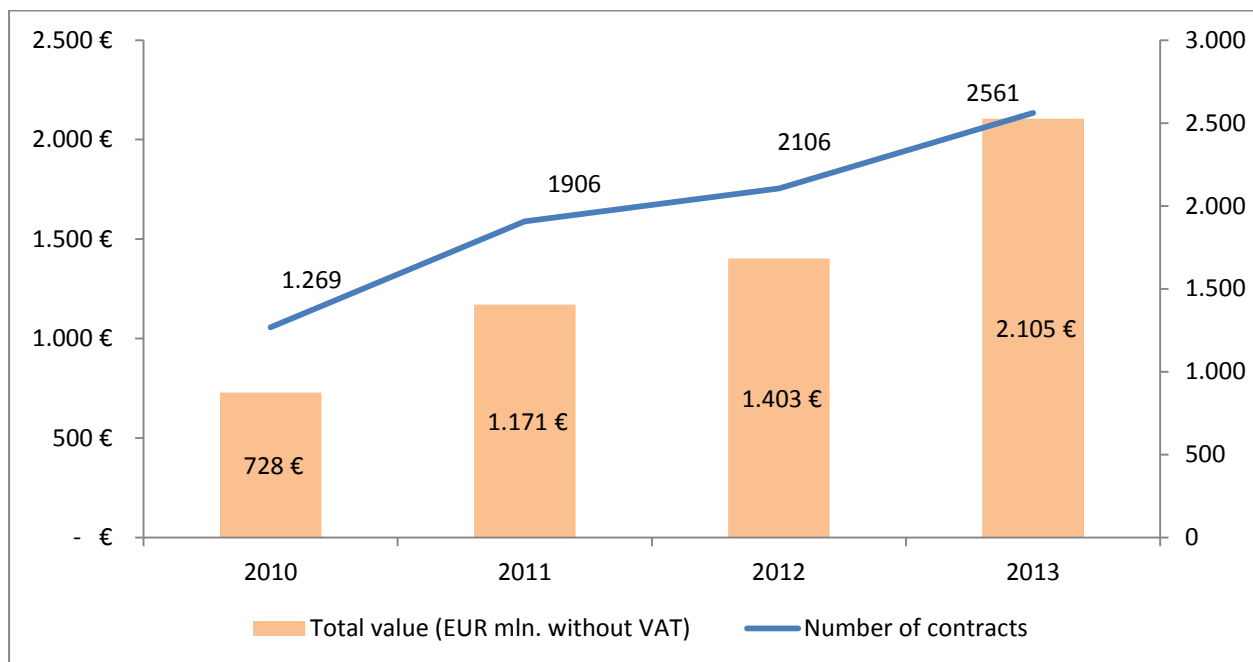
3. Public procurement trends in the Bulgarian construction sector¹⁸

Both the number and value of public procurement contracts for construction works marked a significant increase between 2010 and 2013 (Figure 7)¹⁹. The very low volume of public procurement of construction works in 2010 is attributable to the aftermath of the economic recession in Bulgaria of 2009, and the subsequent tightening of fiscal policy. But even in 2011 and 2012, there has been a significant (for the Bulgarian market) rise in construction works public procurement contracts in 2013. As discussed previously, this is almost entirely related to the rush for absorption of EU funds, since 2013 was the last year for contracting. In addition, 2013 was also an election year, which led to higher pre-election spending and a fiscal loosening by the newly elected majority in parliament. The data analysis shows that the increase in the number of contracts, on the one hand, and in their value on the other, is asymmetrical, signifying an increase in the value of individual contracts. In the four-year period construction works public procurement contacts increased their total value by close to 300%, while the number of contracts went up by 200% from 1,269 in 2010 to 2,561 in 2013.

¹⁸ The Bulgarian Public Procurement Agency assesses the functioning of the public procurement market by reporting several major indicators. The PPA groups public procurement according to its subject - goods, services and construction works. We used the data for "construction works" for the purposes of the current analysis of the general public procurement market in construction.

¹⁹ Publicly available data on construction works contracts is available only for the past four years at the web-site of the Public Procurement Agency. The Annual Reports of the Agency for the 2008 and 2009 years do not provide comparable data to the one available online on construction works.

Figure 7. Number and value of public procurement contracts for construction works (2010-2013)

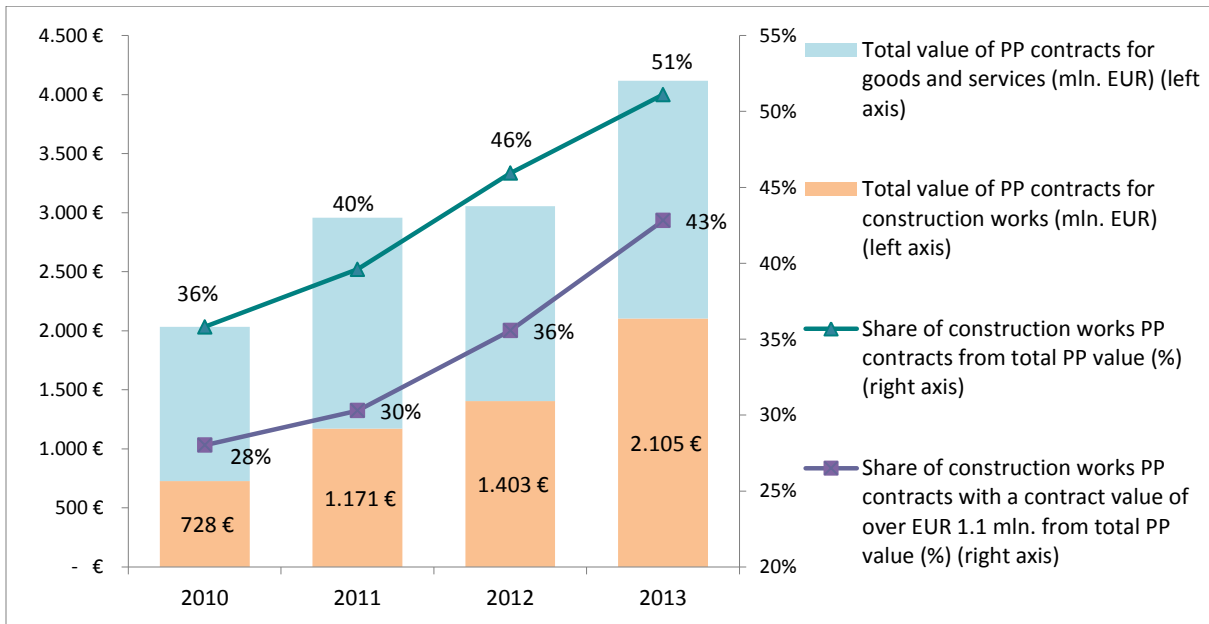


Source: PPA, 2014; CSD calculations

In 2010 – 2013, there was a clear trend of concentration of public procurement contracts in construction works vis-à-vis the supply of goods and services, and in larger value contracts within construction works. While in terms of numbers the share of the construction works contracts has remained relatively stable, their share in the total value of public procurement contracts has increased steadily to over 50% in 2013 (Figure 8). In 2013, the 2,561 construction works contracts represented 11% of all public procurement contracts and 51% of their total value. This rising concentration of public procurement in construction works has been attributable entirely to the rise of large-scale public procurement contracts²⁰. Large-scale contracts for construction works, with a single value above €1.1 million have risen to 43% of the total public procurement value in Bulgaria. The total value of all large-scale contracts for construction works increased to EUR 1,763 million in 2013, with the average value of a single contract exceeding EUR 6 million.

²⁰ The PPA uses the following thresholds for classifying the size of public procurement contracts in goods, services, and construction works: EUR 0 - EUR 102,258; EUR 102,258 - EUR 1.1 mln.; above EUR 1.1 mln. The latter are considered large contracts and undergo a specific pre-screening by the PPA.

Figure 8. Share of total public procurement contracts for construction works and public procurement contracts for construction works over EUR 1.1 m. from total public procurement value (2010 - 2013)



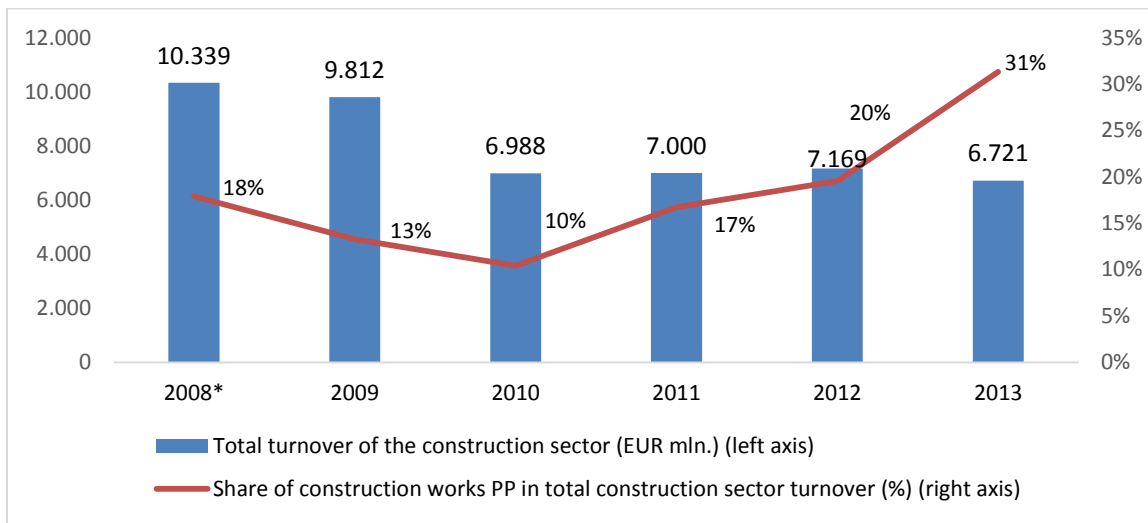
Source: PPA, 2014; CSD calculations

The concentration in large-scale construction works on the public procurement side, coupled with falling overall turnover and value-added in the construction sector, following the onset of the European economic crisis, has resulted in a substantial increase in the importance of public procurement for the construction sector in the 2010 – 2013 period. In 2013 the total public procurement value for construction works reached 31% of the total construction sector turnover, making the public administration effectively the key customer and decision maker in the survival of construction companies (Figure 9). The leverage power of the public administration over the resources available to construction companies has increased substantially, which in the absence of rising deterrence on corruption, implies rising risks of corruption or favouritism. There have been numerous media reports showing a concentration of public procurement among larger companies²¹, and different practices the public administration uses to channel specific public procurement contracts to specific companies besides wide interest among many competitors²².

²¹ See for example Koycheva, Maria. *Eight companies have split among themselves public procurement construction contracts for 1.4 billion leva* (Осем фирми са си поделили поръчки за 1,4 млрд лв. в строителството). Sega daily online edition. Available from: http://www.segabg.com/article.php?id=663140&utm_source=flip.bg [Accessed on 20 March 2015]. The article quotes a Bulgarian MP noting that in 2013, eight companies won public procurement contracts worth 1.35 billion Bulgarian lev from a total of 2 billion lev available for the construction sector.

²² See for example Georgiev, Ognian. (20 February 2015). *Theory and Practice of Manipulation* (Теория и практика на манипулацията). Capital Weekly online edition. Available from: http://www.capital.bg/politika_i_ikonomika/bulgaria/2015/02/20/2476819_teoriia_i_praktika_na_manipulaciata/ [Accessed 20 March 2015].

Figure 9. Share of construction works public procurement in total construction sector turnover (2008 - 2013)



Source: PPA, 2014; CSD calculations

The concentration in the public procurement of construction works in recent years seems to contradict a trend of opening up of the public procurement market in terms of number of contractors and awarding entities. Although more in-depth analysis is needed to validate this statement, the macro level data shows that the number of awarding entities doubled in the period 2009 – 2013, while the number of contractors increased by 25 to 30% (Table 2), which is normally associated with a rising and vibrant market and competition. While this has improved the value for money proposition in competitive markets, it has also made it more difficult for compliance and control authorities to check for irregularities (CSD, 2014). One should also take into account legislative changes, which have increased the requirements for open tendering among private recipients of EU funds, without any direct effect on the transparency and accountability of public sector contracting.

Table 2. Public Procurement Contractors, Announcements and Contracts in Bulgaria (2010-2013)

	2010	2011	2012	2013
Number of awarding entities	2 585	3 217	4 662	5 302
Number of contractors	14 700	16 347	18 257	20 490
Total number of public procurement announcements	7 404	8 194	10 129	11 939
From this sum: above the EU threshold	1 599	2 022	2 570	3 653
From this sum: with EU funding	951	1 210	2 421	3 012
Public procurement announcements in construction works	1 056	1 177	1 552	1 791

Public procurement announcements in supplies	3 463	4 025	4 679	5 162
Public procurement announcements in services	2 877	2 989	3 888	4 986
Number of contracts	15 755	17 579	20 813	22 779

Source: PPA, 2014

Municipalities, predominantly through ESIF financing, have become some of the biggest contracting authorities for construction works. Naturally, among them, Sofia municipality, also acting through Metropolitan EAD, which is the public company in charge of the Sofia metro construction, redistributes the largest number and value of public procurement contracts in the construction sector. Highly ranked in terms of number and value of awarded contracts are also public entities, specializing in construction, such as the National Railway Infrastructure Company and the Road Infrastructure Agency (RIA). The dependency on EU funding for public procurement in the construction sector is further evidenced by the fact that the above mentioned four public entities alone are the largest ESIF beneficiaries with a total of 152 projects amounting to EUR 3.7 billion.²³ The distribution of ESIF projects among public bodies, in particular municipalities, to further contract them out to the private sector has created risks for favouritism – picking up only contracting authorities, which fall in line with the political majority of the day.

4. Firm level analysis of public procurement in the construction sector

4.1. Methodological note

The firm-level analysis presented in this paper is based on a manually constructed database using a sample of the top 40 construction companies, ranked according to their total turnover for the period of 2008 - 2013²⁴. The database includes information on the number of public procurement contracts for construction works, awarded to the selected companies, based on Common Procurement Vocabulary (CPV) classification codes 44, 45 and 71²⁵. For each contract the database contains the following variables: forecast value; contract value; year of award; type of procedure; type of funding (national vs EU); information on subcontracting; number of received offers; name of contractor; and type of awarding body (conventional or sectoral).

For the purposes of simplification of calculations, we have assumed that the contract value has been paid in full during the respective year of the award. Although this is a strong assumption, it

²³ The data is for all ESIF programmes in Bulgaria, as of 14 December 2014. More information is available from: <http://umispublic.government.bg/> [Accessed 14 December 2014].

²⁴ Despite repeated requests under the Access to Public Information Act and the sending of several official letters for obtaining specific indicators for all public procurement contracts in the construction sector, the Bulgarian Public Procurement Agency (PPA) has not responded, and has effectively refused to provide the requested information.

²⁵ These three CPV codes relate most closely to construction. They have been used also in other ANTICORRP analyses, e.g. see Fazekas, M., Toth, 2014.

ensures the comparability of data within the investigation period. This assumption would certainly affect the calculation of the actual turnover of the companies implying that the contracts, which have longer implementation times, contribute lower shares to a company's annual turnover, other things being equal. However, it does not impact the core interest of the analysis that lies in the timing of the decision on committing public funds and their volume, which happens in the year of the signing of a public procurement contract. In very rare cases, where there is no information on the contract value but there is data available on the amount of funds actually paid out during the respective year, the latter is included instead. Public procurement, not referring to the selected CPV codes is excluded from the analysis. Some of the companies included in the top 40 of the construction sector have much high turnover from work unrelated to construction activities, such as utilities, etc. Data on these companies includes only procurement contracts for construction.²⁶ Such companies include sectoral operators in the energy sector, water supply, transportation, and postal services, which bid for procurement contracts for construction works but primarily operate in procurement within their specific sub-sectors.

For a more comprehensive analysis, the firm level data encompasses the construction procurement contracts awarded to third companies (hereafter referred to as linked companies), in which the selected sample of top 40 has equity ownership. The value of each public procurement contract, awarded to a linked company is recalculated depending on the percentage of ownership of the respective primary company, included in the sample. Other (softer) types of dependency between top 40 construction companies and third parties (e.g. participation in the board of directors or similar governance structures) is not considered, and as a result, public procurement contracts, awarded to such related companies are excluded from the analysis.

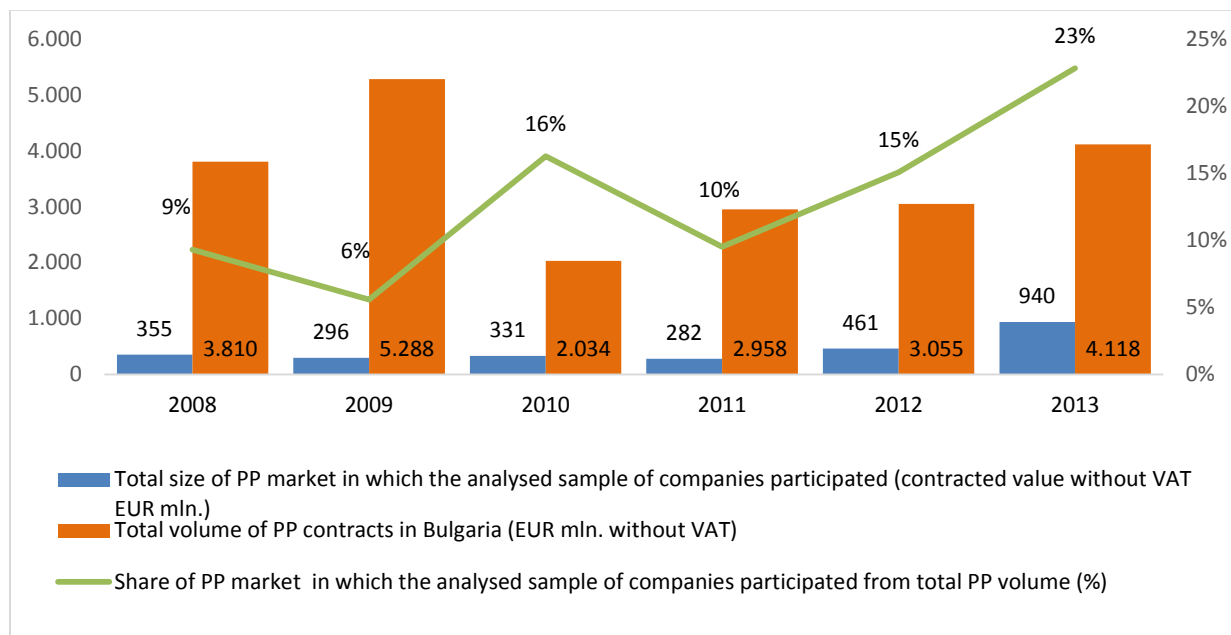
4.2. State of play – public procurement dynamics of the top 40 construction companies

In 2013 the top 40 construction companies controlled 23% of the total value of the public procurement market in Bulgaria, which is more than double their share in the last pre-crisis year 2008 (Figure 10). The total value of the public procurement market of the top 40 construction companies amounted to EUR 2.7 billion for the 2008 – 2013 period. The rapid rise in the volume of the market in 2012 and 2013 can be explained with the accelerated absorption of ESIF financing, a considerable part of which was dedicated to construction and infrastructure projects (Figure 11). After the economic crisis, EU funding clearly displaced national funding in large-scale public procurement of construction works, which theoretically should have improved the quality of procurement and control. However, as it is unlikely that institutions or the governance regime can change dramatically in only three years' time, and research has demonstrated they have not (CSD, 2014), one can expect that this rise of the EU funding share has led to the transfer of inherent public procurement corruption risk to the EU funds realm. This has likely been exacerbated by the fact that municipalities have become the main contracting authorities for the top 40 construction companies (Figure 12). Financial corrections on EU funded projects imposed by the EC and/or delays in reimbursement of funds have led to the deterioration of the

²⁶ Using CPV classification codes 44, 45 and 71

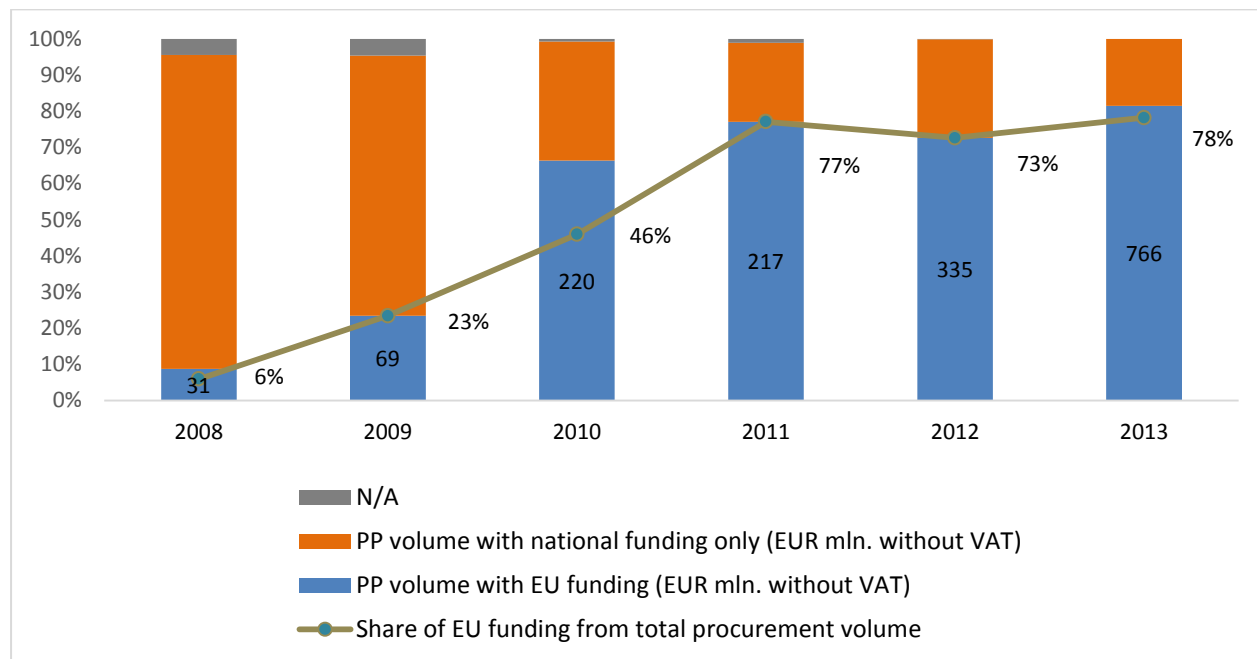
financial viability of municipalities. This in turn has made them more and more dependent on central budget subsidies, which is particularly true for smaller municipalities with no or insufficient funding base of their own.

Figure 10. Value of the public procurement market of the top 40 construction companies*



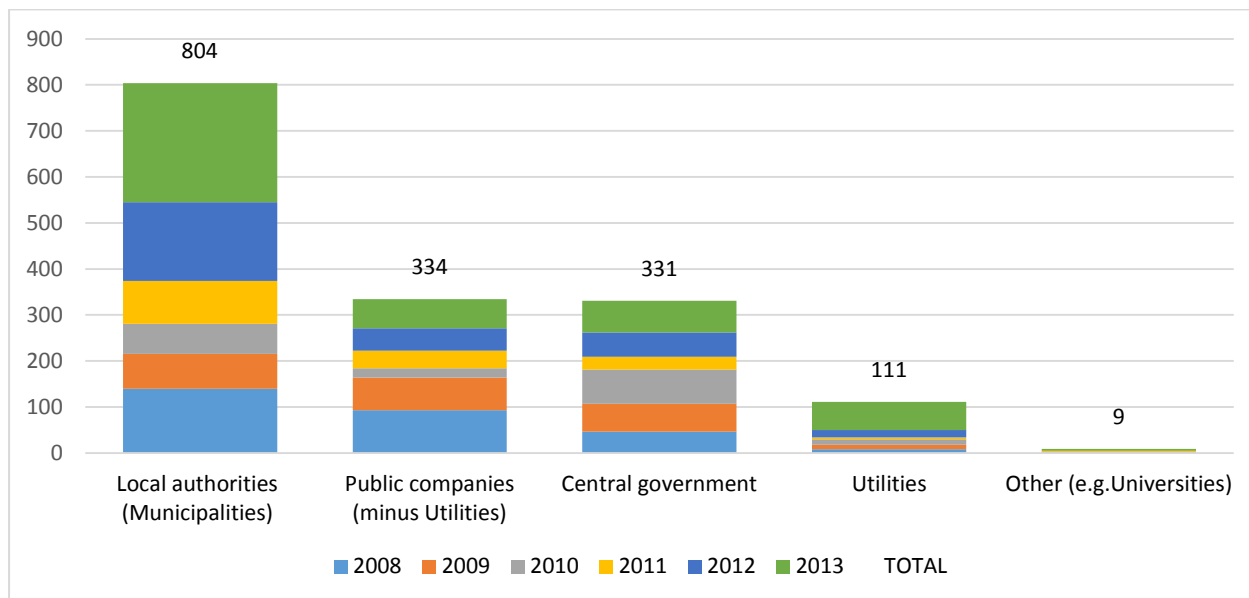
Source: PPA, CSD calculations; * excluding duplicates, i.e. large scale public procurement contracts, in which two companies from the selected sample took part.

Figure 11. Weight of the EU funding in the public procurement market value of the top 40 construction companies*



Source: PPA, CSD calculations; * excluding duplicates, i.e. large scale public procurement contracts, in which two companies from the selected sample took part.

Figure 12. Type of contracting authorities, which have awarded public procurement contracts to the top 40 construction companies (EUR million without VAT)



Source: PPA, CSD calculations.

III. NATIONAL PROCUREMENT LEGISLATION AND PRACTICE

1. Evolution of the Bulgarian legal framework: legislative efforts for increased transparency versus corruption practices

The Law on Public Procurement in Bulgaria identifies three major principles underlying the legal framework of public procurement, all related to anti-corruption and elements of the good governance regime: openness and transparency; free and fair competition; equal treatment and non-discrimination. These criteria serve as a point of departure in the evaluation of the corruption risk level, as well as in the identification of the most vulnerable aspects of the legal framework in the public procurement sphere.

After 1999 the legal framework of public procurement in Bulgaria has been mostly influenced by harmonization with the changing European legislation. The Law on Public Procurement (LPP) from 1999 has been replaced by a new one from 2004 following the adoption of two new directives on public procurement in the EU in 2004.²⁷ Upon EU accession Bulgaria had to repeatedly adjust its legislation to the developing *acquis communautaire*. The public procurement regime of Bulgaria was considerably liberalized. For instance, the scope of

²⁷ Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts (often referred to as “the Public Sector Directive”) and Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procedures of entities operating in the water, energy, transport and postal services sector (often referred to as “the Public Services Directive”).

application of the LPP was narrowed and the value thresholds, above which the law's prescriptions became obligatory, were almost trebled. The contracts below the thresholds became subject to easier procedural rules set out in the Regulation on Small-Scale Public Procurement (RSPP), which was later abolished in 2012.²⁸ In 2006 Bulgaria embarked on a major overhaul of the main control mechanism over public procurement – the public internal financial control. The then existing unitary centralised body for inspecting public procurement of all state institutions and companies has been decentralised, with a much smaller central authority – the Public Financial Inspections Agency, and many independent internal audit units within the respective state authorities, e.g. municipalities. The reform has considerably weakened oversight in the short-term but has laid the ground for a more modern, risk-based approach to uncovering public procurement irregularities.

On 11 February 2014 the European Parliament and the Council adopted a revision of Directives 2004/17/EC and 2004/18/EC, as well as a directive on concession contracts²⁹. The Member States have until April 2016 to transpose the new rules into national law. In 2014 Bulgaria amended the LPP, with several of the changes claiming to address particular corruption risks. A key role in the new legislative texts is attributed to the development of electronic platforms for e-public procurement. For instance, contracting authorities are now required to maintain a full electronic dossier on their websites, including tender documentation, but also records of the meetings of the tender commission, contract and annexes.³⁰

Several of the 2014 legislative amendments more directly affect the public procurement practice in the construction sector. Actions have been undertaken to restrict the weight of the “lowest price” criteria in awarding contracts³¹, as selection will be based on indicators for comprehensive assessment, publicly available in the announcement of the public procurement procedure (Boneva, K., 2014). Lowest price criteria is completely prohibited for certain design and construction public procurement.³² Requirement for publication of forecasted value in the public procurement announcements³³ is a complementary transparency measure against operators bidding with artificially lowered prices. Changes also affect the format of the evaluation committees, which, in the case of public procurement for construction works equal or above the threshold of EUR 5 million, will include one external expert, randomly selected from a list of pre-approved experts.³⁴ Measures were also taken with regard to the vicious practice of companies suspending contracts with their sub-contractors close to the end of the project, in order to avoid payments. The amendments provide guarantees that the contractual agreements between the parties involved will be kept.

²⁸ Regulation on Small-Scale Public Procurement. (Prom. SG. No. 84 of 27 September 2004, repealed SG. No 17 of 28 February 2012). Available from: <http://lex.bg/bg/laws/ldoc/2135492182>

²⁹ Official Journal of the European Union L 94/1. Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts. Available from: <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0023&from=EN> [Accessed 10 December 2014].

³⁰ Chapter II, Art. 22(b) LPP

³¹ Art. 37 LPP

³² Art. 37 (2) LPP

³³ Art. 25(2) and Art. 25(3) LPP

³⁴ Art. 34(2) and Art. 34(b) LPP

The Bulgarian Construction Chamber has publicly voiced disagreement with the enacted changes, which the chamber will seek to overturn in a new drive for LPP changes in 2015³⁵. The Bulgarian Construction Chamber has sent an official letter to the Deputy Prime Minister in charge of the economy and EU matters, in particular objecting to the law's requirements not to change sub-contractors and contract clauses in the implementation phase. Both changes to the law have been enacted in 2014 to preclude the use of what has been seen as two major venues for legal corruption (Kaufmann and Vicente, 2005) in public procurement. Before the enactment of the changes, administrations often awarded construction works based on the lowest price offered only but then changed the contract *post factum* during the implementation phase by signing addendums, and effectively increasing the cost of the works. The risks of legal corruption seem to be confirmed by the very high number of legislative changes introduced to the Bulgarian public procurement legislation citing EU legal approximation. Although the EU has enacted only two major changes in public procurement in the past decade, Bulgarian lawmakers have introduced a total of 27 sets of amendments to the public procurement law since 2005.

2. Control Mechanisms

Checks by the PPA, the National Audit Office (NAO) and the Public Financial Inspection Agency (PFIA) are the key instruments in ensuring transparency in public procurement. The violations of the public procurement law and procedures uncovered by the PFIA remain very high, signifying high corruption risks (Table 3). The capacity of the Agency to tackle problematic public procurement increases, but its deterrence and prevention effects are very limited and violations continue to be widespread. One reason is the constant political interference in the work of the agency, in particular in bigger public procurement contracts. In addition, it remains unclear what the role and impact of the decentralised internal financial control bodies is, which have inherited 9/10ths of the personnel of the former centralised stated internal financial control after the 2006 reform (see above). The NAO has sweeping audit authority but lacks investigative powers (Stoyanov A., Stefanov R., Velcheva, B., 2014).

Table 3. Inspection results of the Public Financial Inspection Agency (2007-2013)

Year	Volume of the inspected public procurement contracts (EUR million.)	Number of public procurement contracts with discovered violations	Volume of the public procurement contracts with discovered violations (EUR million.)
2013	2 333	1 376	918
2012	1 045	1 235	761
2011	746	821	54
2010	1 126	807	609

³⁵ The letter is available in electronic format on the web-site of the Bulgarian Construction Chamber here: <http://www.ksb.bg/images/NOVO1/PredlojeniKSB.pdf>

2009	554	724	337
2008	325	706	156
2007	527	776	307

Source: PPA Annual Reports; PFIA Annual Reports, 2013.

The ex-ante control performed by the PPA shows similarly high number of violations as in the PFIA case. Some 30% of the checked procedures were not fully compliant with the law (Table 4). After the recent LPP amendments, the ex-ante control performed by the PPA encompasses not only ESIF-funded procedures over EUR 1.3 million but also nationally financed public procurement for construction works equal to or above the threshold of EUR 5 million. Additionally, though not required by European legislation, contracting authorities in Bulgaria have been obliged to publish the notifications for opening negotiated procedures without notice, another major corruption risk area. The electronic Public Procurement Registry (PPR) makes these documents available for public scrutiny.³⁶ In parallel, the PPA is required to perform ex-ante control of the documentation in all cases of public procurement involving negotiated procedures without notice.³⁷

Table 4. Results from PPA's ex-ante control of documents from negotiated public procurement procedures without notice

	Number of procurement documents
The selected procedure is fully compliant with the law	2513
The selected procedure could be considered compliant with the law if the Contractor presents sufficient additional evidence	695
The selected procedure cannot be considered compliant with the law or the evidence is not sufficient	461
The selected procedure is not compliant with the law	159
No position available (suspended procedure)	127
Total	4351

Source: PPA, 2014.

The new legislative provisions from 2014 establish two distinct platforms with a view of facilitating full access to information necessary for carrying out control activities on the part of the competent authorities. An "E-Monitoring"³⁸ platform will collect, archive and ensure online access to the protocols from all committees related to carrying out of public procurements, the

³⁶ National Strategy for Development of Procurement 2014 – 2020, available from <http://www.strategy.bg/FileHandler.ashx?fileId=4826>

³⁷ Art. 20(b) LPP

³⁸ Art. 126(a) LPP

framework agreements, the contracts between the contractors and the service providers, the additional agreements annexed to the contracts, and the subcontracting documents. An “E-Audit”³⁹ platform will allow physical persons and institutions to present in a structured way signals for deviation from the legal procedures of the PPL and the implementation of the contracts (Markov M., Dimova E., Aleksandrov A., 2014).

From a policy perspective, the 2014 Co-operation and Verification Mechanism report of the European Commission (EC COM(2014) 36 final) notes that in the area of public procurement, a complex and ever changing legislative framework has made it even more difficult to create a culture of objectivity and rigour. The e-procurement system still has limited functionalities. Some business voices are losing confidence that the tide of manipulation of tenders can be stemmed. The report also underlines that the ex-ante checks by the Public Procurement Agency are limited in scope, which raises questions as to their effectiveness. More importantly, however, there are doubts about the effective enforcement of rules and the application of sanctions. At the same time companies and industrial associations complain of job losses and bankruptcies (for example in the construction sector) due to rigged public procurement contracts that leave no work for the smaller or law-abiding companies.

To address these challenges, a governmental strategy for the development of the public procurement sector for the 2014-2020 period foresees centralized procurement for central and municipal public structures and electronic procurement in various spheres.⁴⁰ A new framework law on public procurement, expected in the first half of 2015, is also in preparation with the aim of fully reflecting the newly adopted EU requirements.⁴¹

IV. DETECTING CORRUPTION RISKS

So far the analysis of corruption risks in public procurement in Bulgaria have been based primarily on two supplementing traditional economic models: (a) the principal-agent model; and (b) the classical individual behavioural model. The former explains the opportunities for gaining private benefit by disposing of taxpayers’ money. Within the framework of this conceptual construct, the measures to counteract abuses in the management of budget spending are primarily related to making the mandate more specific, i.e. providing the details with regard to the responsibilities of contracting authorities in the public procurement process and reducing the scope of administrative discretionary powers in the contract awarding process. The classical individual behavioural model stems from the expected personal benefit and the individual price that the perpetrator expects to pay, depending on the likelihood of detection and punishment. Hence, counteracting measures are most likely to be effective if implemented at the level of individual incentives and disincentives concerning the corrupt interaction between the bribing party and the bribed party (Pashev. K., Dyulgerov A., Kaschiev A., 2006).

³⁹ Art. 126(b) LPP

⁴⁰ National Strategy for Development of Procurement 2014 – 2020, available from <http://www.strategy.bg/FileHandler.ashx?fileId=4826>

⁴¹ Action plan for the implementation of the National Strategy for Development of Procurement 2014 – 2020, available from http://www.aop.bg/fckedit2/user/File/bg/novini/Plan_OP.pdf

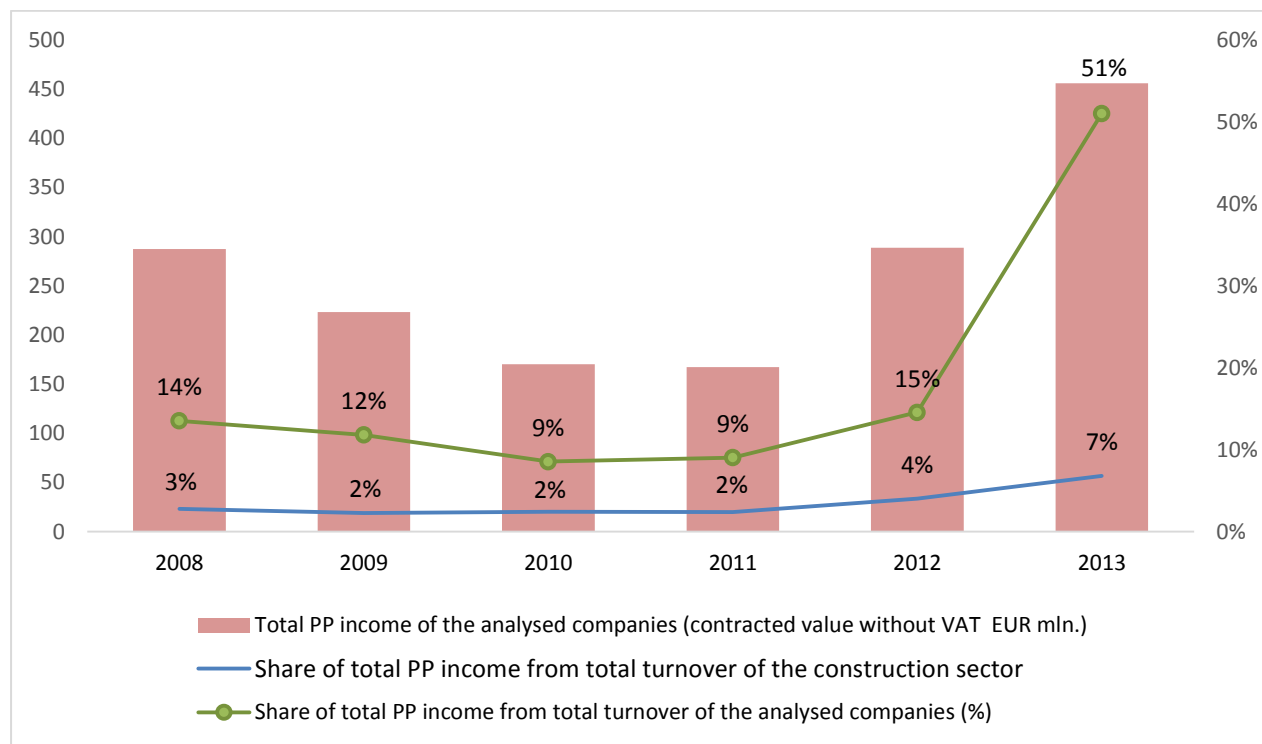
These traditional models regard corruption as an individual trait, and as a deviation from the norm, which is typical for well-established western democracies. They are less helpful in guiding anti-corruption reform policies in societies, in which corruption is still so widely spread that individuals believe it is the norm, which is the case in most new EU member-states, and in particular in Bulgaria (Mungiu-Pippidi, 2011). In this case, governance-based models seem more appropriate for detecting corruption risks. These analyse corruption risks as stemming from a set of institutional characteristics, which either provide resources/opportunities for corruption (e.g. more and larger public procurement contracts awarded through non-competitive procedures to a small set of pre-determined winners, with no independent oversight, nor proper judicial or civil control, etc.) or constraints/control of corruption (e.g. well-functioning system of competitive public procurement with many competing bidders, with systematic oversight and punishment of corrupt behaviour and preventive measures, etc.) (Mungiu-Pippidi, 2013). With its EU membership Bulgaria seems to have embarked on a course towards open access order (or a good governance model), which EU funds and peer pressure from other EU members are supposed to help bring along faster. But the majority of international and local assessments concur that Bulgaria's distribution of resources remains particularistic, with citizens perceiving corruption as the norm, which has impacted the very mechanisms meant to stem it, such as EU funds' management. (Stoyanov, Stefanov, and Velcheva, 2014).

1. Economic dependencies and corruption risks in the Bulgarian construction sector

Bulgarian construction firms have grown increasingly dependent on national and European public funds for revenues and growth, making them vulnerable to corruption pressure. As described above, the decline in the private sector opportunities related to the continuing economic stagnation following the European economic crisis of 2009 has led to the flocking of construction companies to public sector contracts. This coincided with the end of the first full EU budget cycle (2007 – 2013), in which Bulgaria took part, which necessitated an acceleration of EU fund absorption. As the importance of public procurement for construction companies grew, increasing their motivation to engage in non-market advantage seeking, the size of the individual public procurement contracts grew, providing the public administration with control over larger resources. Public procurement contracts have grown even larger for the top 40 construction companies. In 2013 public procurement awarded to the top 40 construction companies made up half of their total annual turnover (Figure 12). Hence, companies' success in achieving growth hinged to a very high degree on their ability to secure public procurement contracts. This in turn increases their sales officers' motivation to apply corruption pressure on the administration to secure public procurement contracts. The stagnation in the private construction market has on the other hand empowered the public administration to influence profits in the private infrastructure construction sector, which has provided it with additional leverage to extract illicit payments. While arriving at specific cases of particularistic distribution of public resources would require deeper case-study analysis, the review of the data derived from CSD's database on awarded public procurement contracts to the top 40 construction companies by turnover for the 2008 – 2013 period has allowed us to show that corruption risks in the public procurement in

construction in Bulgaria have risen in the 2008 – 2013 period. From the available data though we cannot ascertain whether these risks materialised in higher corruption.

Figure 13. Share of public procurement revenue from construction works in the total turnover of the top 40 construction companies (2008 - 2013)

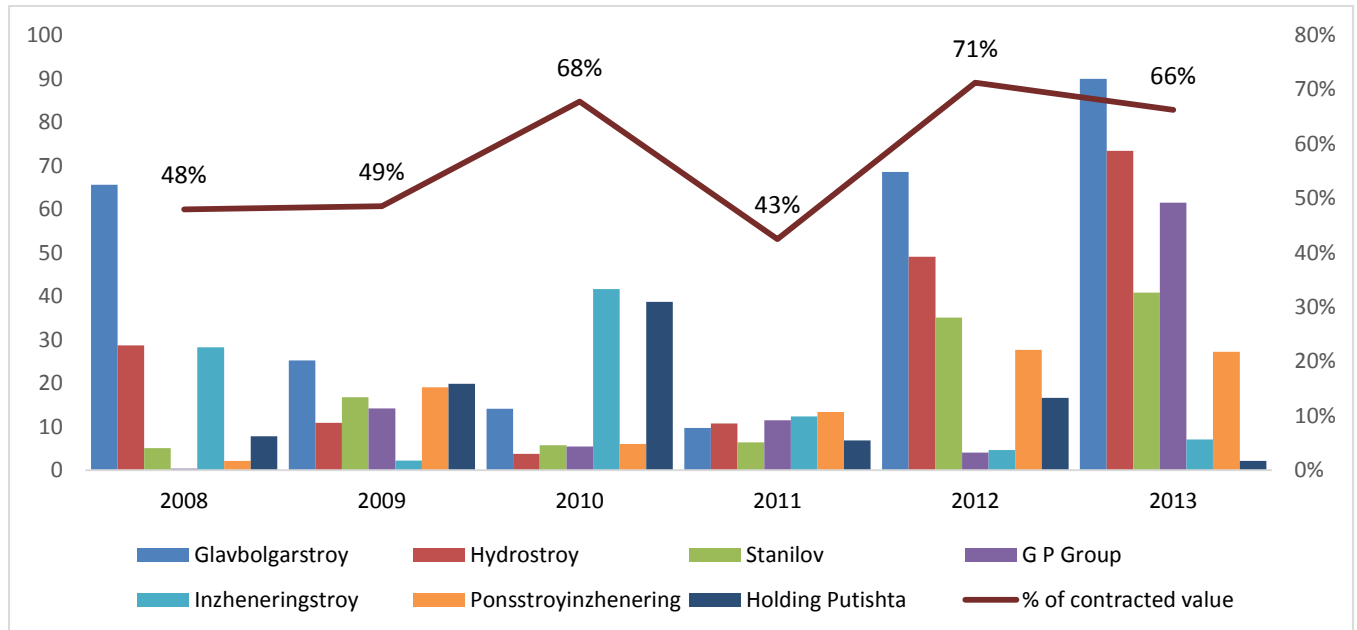


Source, PPR, Commercial registry, CSD calculations

Despite some progress noted, the overall inefficiency of administrative control over the implementation of mushrooming infrastructure projects could allow companies to more easily lower quality standards, thus both saving money and creating artificial demand for their future services, as badly built infrastructure deteriorates at faster rates. Savings stashed through lowering infrastructure quality could later be used to ensure support from the public administration by means of bribes for further projects of the same company. The country might in this manner drag itself into an infrastructure trap, maintaining high infrastructure expenditures as a share of GDP, yet continuously lagging behind average European levels in terms of both quality and quantity (CSD, 2009).

The analysis of the top 40 construction companies participating in the public procurement market demonstrates that few big companies controlled a significant portion of the market during the last five years. The top 7 construction companies in terms of awarded public procurement contracts commanded more than 2/3 of the public procurement contracts for construction works awarded to the top 40 companies. The top seven companies move significantly above the average sample values, both in terms of number of contracts and, especially, with regard to overall contracted value (Figure 13).

Figure 14. Public procurement revenue from construction works of the top 7 construction companies (EUR million left axis) and their share in top 40 construction companies' public procurement revenue (right axis) (2008 - 2013)



Source: PPR, Commercial registry, CSD calculations

The slightly lowered average ratio between forecasted and contracted prices, coupled with the limited number of restricted tenders and the competitive number of offers (5 on average) indicate high levels of competition among companies for winning public procurement contracts, which is also associated with higher leverage on the side of the public administration, as its monopsony power rises. Hence, one would assume that other things being equal, the opportunities for rent seeking have increased on the part of the administration, while they have decreased on the part of the participating companies, potentially producing a better overall outcome for society compared to the situation prior to the economic crisis. This would hold true if the quality of the implemented contracts remained constant or improved too, which cannot be ascertained at this point from the available data.

Previous studies have shown that companies tend to learn their lessons from participating in unsuccessful public procurement by withdrawing from subsequent bidding. With time fewer and fewer companies take part, and the market becomes monopolised by few players taking turns in winning public procurement contracts (CSD, 2007). Forms of corruption, which are more subtle and difficult to detect and counteract, such as favouritism, replace bribery in ensuring allocation of public procurement (Mungiu-Pippidi, 2011). Similar concentration of public procurement in such more subtle forms of influence seems to have taken place in the construction sector in Bulgaria. The top 7 largest enterprises have come to dominate the construction works market. Two of the companies (Glavbolgarsroy and Hydrostroy) have emerged as clear leaders in this respect, with the former winning contracts worth 20% of the total public procurement contracts value of the top 40 construction companies. All seven top construction companies have seen relatively stable performance or resilience vis-à-vis government changes (Figure 14). However,

market concentration has been visible even among the top 40 construction companies with three of the top 7 (Hydrostroy, GP Group, and Stanilov in this order) being the biggest in 2010 – 2013 political period (GERB right of centre minority government) compared to the 2008 – 2009 period (BSP centre-left coalition government). The first two companies added almost 5 pp to their shares in total top 40 public procurement contracts value, and the third one added almost 4 pp, while at the same time winning more and larger contracts. While, it is not possible to draw conclusive arguments from the available data, research has shown that cases of big road and energy infrastructure development projects have demonstrated that political patronage continues to play a role in winning larger public procurement contracts in Bulgaria (CSD, 2012).

2. Public procurement in the Bulgarian energy sector: corruption and state capture risks

Public procurement plays a substantial role in a number of activities related to energy – from building new power plants and purchasing materials and consumables to awarding consultancy and financial services. In public procurement energy enterprises act as contracting authorities in two cases: when they are public undertakings, i.e. when they are controlled by state authorities, or when they operate on the basis of special or exclusive rights related to natural gas, heat and energy, with a number of exceptions.⁴² In both cases they are considered to be sectoral contracting authorities.⁴³

The Bulgarian energy sector, a non-liberalized market with few large privatised electric distribution companies, weak regulatory authority, inherent secrecy and technological complexity presents an example of high corruption risk area. Considerable economic interests are at stake in the sector, with strong political lobbies and substantial national and international financial resources involved (CSD, 2007 & 2009). The high concentration of public funds (of state-owned enterprises) in large-scale complex public procurement in energy generates a persistent risk of corruption, fraud and abuse of public financial resources, which has been well documented throughout the years. Most big energy projects (e.g. Belene NPP, Tsankov Kamak HPP, SouthStream pipeline and the rehabilitation of coal facilities) can serve as examples of the recurring misuse of public procurement mechanisms. The lack of genuine competition and strong monopolization of individual segments in the energy sector; the high volume of energy exported via intermediaries; lack of transparency, public awareness and independent expert assessment; the restricted access to information on national security grounds; the technical complexity of the energy sector; and the critically low inspectorates' capacity are additional major factors contributing to heightened corruption risks in the energy sector. In a nutshell, the large energy infrastructure project initiated in Bulgaria between 1998 and 2008 all display the

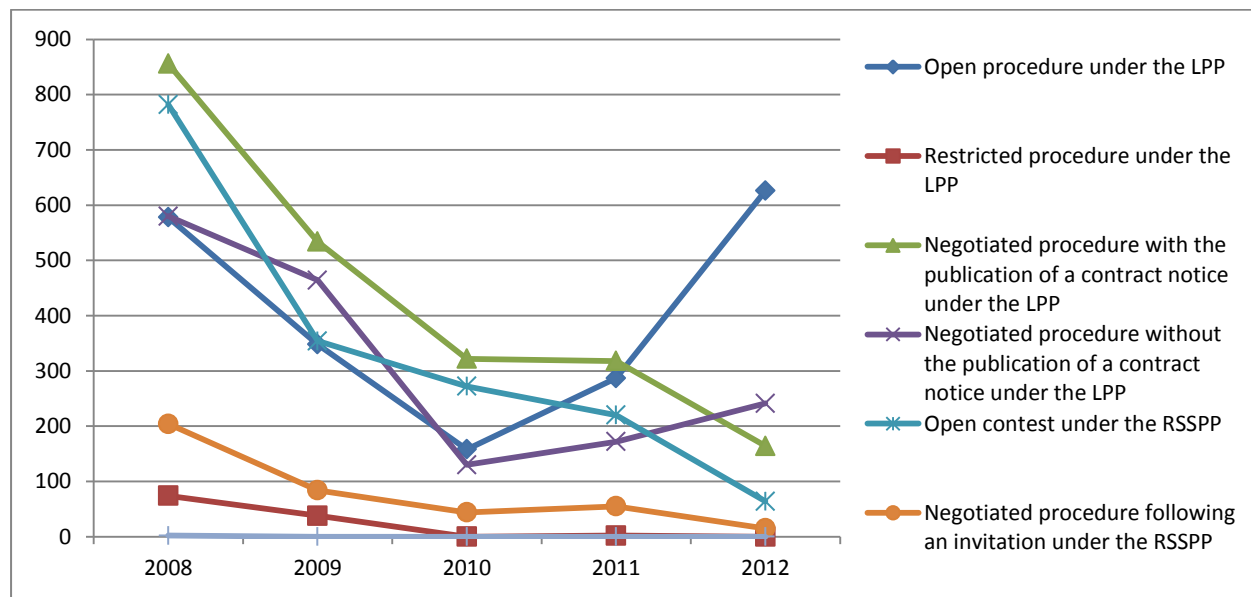
⁴² Article 7, items 5 and 6 read in combination with Article 7a of the Law on Public Procurement.

⁴³ The reasons why special procedures for the award of contracts apply to these entities are set forth in paras 2 and 3 of the preamble of Directive 2004/17/EC and fall in two groups: (a) the variety of ways in which national authorities can influence the behavior of these entities, including participation in their capital and representation in the entities' administrative, managerial or supervisory bodies and (b) the closed nature of the markets in which they operate, due to the existence of special or exclusive rights granted by the Member States concerning the supply to, provision or operation of networks for providing the service concerned.

characteristics of a particularistic distribution of public resources – with concentration of considerable resources in time and place, and the lack of adequate deterrence mechanisms.

Non-competitive public procurement procedures⁴⁴ are generally considered an instrument particularly exposed to corruption. In the period 2008 – 2010, the period of the highest public procurement budgets, the share of non-competitive public procedures in the energy sector was systematically higher than the share of competitive contracts (Figure 15). Even after the exposure of the huge irregularities in the case of Belene HPP the share of non-competitive public procurement procedures remained higher in the energy sector than in the rest of the economy in the period 2010 – 2012. It should be noted that in 2012 the percentage of contracts awarded on a competitive basis in the energy sector increased to 62%, compared to 48.1% in 2011 and 46.4% in 2010. This improvement could be interpreted as the result of increased public scrutiny and ex-post controls by the relevant public institutions. However, in the beginning of 2014 Bulgarian authorities replicated in the South Stream case the worst practice from the now defunct Belene HPP project by awarding a multi-billion euro contract through a single public procurement procedure to a consortium, which media reports had named as the predetermined winner for constructing the pipeline in Bulgaria. In both cases these single public procurement procedures were comparable in size to the total value of the public procurement market in the country at the time of the awarding.

Figure 15. Number of Public Procurement Procedures Carried Out in the Energy Sector by Type (2008-2012)



Source: PPA, CSD calculations

⁴⁴ Non-competitive procedures include a limited number of interested parties submitting a tender, followed by negotiations. This category includes the negotiated procedure with and without publication of a contract notice under the LPP, the competitive dialogue, and the negotiated procedure following an invitation, as well as the selection among three submitted tenders, both under the RSSPP fall under this category.

2.1. Case study: The South Stream project

The implementation of the [momentarily suspended] South Stream project so far has revealed a number of management deficiencies in Bulgarian energy governance, which hint at high corruption risks. At the time of the award of the pipeline contract, many details of the project's implementation had been left unspecified and sensitive issues among the shareholders had not been resolved which could result in future conflicts affecting Bulgaria. The concerns about the management of the project were further substantiated by the lack of transparency in public procurement procedures for the choice of an Engineering, Procurement and Construction (EPC) contractor. As of 2015 the project has been suspended from the Russian side, with Bulgaria saddled with the risks of bad governance, and with no clear perspective of when the invested public money will be recovered.

Even before the EPC tender, the procedure for choosing a contractor to carry out the feasibility study preceded the signing of the statutes of the joint project company, thus blurring the separation of management responsibilities of the shareholders and the joint venture, and riddling the project with many corruption risk red flags (CSD, 2011). In principle, the joint venture is responsible for the organization and the financing of the feasibility study, and should ensure a competitive procedure for the choice of a contractor but has in effect been left to pick up the costs of someone else's decision. Moreover, South Stream Bulgaria has extended the deadline for document submission several times. The last extension was only for several hours implying either bad organisation of the procedure or purposeful tailoring of the tender offer for a specific applicant. In addition, providing only six working days for applications for a contract of such magnitude and levels of technical detail is clearly inadequate, especially in the absence of a prior indicative announcement. This practice is among the most commonly used methods of limiting competition in public procurement in Bulgaria, and is a clear sign of high corruption risk.

The public procurement procedure for a choice of an EPC contractor did not make much of a difference in the overall management of the project. South Stream Bulgaria issued an EPC tender on 31 October 2013 giving only two weeks for companies to submit the necessary documents⁴⁵. In addition, it was surprising that the whole execution of the project has been tendered in one procedure without clear division of the tasks in the respective stages. This immediately raised doubts that the outcome of the tender is pre-determined (Stefanov, R., Vladimirov, M., 2014). On 19 November 2013 the project company cancelled the tender without providing clear argumentation except the explanation that a large number of foreign companies had submitted requests to bid (CSD, 2014).

The second tender competition was announced in a similar fashion right after Christmas 2013 with a deadline for tendering of no more than 10 working days for companies to prepare their tender documentation. The tender specifications revealed extraordinarily strict requirements for the bidders including a proof of EUR 750 million in revenues from gas pipeline EPC contracts for the 2008-2012 period. The bidders had been asked to prove that they had access to EUR 250 million in credit financing or their own capital. Most importantly, the bidders had to prove that in

⁴⁵ According to a Press Release by the Bulgarian Energy Holding from 31 October 2013

the last three years they had participated in pipeline projects with similar size and capacity⁴⁶. With tailored specification in place it was not surprising that the winner of the tender was a Russian-Bulgarian consortium led on both sides by companies seen as intimately close to the ruling elites in the two countries. The Bulgarian companies in particular have not had any prior experience with pipeline construction, indicating they were included in the bid on non-market considerations. The organization of the tender, its requirements, and the ultimate winner have all pointed to the presence of pre-existing preferences on the winning combination violating free and fair competition.

The irregularities related to the project's public procurement were further aggravated by the worsening geopolitical confrontation between Russia and the EU. In August 2014, the Russian side had to withdraw the leading company from the project as its manager was included in the US and EU sanctions list against Russia for its participation in the Ukrainian conflict⁴⁷. Instead of opening a new tender procedure the lead company was simply replaced by a Gazprom subsidiary, which further worsened Bulgaria's control on the project. Thus the Bulgarian authorities have, contrary to common sense, continued to uphold the country's stake in the project as the risks for its realisation have continuously increased while the control over the project outcomes has further slipped away from the Bulgarian side (Stefanov, R., Vladimirov, M., 2014).

V. CONCLUSION

Bulgaria has continuously modernized and improved its public procurement management and control institutions in line with its EU accession and membership. But public procurement remains trapped in the wider governance problems of the country, which still display the main features of a particularistic regime, far from being aligned to good governance or open access order norms. Recent developments have increased corruption risks in public procurement. Declining private sector opportunities and rising pressures for EU fund absorption by the end of the EU funding cycle in 2013 have led to both concentration of public procurement resources and market leverage in the public administration. Construction projects have increased as a share of total public procurement of the country, while its importance has also spiked for private, construction company turnover. EU financing has also risen steadily in construction works public procurement signifying that corruption risks inherent for the national public procurement system have unavoidably been transferred into the EU funds' realm.

The firm level analysis of public procurement contracts awarded to the top 40 construction sector companies introduced in this paper confirms the trend of concentration of the public procurement contracts to the top 7 companies in the construction sector, as well as the increasing reliance of the sector on public procurement for its survival. The data does not confidently project specific type of favouritism but does hint that some companies' public procurement performance seems linked more to the government in office than to past or future

⁴⁶ Data from the Public Procurement Registry, available from: www.aop.bg

⁴⁷ Petkova, Delyana. (4 August 2014). *Stroytransgaz leaves the South Stream project in Bulgaria ("Стройтрансгаз" напуска проекта "Южен поток" в България)*. Investor.bg. [WWW]. Available from: <http://www.investor.bg/ikonomika-i-politika/332/a/stroitransgaz-napuska-proekta-iujen-potok-v-bylgariia--177475/> [Accessed 8 December 2014].

performance. Corruption risks however are detected in specific cases, especially involving large-scale infrastructure projects in the construction and energy sectors.

The Bulgarian public procurement framework is largely in line with EU legislation but its implementation remains haphazard and riddled with corruption risks, as changes in the legislation continue to be too frequent to be explained only with EU approximation efforts. Recent amendments, introduced in 2014 have succeeded in addressing some particular corruption risks, such as lowering the weight of the lowest price criteria in award decisions, introducing additional ex-ante controls, and increasing overall transparency. Nevertheless, important limitations exist in terms of capacity of the controlling authorities and effectiveness of the procurement system, while detected violations remain high, hinting at the lack of proper preventive capacity.

The public procurement process cannot be decoupled from the overall progress in the transition from a particularistic to an open access or good governance regime. First and foremost, Bulgaria needs to tackle its endemic lack of trust of citizens in public institutions through strengthened law enforcement in particular as concerns higher-level, political corruption. Simultaneously, the government and its European partners can work to reduce opportunities and increase constraints to corruption in public procurement in the construction/infrastructure sector by adopting several groups of tools:

- Discontinuing the practice of awarding single public procurement contracts worth more than a certain threshold, which is aligned with the current management capacity of contracting authorities; a reasonable approach would be to limit single tender procedures to 5% of the average annual total public procurement market value for the past three years;
- Optimization of the legal framework towards increased transparency and competition in public procurement through the more aggressive introduction of e-tools;
- Enhancement of the effectiveness of legal remedy and control mechanisms, as well as more active prevention of market concentration;
- Strengthening the administrative capacity and more stringent requirements to the professional ethics of the responsible officials in the contracting authorities;
- Increasing the effectiveness of criminal prosecution, in particular in cases involving larger public financial resources;
- Introducing effective control over the property and income affidavits submitted by senior officials but also over conflicts of interest, which might hint at more subtle forms of corruption such as favouritism;
- Optimization of the legal framework regulating the financing of political parties and election campaigns, including independent candidates and lobbying to include non-monetary contributions such as employment, hidden subsidies, etc.

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ABSTRACT

This paper seeks to assess the extent of favouritism – i.e., preferential treatment for some bidders over others - in the allocation of public procurement contracts in the construction sector in Croatia. The methodology is based on identifying opportunities for favouritism and evaluating the effectiveness of constraints. The research finds that Croatia's public procurement law sets a high standard and there are numerous transparency and control mechanisms in place. Nevertheless, the integrity of procurement is undermined because a large share of it is contracted by entities which are owned by government units and thus subject to political influence and constrained by a much weaker control framework. Data on the procurement of high-value construction works is analysed for indicators of favouritism in the process or outcomes. Whilst there is only limited use of restrictive procedures, competition for public contracts is surprisingly weak in a sector under considerable economic pressure. Moreover, around one-half of the total contract value is won by tenderers which are not private companies but rather entities that are partially or fully owned by the state. This raises further questions about the potential for political leaders to influence the process in order to achieve favouritism in the allocation of public contracts, to benefit themselves or third parties. Evidence from the verdict of a trial involving high-ranking politicians suggests further that such favouritism may be widespread.

ABBREVIATIONS

CBS	Central Bureau of Statistics
CCI	Commission for Conflict of interest
CFCA	Central Finance and Contracting Agency for the European Union Programmes and Projects
CNB	Croatian National Bank
CPV	Common Procurement Vocabulary
CSO	Civil Society Organization
DPPS	Directorate for the Public Procurement System
FA	Framework agreement
FINA	Financial Agency
GDP	Gross Domestic Product
OG	Official Gazette
PP	Public procurement
PPA	Public Procurement Act
PRAG	Practical Guide
SCSPPP	State Commission for Supervision of Public Procurement Procedure
VAT	Value Added Tax

GLOSSARY¹

Common Procurement Vocabulary (CPV) designates the reference nomenclature applicable to public procurement procedure, while ensuring equivalence with existing nomenclatures.

Contracting authority/entity refers to contracting authorities and contracting entities.

A *contract notice* is published by contracting authorities intending to award a public procurement contract or conclude a framework agreement in an open, restricted and negotiated procedure with prior publication and competitive dialogue. It is drawn up so as to contain all the necessary data allowing the economic operator to prepare the request to participate and/or tender.

Framework agreement is an agreement between one or more contracting authorities/entities and one or more economic operators, the purpose of which is to establish the terms governing contracts in a given period, in particular with regard to price and, where appropriate, the quantity envisaged.

Group of tenderers or candidates is an association of several economic operators submitting a joint tender, or request to participate.

Public procurement contract is a contract for pecuniary interest concluded in writing between one or more economic operators and one or more contracting authorities/entities and having as its object the execution of works, the supply of products or the provision of services.

Public works contract is a public procurement contract having as its object:

¹ Definitions are taken from the Public Procurement Act (Official Gazette 90/11, 83/13, 143/13, 13/14).

1. Either the execution, or both the design and execution, of works related to one or more activities within the meaning of Annex I, List of activities in Construction of the Public Procurement Act, or

2. Work, or the realisation, by whatever means, of work corresponding to the requirements specified by the contracting authority/entity. The 'work' refers to the outcome of building or civil engineering work taken as a whole, which is sufficient of itself to fulfil an economic or technical function.

Subcontractor is an economic operator delivering supplies, providing services or performing works directly related to the subject matter of procurement for the selected tenderer with whom the contracting authority/entity has concluded a public procurement contract.

A *tender* is a written statement of the tenderer's willingness to deliver supplies, provide services or perform works in accordance with the terms and requirements listed in the tender documents (contract notice).

Tenderer is an economic operator who has submitted a tender on time.

Public expenditure (cost of general government) is the sum of the expenditure of all levels of government: central government (state), local and regional government and extra-budgetary users.

Value of executed construction works refers to all construction works (public or private, new constructions and reconstructions, maintenance and repair works on existing constructions) performed in the territory of the Republic of Croatia.

Value of public procurement is the sum of works, goods and services.

Value of the procurement of works represents the sum of all concluded public works contracts.

FIGURES

Figure 1 Structure of total public procurement (works, goods and services) by type of contracting authorities and as % of GDP (in current prices), 2008-13

Figure 2 Total value of executed construction works, Croatia 2008-13 (left axis, HRK bn; right axis, % of GDP)

Figure 3 Structure of public procurement of works (construction) contracts exceeding HRK 7,452,830 (1mn euros), by type of contracting authority, 2011-13

Figure 4 Number of managerial changes in legal persons and sectoral (Type C and D) contracting authorities owned by central government, Croatia 2010-2013 (N=28)

Figure 5 Number of managerial changes in Type C and Type D contracting authorities owned by regional and local government, 2009-14 (N=95)

TABLES

Table 1 Value of executed construction works, Croatia 2008-13 (in HRK bn and % of GDP)

Table 2 Public procurement of works (construction) by type of procedure, contracts valued over HRK 7,452,830, 2012-13

Table 3 Public procurement of works by type of procedure, framework agreements valued over HRK 7,452,830, 2012-13

Table 4 Public procurement of works (construction) by number of tenders received, contracts valued over HRK 7,452,830 (EUR1mn), 2012-13

Table 5 Public procurement of works by number of tenders received, framework agreements valued over HRK 7,452,830, Croatia 20-2013

Table 6 Analysis of tenderers with contract(s) above HRK 7,452,830 in public procurement of works, 2011-13

Table 7 Top 10 Tenderers by value of public procurement, works contract/s (HRK) – state owned enterprises, 2011-13

Table 8 Top 10 winning tenderers by value of contract/s (HRK) – Privately owned enterprises, 2011-13

Table 9 SCSPPP Motions filed for indictment in relation to misdemeanours prescribed by the Act, 2010-13

Table 10 Tenderers with contract(s) above HRK 7,452,830 in public procurement of works detected by accountability mechanisms

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Appendix 1 Value of public procurement and the proportion of public procurement in GDP, Croatia 2008-2013

Appendix 2 Structure of the value of public procurement by type of contracting authority, Croatia 2008-2013 (in HRK bn and % of total)

Appendix 3 Value of executed construction works, Croatia 2008-2013 (in HRK bn and % of GDP)

Appendix 4 Contracting authorities with contracts for the procurement of works equal to or greater than HRK 7,452,830, Croatia 2011-13

I. INTRODUCTION

The integrity of the public procurement process is best assured when the allocation of resources occurs in conditions of open competition and where mechanisms exist to monitor the government agents in charge of the process and check that their decisions reflect nothing but the relative merits of competing bidders. However, if insufficiently constrained, the government agents in charge of procurement may seek to allocate resources in a particularistic manner, in order to benefit themselves or other parties. This paper seeks to assess the extent of favouritism – i.e., preferential treatment for some bidders over others - in the allocation of public procurement contracts in the construction sector in Croatia. The research is conducted within a theoretical framework which posits that corruption is most likely to occur where the opportunities are high and the constraints low (Mungiu-Pippidi et al 2011). The methodology is therefore based on identifying opportunities for favouritism and evaluating the effectiveness of constraints.

The paper proceeds as follows. First, the legal framework concerning public procurement in Croatia is explained and evaluated. Second, data on the public procurement of high-value construction works is analysed for indicators of favouritism in the process and outcomes. Third, further analysis is undertaken of a key risk area that emerges from the research, relating to political influence over the procurement process. Fourth, the control framework is elaborated and evaluated. Finally, conclusions are presented about the balance of opportunities and constraints with respect to favouritism in the public procurement of construction works in Croatia.

II. THE LEGAL FRAMEWORK FOR PUBLIC PROCUREMENT

The first national act regulating public procurement was the *Act on the Procurement of Goods, Services and Works*² adopted in 1997. Since that time, the Act has been amended substantially on several occasions, with each version making the process more stringent, better controlled, and more transparent.³ These amendments finally led to the passage of an entirely new law in 2011, the Public Procurement Act, effective since 1 January 2012.⁴ The new act simplified procedures and reduced administrative costs for both contracting authorities and tenderers. It created conditions for tender documents to be submitted electronically, although progress towards e-public procurement⁵ had already been made in 2008 with the introduction of the mandatory electronic publication of all public procurement notices on the Electronic Public Procurement Classifieds platform of the Official Gazette.⁶ The platform also includes an e-auction module, although barriers remain to rolling out e-procurement in Croatia, particularly for goods and services which require tenders to be evaluated on conditions other than price. The Public Procurement was amended once again

² The Act on the Procurement of Goods, Services and Works was adopted on 19 December 1997 and published in the Official Gazette (OG) 142/97, 31 December 1997. Amendments to the Act were published in the Official Gazette 32/01, 10 April 2001)

³ OG 117/01, 92/05, 110/07, 90/11.

⁴ OG 90/11.

⁵ The Decision on the adoption of the Strategy for the development of electronic public procurement in Croatia 2013-2016 (Official Gazette No. 54/13).

⁶ OG 110/07.

in 2013⁷, resulting in further improvements in control and the introduction of some provisions that were only later, through the EU Directives of 2014⁸, accepted as the European standard.

Interviews with public sector procurement professionals⁹ suggest that the 2011 law was primarily driven by a need to align Croatian legislation with that of the European Union as part of the accession process, as well as by a need to address deficiencies of the previous legal framework which had allowed corrupt practices. Several experts commented that the current legislation is advanced and more stringent than European standards in some areas. As the Head of the Department for Infrastructure and Construction Works in the Central Finance and Contracting Agency for the European Union Programmes and Projects (CFCA) explained,

“The legislation is very strict and I do not see any opportunities for favouritism. It is so strict in some areas that it limits the logic and the structure of the process.”

For the construction sector, the Act and its first amendment¹⁰ resulted in significant changes concerning subcontractors. According to Article 86 (2), economic operators who intend to subcontract part of a public procurement contract to one or more subcontractors should include information about the subcontractor in the tender, including the company name and the proportion of the public procurement contract to be subcontracted.¹¹ This amendment is intended to prevent economic operators from acting merely as intermediaries, winning contracts but then passing on the majority of the work to other contractors whose credentials were not subject to the scrutiny of a public tender. Contracting authorities now also make payments to subcontractors directly, providing an additional security mechanism to prevent payment blocking or fraud.

The legal framework also stipulates an obligation to control the execution of public procurement contracts after the award, i.e., the obligation to check whether the execution complies with the conditions laid down in the tender. This clause is unusual, because most PP laws in the EU regulate only until the point of signing the contract. The clause has important potential to detect and deter corruption, with a considerable body of research suggesting that irregularities in the procurement of construction are common in the post-award phase (Guasch 2009). However, although the clause came into effect on 1 January 2012, the institution responsible for overseeing this part of the PP process has not yet been specified.

Overall, the legal framework sets high standards and includes a number of provisions which constrain the opportunities for private companies to seek to distort the competitive process.

⁷ OG 90/11, 83/13 and 143/13.

⁸ Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC Text with EEA relevance; Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC Text with EEA relevance; Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts Text with EEA relevance.

⁹ Five semi-structured interviews conducted with the representatives of the Central Finance and Contracting Agency (SAFU), Office of Contracting & Head of Infrastructure and Construction Department; Ministry of Economy, Directorate for the Public Procurement System, Ministry of Regional Development and EU funds: Head of Procurement.

¹⁰ OG 83/13.

¹¹ The information about the subcontractor must include the name, company name, seat, national identification number (or national identification number of the country seat of the economic subject, if applicable), account number of the subcontractor and the subject, quantity, and value of the subcontract.

However, the experts we interviewed also argued that several challenges remain regarding the implementation of the law.¹² For example, many contracting authorities lack an adequate number of professionally trained procurement staff. Although the Directorate for the Public Procurement System (DPPS) conducts training in this area in accordance with the Regulations on training in the field of public procurement¹³, one DPPS representative the interviewed for this research pointed out that,

“Negative personnel selection is often evident in the internal organisation of contracting authorities, with insufficiently qualified, non-specialist and unmotivated staff in charge of public procurement.”

This casts doubt on the professionalism with which the procurement process is executed and puts the onus on control mechanisms to monitor and detect inadequacies.

III. THE PUBLIC PROCUREMENT OF CONSTRUCTION: MARKET OUTCOMES

1. Overview of public procurement in Croatia

Public procurement in Croatia accounted for around 9.7% of GDP on average in the years 2011-13, comparable to Cyprus (10.5% in 2010) and Greece (10.8%). Procurement can be undertaken by four types of contracting authority:

1. **Type A.** State authorities or central government bodies such as ministries, departments, state agencies and other public bodies, which are under the direct rule of the Government, or ministries.
2. **Type B.** Bodies of local and regional government/local and regional agencies and offices consisting of counties, cities and municipalities, and agencies and offices within the internal organisation of local and regional government.
3. **Type C.** Legal persons other than public authorities, including public companies other than sectoral contracting authorities in the ownership of central, regional and local government, institutions under their ownership and other legal entities that are not directly subordinate to public authorities, but come under the indirect influence of public authorities pursuant to their founding rights. This category includes several organisations that play a major role in construction, including Croatian Roads Ltd., the Croatian water management company, and county road administrations.
4. **Type D.** Sectoral contracting authorities, which are state-owned companies¹⁴ (owned at least partly by the central, regional or local government) characterised by a special position in the market (usually strategic sectors, such as water, energy and transport).¹⁵

An analysis of the structure of public procurement finds around one-half of total public procurement contracting value in Croatia during the period 2008-13 was executed by

¹² This is evident from responses obtained from representatives of relevant institutions in the field of public procurement, who were interviewed for the purpose of this study.

¹³ See relevant provisions in the law in OG 06/12 and 125/14.

¹⁴ A sectoral contracting authority is not necessarily a public company, according to EU legislation. However, in the Croatian context, there is no example in which a sectoral contractor is not at least partially owned by a state entity.

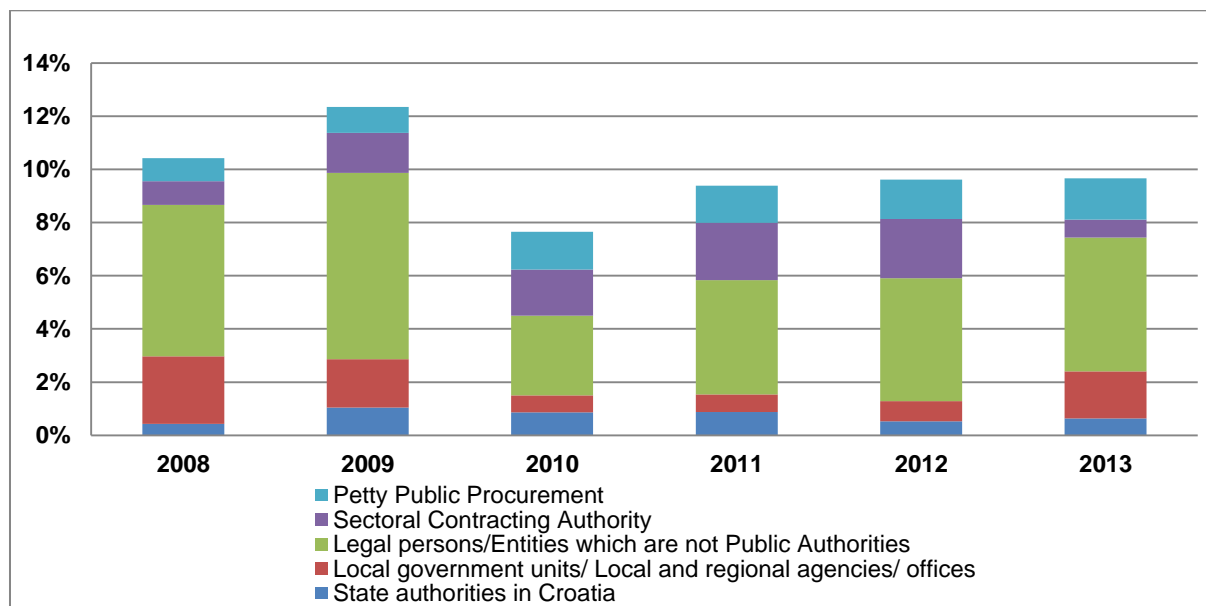
¹⁵ For example gas distribution companies (HEP Plin d.o.o., Energo d.o.o., Plinara d.o.o., Plinacro d.o.o., HEP Toplinarstvo d.o.o.), transmission and distribution operators (HEP –OPS d.o.o., HEP – ODS d.o.o.), water management companies (Vodovod i kanalizacija d.o.o. Karlovac, Vodovod d.o.o. Slavonski Brod) etc.

contracting authorities in categories C and D (see Figure 1). This is significant because different types of contracting authorities are subject to different control mechanisms, and thus are vulnerable to corruption risk to varying degrees.

Type C and D authorities are subject to weaker controls than other contracting authorities. The law itself provides for preferential treatment in public procurement conducted by such authorities, in that a weaker justification is needed for the use of restricted procedures. Thus, many actions that would represent breaches of the law if procedure was conducted by a Type A or B authority are permitted for Type C and D contracting authorities.

The academic literature on the state entities which constitute Types C and D contracting authorities finds that they typically have poor management, reflected in weak profit and loss accounts and making them highly dependent on budget subsidies (Crnković et al., 2011). These findings raise questions about the technical capacity of the organisations to conduct complex public procurement procedures, as well as highlighting the organisations' likely sensitivity to maintaining favourable relations with their political 'owners'. These risks are assessed in greater depth in part three.

Figure 116 Structure of total public procurement (works, goods and services) by type of contracting authorities and as % of GDP (in current prices), 2008-13¹⁶



Source: Author's calculations based on data from Croatian Bureau of Statistics and Directorate for Public Procurement System

2. The construction sector and public procurement

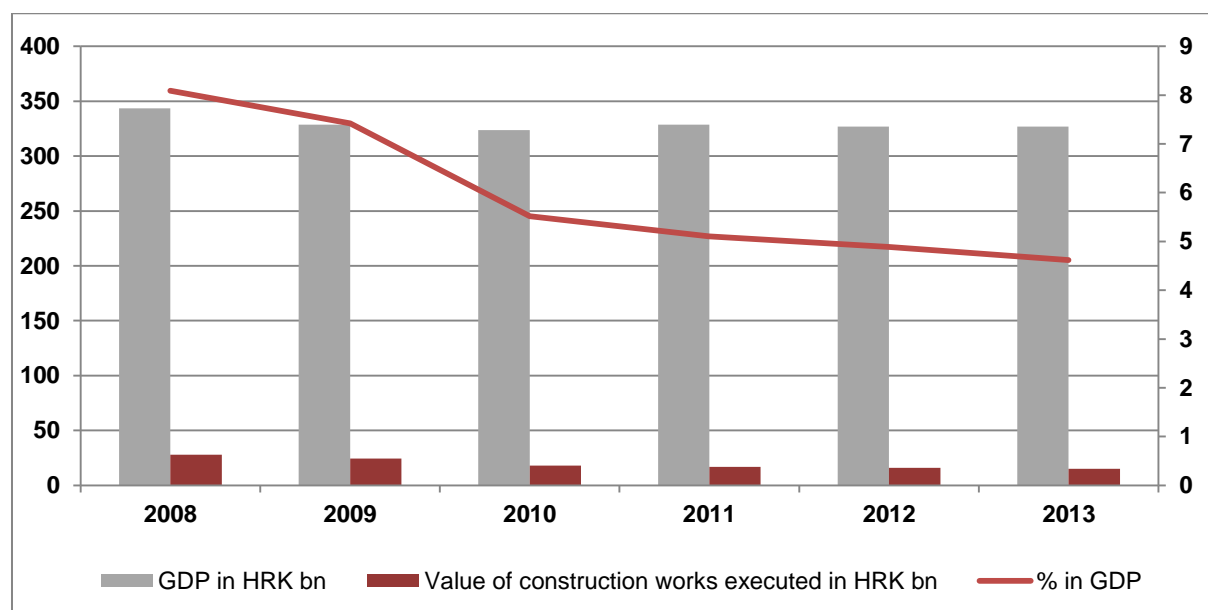
The construction sector has been in decline since 2008, losing 45.7% of its value over 2008-13 and with the sector's share in GDP collapsing from 8.1% in 2008 to 4.6% in 2013 (see Figure 2)¹⁷. The sector was, however, buoyed somewhat by an increase in public investment in infrastructure in 2009 as part of a government plan to stimulate an economic recovery, while a change in public procurement laws in the same year prompted many contracting

¹⁶ Underlying data are provided in Appendix Two.

¹⁷ The value of construction works executed is presented in terms of current prices and includes works performed in the reporting year, regardless of whether or not they were paid for in the reporting period.

authorities to invite tenders for large framework agreements.¹⁸ Overall, the total value of public procurement contracts and framework agreements in the sector reached HRK 21.8bn in 2009, more than double the previous year's total of HRK 8.4bn in 2008 (DPPS, 2010). The ten highest value contracts and framework agreements in the construction sector accounted for one-quarter of the total value of public procurement in that year (DPPS, 2010).

Figure 2 Total value of executed construction works, Croatia 2008-13 (left axis, HRK bn; right axis, % of GDP)



Note: GDP data for 2013 are provisional (the sum of quarterly data)

Source: author's calculations based on data from the Croatian Bureau of Statistics

Indeed, the sector became increasingly dependent on public procurement in this period. In 2008, public procurement had accounted for 30.2% of the total value of construction works executed, indicating that most of the value created by the sector was achieved under the rules of market competition. In subsequent years, public procurement came to account for the majority of construction business (see Table 1).¹⁹

Table 1 Value of executed construction works, Croatia 2008-13 (in HRK bn and % of GDP)

Year	GDP in HRK bn	Total construction sector, value in HRK bn	% of GDP	Construction procurement value in HRK bn	% of procurement in construction sector value
2008	340	25	7.35	8.4	30.2
2009	325	25	7.69	21.8	87.1
2010	320	20	6.25	15.0	75.0
2011	325	18	5.54	15.0	83.3
2012	325	18	5.54	15.0	83.3
2013	325	18	5.54	15.0	83.3

¹⁸ The amended Public Procurement Act in 2008 created the possibility for contracting authorities to establish framework agreements (FA), i.e., multi-year contracts with one or more tenderers, for a period of up to four years. See OG 110/07 and 125/2008.

¹⁹ The figure for 2009 is particularly high, but is not comparable owing to the legislative change and the widely used opportunity for contracting authorities to sign FAs.

2008	343.4	27.8	8.1	8.4	30.2
2009	328.7	24.4	7.4	21.8	89.3
2010	323.8	17.9	5.5	9.8	54.7
2011	328.7	16.8	5.1	9.4	56.0
2012	327.0	16.0	4.9	9.1	56.9
2013	326.8	15.1	4.6	10.0	66.2

Source: author's calculations based on data from the Croatian Bureau of Statistics and the Directorate for Public Procurement System

The rest of our analysis focuses on a specific sample of public procurement contracts: those for construction works worth 1mn euros or more awarded in the period 2011-2013.²⁰ The total value of contracts in our sample is HRK 17.9bn, and they were awarded by 192 contracting authorities.²¹ We analyse several aspects of the process and outcomes to assess whether there is evidence of favouritism. In terms of process, we consider the structure of spending by contracting authority, the use of restricted procedures, and the number of tenderers. In terms of outcome, we assess the characteristics of winning bidders according to their type.

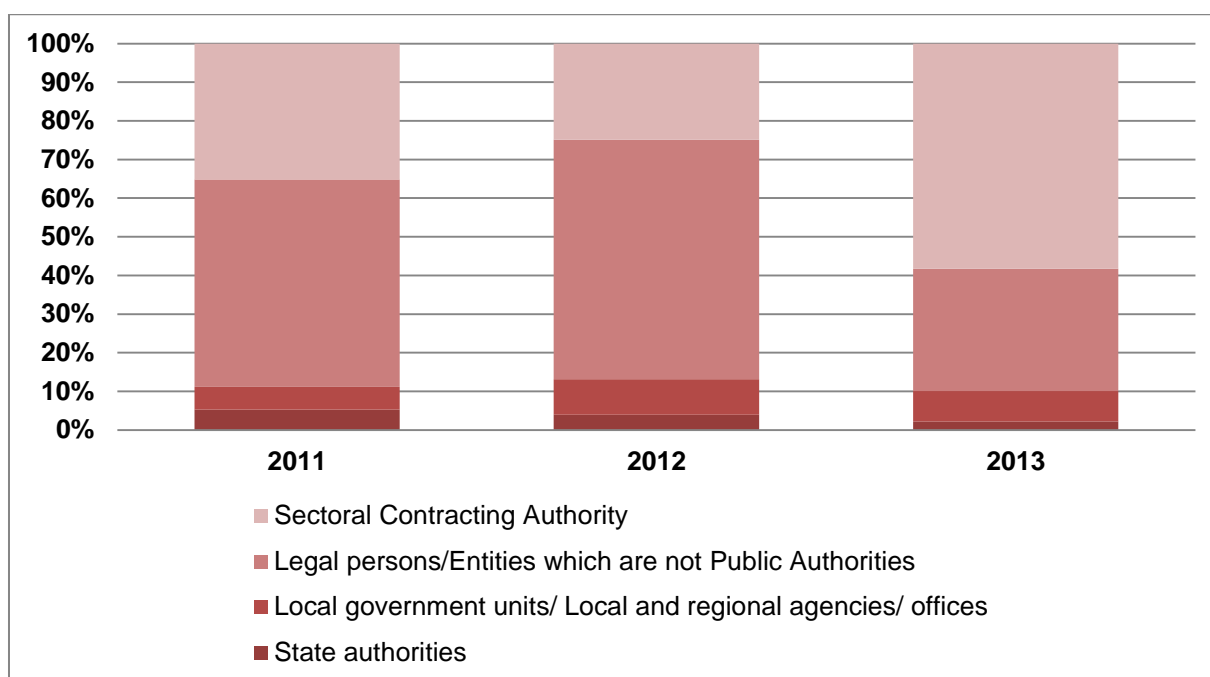
3. Structure of construction procurement, by type of contracting authority

When focusing on the construction sector alone, the predominance of procurement by Type C and D contracting authorities is yet more striking (see Figure 3). Around 90% of contracts in our sample were awarded by these types of authorities, which are subject to weak controls.

²⁰ Construction works are defined as Group 45 within the EU Common Procurement Vocabulary (CPV). The data has been collected and consolidated from several sources, including the Ministry of Economy's Directorate for Public Procurement System (DPPS), the Financial Agency (FINA), the Central Bureau of Statistics (CBS), the Commercial Court Register, the Central Finance and Contracting Agency for European Union Programmes and Projects (CFCA), and the Integrity Observers Database on public procurement (available at: www.integrityobservers.eu). The period of analysis was limited by a paucity of comparable data for earlier years. Moreover, while it was possible to collect a great deal of data from the state, considerable work had to be undertaken to standardise the data from different sources and to take account of changes in the law and rules relating to procurement and reporting of procurement. Given changes in practice on the inclusion of VAT, for example, as well as in the rate of VAT, contract values were standardised to exclude VAT to allow comparison.

²¹ The total value of all contracts signed by contracting authorities is not comparable to the value of contracts signed by individual tenderers quoted later in the paper. This is because the value of contracts signed by contracting authorities includes the value of contracts signed with a group of tenderers, as well as framework agreements. When analysing the tenderers, the value of framework agreements and group tenders were excluded because (due to the specifics of such arrangements) it cannot be precisely determined how much of the total value of particular framework agreement or contract within the group of tenderers belongs to each tenderer.

Figure 3 Structure of public procurement of works (construction) contracts exceeding HRK 7,452,830 (1mn euros), by type of contracting authority, 2011-13



Source: author's calculations based on data from the Directorate for Public Procurement System

4. The use of restricted procedures

The use of restricted procedures is examined because this is one way in which government agents may seek to restrict competition in the public procurement process, thereby benefiting cronies or allies. The use of such procedures is strictly regulated by law, and there are certain conditions in which it is permitted to limit competition by negotiating contracts with companies rather than conducting open tenders. Such procedures are legitimate, for example, in emergency conditions or when negotiating in specialist areas. However, governments seeking to allocate resources in a particularistic manner may seek to over-use or abuse such mechanisms. The pattern of usage of such procedures can therefore serve as a probabilistic indicator of particularism.

In our sample, a significant proportion of contracts, representing 27% of the total value, was contracted through negotiated procedures without being announced publicly, as shown in Table 2. In the case of FAs, however, the use of restricted or negotiated procedures was negligible (Table 3).

Table 2 Public procurement of works (construction) by type of procedure, contracts valued over HRK 7,452,830, 2012-13

	Number of contracts	Value of contracts (HRK)	% of total value of all contracts

Open procedure	214	4,222,463,130	72.63
Negotiated w/o prior publication	15	1,578,072,839	27.14
Not defined by law - exempted	1	13,040,449	0.22
Total	230	5,813,576,417	100.00

Source: author's calculations based on data from the Integrity Observers database.

Table 3 Public procurement of works by type of procedure, framework agreements valued over HRK 7,452,830, 2012-13

	No. of FAs	Value of FAs (HRK)	% total value of all FAs
Open procedure	46	2,575,430,547	96.46
Restricted procedure	2	28,502,987	1.07
Negotiated procedure with prior publication	2	66,066,385	2.47
Total	50	2,669,999,919	100.00

Source: author's calculations based on data from the Integrity Observers database.

5. Competition for contracts and the prevalence of sole bidders

Another potential indicator of favouritism is the number of bidders, which signals the extent of competition in the market. In a highly competitive market with many bidders for every contract, it may be more difficult for corrupt government agents to manipulate the allocation of a contract, while the process will be under greater scrutiny from interested parties, i.e., the competing tenderers.

In conditions where favouritism is rife, by contrast, competition may be low for two reasons. First, systematic favouritism over a long period would have driven out of the market companies which were unable to win contracts because they lacked relevant political connections. Second, if competitors expect a contract to be allocated in a particularistic way, they will not incur the costs of tendering and hence will opt out of the market. Equally, though, a low number of tenderers may simply reflect a lack of relevant expertise or interest in a particular contract. This indicator must therefore be interpreted with care. However, given the extensive pressures on the construction sector in Croatia during this period, it is reasonable to expect that competition would be intense.

However, the majority of contracts in our sample (63.8%) were acquired in an environment of relatively low competition, with three or fewer tenderers (see Table 4). Almost 40% of these large tenders had one sole bidder, despite 43 of the 58 being tendered on open procedures. Competition for FAs was also surprisingly low, with 60.4% of the contract value the result of processes with three or fewer tenderers, while 40% of the value of FAs in 2012 and 2013 attracted only one bidder (Table 5).

Table 4 Public procurement of works (construction) by number of tenders received, contracts valued over HRK 7,452,830 (EUR1mn), 2012-13

	Number of contracts	Value of contracts signed (in HRK)	% of total sum of contracts ≥ EUR 1m
1 tender received	58	2,317,775,476	39.87
2 tenders received	40	732,320,272	12.60
3 tenders received	38	654,920,160	11.27
≥ 4 tenders received	94	2,108,560,508	36.27
Total	230	5,813,576,417	100.00

Source: author's calculations based on data from the Integrity Observers database.

Table 5 Public procurement of works by number of tenders received, framework agreements valued over HRK 7,452,830, Croatia 20-2013

	No. of FAs	Value of FAs (HRK)	% total value of FAs
1 tender received	21	1,099,506,958	41.18
2 tenders received	5	349,170,956	13.08
3 tenders received	9	163,888,783	6.14
≥ 4 tenders received	15	1,057,433,223	39.60
Total	50	2,669,999,919	100.00

Source: author's calculations based on data from the Integrity Observers database.

6. The characteristics of winning bidders

Further indicators of favouritism in public procurement derive from studying the characteristics of winning bidders. If there are very few winners, or the winners appear to have links with political leaders, this is indicative of favouritism in the procurement process. In addition, if winning bidders exhibit unusually good economic performance relative to other market actors, this is suggestive of public contracts having been designed or awarded in ways that did not achieve the best value for money for the public, which may indicate corruption.

Overall, the contracts and FAs in our sample were won by a reasonable number of tenderers (175 different entities) and accounted for 17.3% of the tenderers' total revenue. However, for contracts amounting to almost one-half (46.5%) of the total value, the winning bidders were state-owned companies in the same legal category as Type C and D contracting authorities. This means that, for a large share of public procurement in construction, both the contracting authority and the winning tenderer were state entities under the control of political principals. Thus, politically elected executive branch officials at the national, regional and local levels have the *potential* to control both ends of the process, including the design of the contract notice and the tender submitted by winning bidder.

The winning tenderers were then separated into profitable and loss-making companies (results presented in Table 6). State-owned companies recorded higher cumulative profits (from a lower total value of contracts) than tenderers from the private sector. Privately owned companies recorded higher cumulative losses, despite the higher total value of signed contracts.

These findings might suggest that public sector tenderers are simply more efficient and therefore extract more profits from less revenue. However, the research analysed whether the proportion of public contracts in total revenue is relevant to performance. The publicly owned contractors which recorded cumulative profits were reliant on public procurement contracts for an average 24.2% of their revenues, while public contractors which recorded losses had only an average of 8.4% of procurement contracts in revenues. This relationship, i.e., the higher the proportion of procurement contracts, the greater the profits, applies to private contractors as well. Profitable private contractors have an average of 19.5% of public procurement in their revenues, while the average proportion for loss-making private contractors is only 16%. This at the very least raises concerns as to whether the companies which win public procurement contracts are providing the best value for public money.

Table 6 Analysis of tenderers with contract(s) above HRK 7,452,830 in public procurement of works, 2011-13

Tenderers with net profit					
	Value of public procurement, works contract/s (in bn HRK)	Cumulative revenue of tenderers (in bn HRK)	% of value of work contracts in cumulative revenue of tenderers	Cumulative number of tenderers with profit	Profit (in bn HRK)
State owned enterprises	5,4	22,4	24,2	29	1,8

Private enterprises	6,2	32,1	19,5	95	1,4
TOTAL	11,7	54,5	21,4	124	3,2

Tenderers with net loss					
	Value of public procurement, works contract/s (in bn HRK)	Cumulative revenue of tenderers (in bn HRK)	% of value of work contracts in cumulative revenue of tenderers	Cumulative number of tenderers with loss	Loss (in bn HRK)
State owned enterprises	1,9	23,1	8,4	20	-2,1
Private enterprises	2,3	14,3	16,1	31	-2,4
TOTAL	4,2	37,4	11,3	51	-4,5

7. The Top Ten State-Owned Winning Tenderers

The next phase of analysis focused on the top ten most successful state-owned tenderers, by contract value (Table 7). This revealed that the top three companies, which won almost 20% of the total sum of contracts in our sample, were members of the same group, Croatian Railways. Moreover, the contracting authority for these contracts was the same entity, Croatian Railways. This represents an unusual deviation from international standards for public procurement.

Table 7 Top 10 Tenderers by value of public procurement, works contract/s (HRK) – state owned enterprises, 2011-13

	Value of contracts in HRK
PRUŽNE GRAĐEVINE d.o.o.	2,784,220,531
POSIT d.o.o.	403,123,217
REMONT I ODRŽAVANJE PRUGA d.o.o.	325,823,109
STSI-Integrirani tehnički servisi d.o.o.	277,926,594
Vodoprivreda Zagreb d.d.	248,045,308
KONČAR - Inženjering za energetiku i transport d.d.	209,846,523
VODOPRIVREDA VINKOVCI d.d.	186,954,399
Istarske ceste d.o.o. Pula	171,780,657
Županijske ceste Split d.o.o.	162,395,384
CESTE-RIJEKA d.o.o.	152,520,741

Source: author's calculations based on data received from the Directorate for the Public Procurement System

8. The Top Ten Private-Sector Winning Tenderers

A further stage of analysis focused on the private companies that were the most successful tenderers in terms of the highest aggregate value of contracts. Of the top ten, nine were former state-owned companies that had been privatized – all except Lapor d.o.o (Table 8).²²

Table 8 Top 10 winning tenderers by value of contract/s (HRK) – Privately owned enterprises, 2011-13

	Value of contracts in HRK
GRADNJA d.o.o. OSIJEK*	424,295,084
GP KRK d.d.*	369,369,287
HIDROELEKTRA NISKOGRADNJA d.d., Zagreb	287,537,784
ZAGORJE TEHNOBETON d.d.*	280,993,865
OSIJEK-KOTEKS d.d.*	263,186,500
VIADUKT d.d.*	238,730,927

²² Only one company among the top ten private tenderers has been private since its establishment, Lapor d.o.o. This company co-owns one of the public companies that is a major contractor in the water management sector, Vodoprivreda Zagreb d.d. (Bohutinski, 2011).

LAVČEVIĆ d.d.*	205,125,845
VODOPRIVREDA d.o.o., Buzet*	195,297,215
VODOGRADNJA RIJEKA d.o.o.*	179,937,878
LAPOR d.o.o.	175,151,809

Source: author's calculations based on data received from the Directorate for the Public Procurement System

* Private ownership after privatisation

The history of these enterprises is relevant to our analysis because the privatisation process in Croatia was associated with serious weaknesses in terms of fairness, transparency and procedure (Bajo, 2011, Grubišić et al., 2009, Bendeković, 2000). Several scholars have characterized the process as one in which resources were allocated according to favouritism and cronyism, with political principals distributing resources so as to extend their political control over the emerging private sector (Čučković 2002, Franičević 1999). The new owners were often successful in securing assets not because of their business competence or financial resources, but because they had fruitful connections to the political elite (Franičević 1999; Petričić).

IV. RISKS OF POLITICAL INFLUENCE OVER PUBLIC PROCUREMENT

1. The appointment of managers of contracting authorities

One way in which favouritism might be practiced in the allocation of contracts is through political influence over the managers of contracting authorities. This is a potential risk area in Croatia owing to the governance structures pertaining to the procurement process, particularly for Type C and Type D authorities which, as discussed, are responsible for around one-half of public procurement in Croatia and 90% of the contract value in our sample.

According to law, in the case of *legal persons that are not contracting authorities and sectoral contracting authorities (if they are public companies)* - i.e., most Type C and Type D authorities - the head of the contracting authority is appointed by the relevant public authority (national, local, or regional executive branch government), pursuant to its founding rights.²³ Thus, the managers of these authorities are appointed by the politically elected leadership of the owner organisations be they central, regional or local government.

Political principals might choose to use this power of appointment more or less proactively, and for different reasons. Incoming political leaders are not compelled to change the management of contracting authorities under their control and might decide only to make

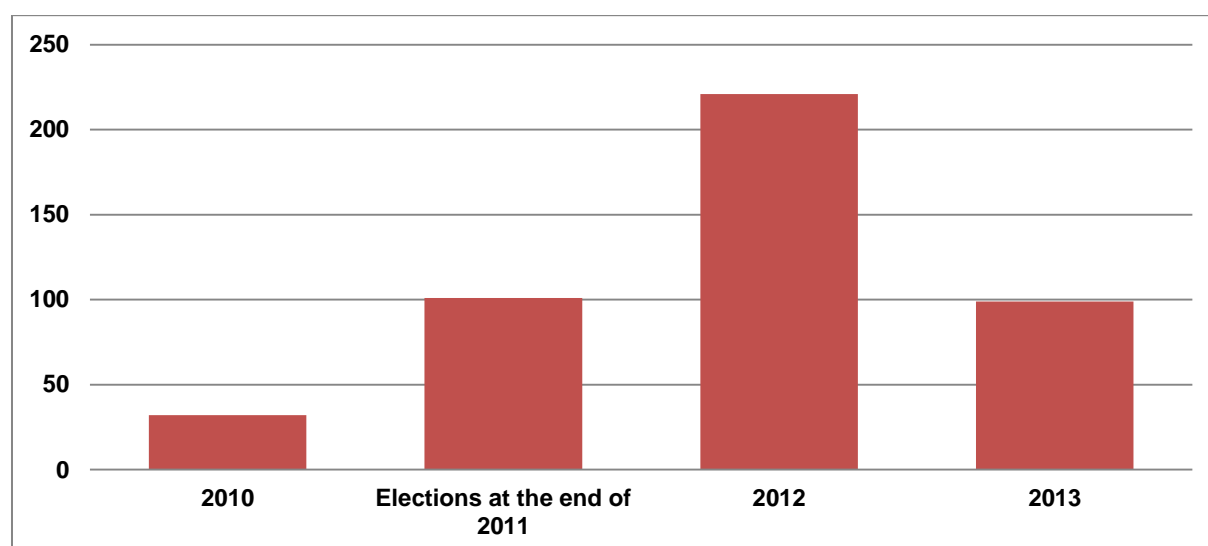
²³ The Act on the Management and Disposal of Assets owned by the Republic of Croatia, Official Gazette 94/13, 130/14 (Article 28.6 of the Act); Act on Local and Regional Self-government, Official Gazette 33/01, 60/01, 129/05, 109/07, 125/08, 36/09, 36/09, 150/11, 144/12, 19/13 (Article 45.1 of the Act). Founding rights, as described in the Act, are those pertaining to the owner or establisher of the entity. In the case of public companies, these are the rights of the owner (a public authority that has established such a company), but in the case of schools, hospitals, social care institutions and similar, that are by nature non-profit and non-state, though established by the state, the public sector (national, regional, or local government) has founding rights. These rights are similar to those of owners in the case of companies, but cannot be equated.

appointments when positions become available owing to retirements or resignations. If they do replace incumbent managers, they might do so for a variety of reasons. For example, they might evaluate an incumbent as being unfit for the job, and wish to replace him or her with a better-qualified candidate. Another possibility is that they might wish to use their power of appointment to reward an informal ally or crony, or to ensure informal influence over an appointee so as to facilitate corrupt transactions. It is near impossible to gain evidence as to the *reasons* for changes in management boards. This analysis seeks rather to measure the extent to which incoming political leaders use their powers of appointment. This will yield insights into the scale of managerial changes associated with political change, and therefore provide an indicator of *potential* political influence over the management of contracting authorities.

The analysis of the relationship between election cycles and changes in management structure uses the following methodology. Data on changes in the management structures of type C and type D contracting authorities were obtained from the Commercial Court Register. The authorities in our sample (i.e., those that had signed contracts for the procurement of works equal to or greater than 1mn euros) were then divided into those owned by the central government and those owned by local and regional governments. This allowed us to identify the relevant electoral cycles in which political change might occur, and subsequently to analyse whether the number of changes in the management of these authorities changed in the periods after elections.

For contracting authorities owned by the central government (a sample of 28), the number of managerial changes increased significantly in the year following the elections held in December 2011 (see figure 4). The number of changes in management personnel in 2012 accounted for 49% of all changes observed in the 2010-2013 period. Of the 28 companies covered in the analysis, 24 had at least one change in management that coincided with the change of government.

Figure 4 Number of managerial changes in legal persons and sectoral (Type C and D) contracting authorities owned by central government, Croatia 2010-2013 (N=28)

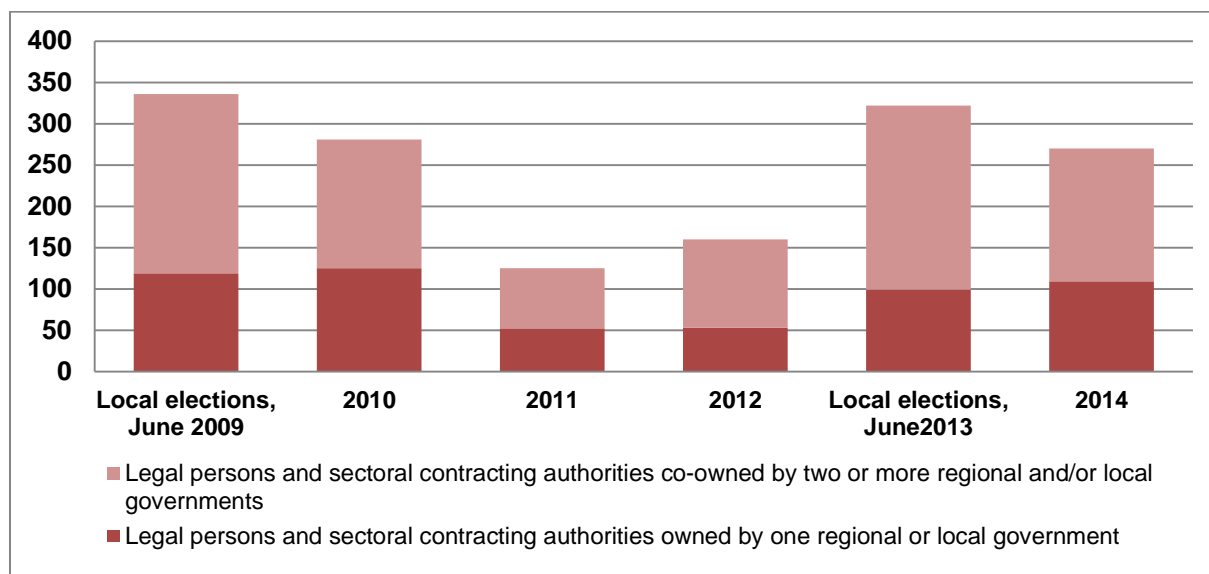


Source: author's calculations based on data from the Commercial Court of Zagreb

For our sample of 95 contracting authorities owned by local government, changes in management were analysed in relation to two elections, in 2009 and 2013. Since local and regional elections are usually held mid-year (before the summer holidays), political

appointments of management board members are expected to occur in the election year and the first post-election year. The number of changes in management does indeed increase at the expected times (see figure 5).

Figure 5 Number of managerial changes in Type C and Type D contracting authorities owned by regional and local government, 2009-14 (N=95)



Source: author's calculations based on data from the Commercial Court of Zagreb

Some entities have more than one governmental owner. A higher number of owners increases the chance that there will be owning government units where elections bring about political change. Since all owners have rights to make appointments to management boards, this also increases the probability that there will be management changes following elections. The evidence confirms this prediction: the number of changes in management in those authorities that were jointly owned by several local and/or regional government units was 68.2% higher than in those owned by a single local/regional government. This finding appears to confirm that changes in management reflect changes in the political leadership of the owning government units, i.e., that political leaders use their powers of appointment over contracting authorities extensively.

An additional check was conducted by focusing on 13 contracting authorities in which no managerial changes were recorded in the observed period. If managerial changes are largely a result of changes in the political control of the owning government unit, we would expect that a lack of change in management would be associated with the absence of political change in the relevant local and regional governments in the period covered. Of 26 possible cases (13 authorities in two election cycles), a change of political leadership in the founding entity (local/regional government), was observed in only four. These findings further support our argument.

2. The Discretionary Power of Managers of Contracting Authorities

Control over the appointment of the manager of a contracting authority can only facilitate favouritism if the manager has significant discretionary power over the entire procurement

process. This is, however, provided for in law. These powers are set out in the 2011 Public Procurement Act. Specifically, the head of the contracting authority is responsible for:

- establishing the entire procurement plan (Article 20.1);
- appointing the Certified Procurement Officers, the authorized representative of the authority responsible for executing the process (Article 24.3);
- appointing the members of the selection committees – whether ad hoc or permanent - who make contract award decisions (Article 24.5);
- signing all documents in the public procurement process, including the final contract (Article 96); and
- supervising the execution of the contract (Article 105.3).

The heads of contracting authorities thus have considerable resources and opportunities to influence the process to serve private interests, if they wish. Given that they in turn rely on political leaders for their initial appointment, their continuance in office, and often for state financial support for their institution, they may also be susceptible to political influence. This suggests that political leaders at central, regional and local government level could have significant informal power over public procurement through their patronage powers.

3. The Role of Central Procurement Officers

Political influence might easily extend - through the head of the contracting authority's power to appoint the Central Procurement Officer - to fine details of the procurement process. The 2011 Act stipulates that public procurement procedures, stretching from the preparation of the tender and conduct of the procedure through to the signing of the contract, are to be carried out only by authorised representatives of the contracting authority, i.e., the CPO. The CPO is appointed by the head of the contracting authority.

The CPO must hold a valid certificate from a special training programme and this must be renewed on the basis of ongoing education or training. Although this stipulation is intended to ensure professional capacity in contracting authorities, in practice it may indirectly create another risk area. This research found that there is a paucity of qualified individuals and typically only one accredited CPO in many contracting authorities. This means that there is nobody else in the organisation qualified to check or oversee the CPO's work.

Since CPOs report to the head of the authority, who is in turn responsible only to the political leader to whom he or she owes his appointment, the overall governance structure potentially allows for one political leader to exert considerable control over the details of individual procurements, while there is scant provision or incentive to carry out internal checks and balances. The existence of such a governance structure is not evidence that corruption occurs. Yet it does indicate that there is significant potential for political leaders to collude with or exercise power over the managers and officers of contracting authorities, with the objective of ensuring favouritism in the allocation of contracts, to benefit themselves or others. The following case study demonstrates that such political influence over the procurement process has been used in the past to channel public money to private interests.

4. Case Study: Political influence over Public Procurement in the FIMI Media case²⁴

The highest-level corruption case ever prosecuted in Croatia concerns the allocation of public procurement contracts to FIMI Media. Several members of the political elite were prosecuted, including former Prime Minister Ivo Sanader, three other high-ranking members of the HDZ, and one of the owners of the private company as well as the ruling political party (HDZ). Although the Sanader case was prosecuted in 2010-11, the appeal is still pending before the Supreme Court. Moreover, legislation has changed since these events occurred, and control mechanisms may have improved. However, for the purposes of this paper, the verdict of the trial has been analysed in order to extract insights into how public procurement might be used to channel resources out of the state for the private benefit of political leaders and parties.

The verdict notes that Sanader and others took advantage of the fact that the HDZ, as the leading parliamentary party, represented a concentration of decision-making power and authority able to play a role in furthering the interests of its financial supporters. The party used its concentrated power in government to collect financial donations from both individuals and legal entities, on the grounds that it needed to finance the party's political activities. In exchange for funds, however, promises were made about using state resources to channel contracts to the companies controlled by the donors.

In his further comments on Sanader's role, the judge emphasised the role played by public companies (entities of Types C and D) in a complex procedure which used public procurement to extract money from the state during the period from the end of 2004 until 2 July 2009. The verdict found that the first accused (Sanader), as the Prime Minister of the Government of Croatia, had engaged the second accused (Mladen Barišić, Head of the Customs Service) to act on his orders. Together they had attended a meeting held on 4 April 2007 in the premises of the Croatian Government, with representatives of companies solely or majority-owned by the state and public institutions. The meeting was also attended by the third accused, Ratko Maček. Sanader had then personally proposed to the leaders of some government bodies, CEOs and others responsible for commercial companies which were exclusively or partly state-owned, using his authority as Prime Minister, and exploiting their relation of dependency (since the Croatian Government appointed their management structures), that they engage the services of Fimi Media (the seventh accused) for the procurement of certain goods and services.

The involvement of so many high-ranking politicians and officials in the government and the evidence that they systematically abused their formal and informal powers over public companies and relevant public entities to influence the public procurement process, suggests that favouritism may be widespread in Croatian public procurement. The scheme involved an

²⁴ This case study is based on the first-instance verdict in the case against former Prime Minister Ivo Sanader, the HDZ and four other persons. The case is currently under the appeal procedure before the Supreme Court, and this research makes no judgement on the guilt or innocence of those indicted. The verdict does however offer important insights into the ways in which politicians interact with the management of public companies. The verdict is based on thousands of pages of evidence and numerous testimonials gathered during a two-year investigation and trial. Source: County Court of Zagreb, First-instance verdict, Reference number: 13 K-US-8/12, March 11th 2014

extensive range of state-owned entities, including two government ministries,²⁵ with political influence over such bodies used to further private interests.

Moreover, existing mechanisms for internal and external monitoring of public procurement proved inadequate to detect these operations, although they were conducted during a period from the end of 2003 until July 2009. Indeed, Sanader and the HDZ were prosecuted only after he had resigned, apparently voluntarily, rather than in response to public pressure. It is unclear whether he would have been prosecuted if he had remained in power.

The verdict also provides evidence about the gains made by the HDZ, the politicians, and the individuals associated with these state-owned entities. It lists nine prominent individuals who made cash donations to the HDZ and the prime minister, many of whom subsequently won contracts from companies owned by the state²⁶, for example:

- **Marijan Primorac** donated EUR 322,368 and paid for Sanader's BMW. His company 'Primorka' benefited from a lucrative contract to rent office space to the Croatian Lottery (public company).
- **Marinko Mikulić** donated EUR 171,052. As the owner of the privatized 'PAN' company, there was no evidence proving that he did illicit business with the state, although questions were raised about how he amassed his personal wealth.
- **Miha Zrnić Marinović** donated EUR 263,157. He owned 'Odlagalište sirovina' (Raw Material Landfill) which, with the Fund for Environmental Protection (state entity), drained the state budget of millions.
- **Božidar Longin** donated EUR 36,000. From 2003 to 2012, he was a board member in charge of legal affairs, including public procurement, in Hrvatske šume (Croatian Forests).

In terms of those who benefited from this scheme, in addition to the five individuals and one political party charged, 30 other members of the HDZ were given cash by the organisers of the scheme (the five accused). They included individuals at all staff levels, from doormen and bodyguards to secretaries and ministers.

V. CONTROL MECHANISMS

The procurement process is subject to control by a number of internal institutions, assessed below. In addition, the potential for civil society, the media, and members of the public to exercise 'external' control is evaluated.

1. The State Commission for Supervision of Public Procurement Procedure

The SCSPPP is charged with investigating potential breaches of the law in connection with the rights and interests of interested parties or competing tenderers (Kolar, Loboja, Vuić, 2011) and is the key legal protection mechanism for the interests of tenderers (Pejaković,

²⁵ The list of public companies involved reads: Hrvatske šume d.o.o., Hrvatska elektroprivreda d.d., Hrvatska poštanska banka d.d., Hrvatske autoceste d.o.o., Autocesta Rijeka-Zagreb d.d., Environment Protection and Energetic Efficiency Fund, Ministry of Interior Affairs, Hrvatska HŽ group – Hrvatske željeznice d.o.o., Croatian National Tourist Board, Proplin d.o.o., Viadukt d.d., Hidroelektra niskogradnja d.d., Konstruktor inženjering d.d., Hrvatske ceste d.d., Croatia airlines d.d., Croatia osiguranje d.d., Narodne novine d.d., Ecos trgovina d.o.o., Financial Agency, Ministry of Sea, Transport and Infrastructure, Ministry of Foreign Affairs and European Integration, ACI d.d.

²⁶ Specifically, companies defined in law as legal entities that are not public authorities or sectoral contracting authorities.

2008).²⁷ However, it may act only at the request of tenderers or interested tenderers (those considering submitting tenders, if a complaint refers to conditions set in the tender), and its enquiries are limited to the irregularities stipulated by the complainant. If no complaint is lodged by any of the tenderers, the SCSPPP will not act and even if a complaint is lodged, it will rule only on the matter stipulated in the complaint and will not investigate further. Thus, in restricted procedures (i.e., negotiated procedures without prior publication) where there is no open competition, there are no grounds for complaint by other interested parties. The fewer the competitors, the less potential there is for the SCSPPP to act.

If it finds irregularities, the *SCSPPP* may cancel the procedure or render a decision resulting in the annulment of the contract. In some cases, it may levy an administrative fine on the contracting authority. Since February 2010, the SCSPPP has also been authorized to file motions for indictment in relation to misdemeanours set out in the Act and other regulations pertaining to the field of public procurement.²⁸

The SCSPPP has used these powers to a limited extent (see table 9). However, given that 1,924 active contracting authorities sign approximately 10,000 public procurement contracts and framework agreements each year, it is not clear that this control mechanism acts as a major constraint on favouritism.

Table 95 SCSPPP Motions filed for indictment in relation to misdemeanours prescribed by the Act, 2010-13

Year	No. of motions filed	Misdemeanours prescribed by the PPA
2010	5	Goods, works or services were procured without a PP procedure
2011	7	Goods, works or services were procured without a public procurement procedure and provisions of the PP Act were not applied
2012	2	Contracting authorities failed to submit requested documentation
2013	7	Contracting authorities failed to submit requested documentation (5 cases) or acted contrary to or failed to comply with a decision (2)

2. The Directorate for the Public Procurement System

The DPPS is in charge of capacity building in the procurement system, including the obligatory, ongoing certified education of CPOs, supervising all aspects of the PP system, and initiating procedures before the Misdemeanour Court for violations of legal provisions prescribed in the PP Act (*ex ante* and *ex post* supervision).²⁹ The DPPS focuses on misdemeanours related to breaches in public procurement systems. Through administrative investigations, the DPPS may act upon an extensive list of breaches of the PP act, relating to

²⁷ Public Procurement Act, Official Gazette 90/2011, 83/2013, 143/2013; Act on the State Commission for Supervision over Public Procurement Procedure, Official Gazette 18/2013, 127/2013, 74/2014.

²⁸ Article 2 paragraph 4 Act on the State Commission for Supervision over Public Procurement Procedure, Official Gazette 21/2010.

²⁹ Note that official title of the body in the Act is the Central Government Authority Responsible for the Public Procurement System, and the official name of the authority in the court register is the Ministry of the Economy; Directorate for the Public Procurement System

failures by the contracting authority to comply with the necessary procedures.³⁰ The DPPS has filed 78 motions since 1 January 2012.

However, our research revealed a number of causes for concern. First, the organisation lacks the capacity to monitor and supervise the large number of contracting authorities and contracts. Second, there is a conflict of interest between its investigative and monitoring powers on one side, and its capacity-building role on the other (training and certifying CPOs, which represents a significant proportion of its operational income). Third, the DPPS as prescribed by law, treats potentially serious criminal activity (conflicts of interest, disregard for competitive procedures and direct contracting) within the (non-criminal) misdemeanour framework, which means that serious infringements may remain beyond the reach of the punitive justice system. Fourth, decisions about the targets of pro-active investigations are left to the discretionary powers of DPPS employees and managers. Fifth, the DPPS is a department of the Ministry of Economy, and may therefore be deterred from undertaking investigations that might criticise the government or ruling party.

3. The State Audit Office

The State Audit Office (SAO) audits the financial management of state entities and establishing whether it is in accordance with public accounting standards. In reference to public procurement, the SAO verifies whether the PP procedure has been applied in areas where it is obligatory, but does not typically examine the details of a particular procurement procedure. However, in accordance with state audit standards and principles, the SAO verifies whether the financial statements issued by an audited entity, including statements on public procurement, are true and accurate.

The SAO acts pursuant to its adopted annual action plans³¹, but it has considerable discretion in terms of the subjects and timing of audits. It is quite possible that Type C and D contracting authorities will never (or only very rarely, perhaps once a decade) be subject to audits by the SAO. Moreover, the SAO cannot impose remedies or sanctions on an audited entity. It simply publishes reports and, if criminal activity is indicated, may forward a report to the relevant prosecutor's office. However, this practice has so far not led to any significant investigations or verdicts in the field of public procurement.

4. The Commission for Conflict of Interest

The CCI regulates provisions relating to conflicts of interest for most elected officials in Croatia, but has no specific responsibility for overseeing public procurement and our research revealed some uncertainty as to whether it is responsible for enforcing the provisions on conflicts of interest under the PP Act.

Article 13 of the PP Act defines situations in which a conflict of interest may exist: (1) if the representative of the contracting authority simultaneously performs managerial duties for the economic operator, or (2) if the representative of the contracting authority holds a business share, stocks or other rights entitling it to participate in the management or in the capital of the economic operator with the share of more than 0.5%. Moreover, representatives of contracting authorities must sign a statement declaring the existence or absence of conflicts

³⁰ See Articles 177 and 182 of the Act.

³¹ According to the provisions of the Act on the State Audit Office (Official Gazette 80/11), audits are planned and performed in accordance with the annual work plan and program, which is adopted by the Auditor General. 2014 work plan is available at: <http://www.revizija.hr/datastore/filestore/34/godisnji-plan-za-2014.pdf>

of interest, which extends to personal relationships with representatives of the economic operators. Such rules apply whether the economic operator with a potential conflict of interest is a single tenderer, member of a group of tenderers, or a subcontractor to the any of the above.

In theory, any action in breach of the law would lead to the contract being void and criminal charges being filed with the State Attorney's Office. However, the Act does not specify who is responsible for monitoring compliance with this provision. The representatives of the institutions interviewed for this research (the SCSPPP, the DPPS, and the Faculties of Law in Zagreb and Osijek), were unsure about who would be responsible for cancelling a contract and reporting the case for further action.

One representative of the CCI took the view that the CCI is competent to perform this role, to the extent that the provisions in the procurement act coincide with Articles 17 and 18 of the Act on Preventing the Conflict of Interest.³² However, this omits many personnel involved in the public procurement process, particularly at the local level. CPOs, for example, are beyond its remit³³, as are the senior managers of economic operators owned and established by local and regional governments remain out of their jurisdiction. The Act on Conflicts of Interest does not cover most Type C and Type D contracting authorities. The Act on the Prevention of Conflicts of Interest does cover the senior management of state-owned companies³⁴, but not public companies that are owned by regional and local governments. In addition, the Act does not cover the heads of contracting authorities that are appointed by individual ministers, mayors or city councils. Overall, the majority of public sector entities (such as schools, hospitals, and social service providers) are beyond the scope of the Act³⁵.

The CCI ruled in 30 cases relevant to public procurement in the period observed³⁶, with consequences for the offenders in 2 cases (HRK 30.000 and HRK10.000 fines).

5. The Criminal Justice System

The criminal justice system has the power to act on reports or indications of criminal acts in the public procurement domain. The police may initiate an investigation following a report from an interested party (a citizen, legal person or prosecutor's office), while prosecutors may initiate investigations based on any information or suspicion of a criminal act, whether originating in the media, public statements or reports by other state authorities or citizens.

However, while Croatia's USKOK institutional framework³⁷ is advanced in terms of the fight against corruption, the lack of public procurement expertise in prosecutors' offices and police departments means they depend on other state bodies for expertise in understanding specific violations of the PP Act. Although the crime of abuse of the public procurement procedure (Criminal Code, Article 254) has existed since 2012, there is no evidence of a

³² Officials covered by the Act on Preventing the Conflict of Interest are officers appointed by or approved by the Croatian Parliament, Government of the Republic of Croatia or the President of the Republic of Croatia; see OG 26/11, 12/12, 124/12, 48/13.

³³ The notion of an official is prescribed in Act On Preventing Of The Conflict Of Interest in Article 3 paragraph 1 (Official Gazette 26/11, 12/12, 124/12, 48/13)

³⁴ Article 3, paragraph 1 (41) of the Act.

³⁵ Act on Conflicts of Interest, Official Gazette 26/11, 12/12, 124/12, 48/13.

³⁶ In 2010, 2011 and 2013. Data for 2012 not available.

³⁷ Croatia has set up a combination of law enforcement and judicial structures specialised in dealing with corruption and organised crime; the so called USKOK Vertical, including the following institutions: National Police Office for the Suppression of Corruption and Organised Crime (PNUSKOK); Office for the Suppression of Corruption and Organised Crime (USKOK) and Special USKOK courts.

single case being prosecuted. The Criminal Justice system has acted on one case of a suspected violation of Article 254 of Criminal Code (*Public procurement procedure abuse*), since this article was introduced in the new Criminal Code and entered into force on 1 January 2013.³⁸ In this case, the criminal allegation was rejected by the Slavonski Brod public prosecutor's office (CBS, 2014).

6. The Transparency Framework and Civil Society Scrutiny

The 2011 Act introduced several new instruments to increase transparency and enhance civil society scrutiny of public procurement procedures. For example, the Act obliges contracting authorities to adopt and publish procurement plans for the budget or business year, to establish and publish a register of public procurement contracts and FAs awarded³⁹, and to update the information in the register at least every six months. However, this research has found that a majority of public procurement procedures take place among state-owned entities that are beyond the scope of many of these rules. In addition, Bajo (2012) has questioned the ability of the public or civil society to scrutinise the financial operations and performance of Type C and D entities, because the official data on their revenues, expenditure, assets and liabilities is provided without adequate information on methodology.

Moreover, the ability for civil society to hold these institutions to account is fundamentally undermined by their governance structure. Civil society organisations might find evidence of anomalies or violations by contracting authorities and raise concerns in the public domain. However, for many Type C and Type D contracting authorities, it is only the owners of the contracting authorities that have the power to impose sanctions on managers. Thus control rests with internal accountability mechanisms that are ultimately controlled by the political party (or political patrons) which appointed those managers. Because national, regional and local governments, and thus elected politicians at these levels, have the right to appoint the senior management structures of these companies, the exertion of political influence over these companies is legal, indeed, institutionalised.

Our research sought to establish the importance of civil society scrutiny in monitoring public procurement by conducting an analysis of media and publicly available data to establish⁴⁰ the number of cases where companies were accused of wrongdoing by the public, civil society or media organisations in connection with the public procurement in our sample. This was then compared with the number of cases in which internal control institutions acted to investigate allegations, and the number of investigations which have thus far led to a verdict. The results are presented in table 10.

³⁸ OG 125/11, 144/12.

³⁹ Publication of actual contracts and framework agreements.

⁴⁰ NB: for the purpose of analysing publicly available data, the following code words are used (affair; procurement; abuse; corruption; investigation; verdict) that commonly appeared in reports on corruption in public procurement or public and private companies.

Table 10 Tenderers with contract(s) above HRK 7,452,830 in public procurement of works detected by accountability mechanisms

	Number of tenderers	Value of work contracts (2011-2013)
Total number of tenderers	175	15.9bn
Allegations	85	7.8bn
Investigations	34	3.2bn
Verdict	7	0.9bn

Source: author's calculations based on online media reports.

The discrepancies between the numbers of allegations, investigations and verdicts suggests that state prosecutors are not actively concerned about public procurement, despite the high standards set in the legal framework. This implies a lack of coordination which may jeopardise the system for ensuring integrity in public procurement procedures. It might also be indicative of particularism in the judicial system.

VI. CONCLUSIONS

Croatia's public procurement law sets a high standard and has established some important transparency and control mechanisms. However, the integrity of procurement is seriously undermined because of the common practice of contracting through entities which are outside the scope of the control framework and, by contrast, greatly subject to political influence. The scope of this problem is extensive. In 2012, the total value of public procurement carried out by Type C and D authorities under weak control mechanisms, along with petty procurement (for which there is no obligation to implement conduct procurement in line with specified procedures), represented around 85% of total procurement. Moreover, analysis of the timing of management appointments suggests that political leaders use their patronage powers over the heads of these contracting authorities extensively.

The research also analysed high-value construction contracts awarded in 2011-13 for indicators of favouritism in the process or outcomes. Whilst use of restrictive procedures is not excessive, competition for public contracts is surprisingly weak in a sector under considerable economic pressure. However, in combination with the weak control mechanisms around many contracting authorities, the indicator of greater concern is that around one-half of contract value is won by tenderers which are not private companies but rather entities that are partially or fully owned by the state. This suggests that political leaders and parties have the potential to influence the process so as to achieve favouritism in the allocation of public contracts, to benefit themselves or third parties. Evidence from the FIMI Media case, involving the most senior politicians in a scheme that used public procurement to trade political donations for contracts, suggests that such favouritism may be widespread. Finally, the existing control mechanisms have a reasonable array of powers in theory, but in practice lack expertise and will to monitor public procurement adequately.

APPENDICES

Appendix 1 Value of public procurement and the proportion of public procurement in GDP, Croatia 2008-2013

Year	GDP in HRK bn	Public procurement in HRK bn	% of GDP
2008	343.4	35.8	10.4
2009	328.7	40.6	12.4
2010	323.8	24.8	7.7
2011	328.7	30.8	9.4
2012	327.0	31.5	9.6
2013	326.8	31.6	9.7

Source: author's calculations based on data from the Directorate for Public Procurement System and Croatian Bureau of Statistics

Appendix 2 Structure of the value of public procurement by type of contracting authority, Croatia 2008-2013 (in HRK bn and % of total)

		Type A	Type B	Type C	Type D	Petty PP	Total
2008	HRK bn	1.5	8.7	19.6	3.1	3.0	35.8
	%	4.1	24.4	54.7	8.6	8.3	100.0
2009	HRK bn	3.4	6.0	23.0	4.9	3.2	40.6
	%	8.4	14.7	56.7	12.1	8.0	100.0
2010	HRK bn	2.8	2.1	9.7	5.6	4.6	24.8
	%	11.21	8.35	39.14	22.69	18.60	100.0
2011	HRK bn	2.9	2.2	14.1	7.1	4.6	30.8
	%	9.3	7.0	45.9	22.9	14.9	100.0
2012	HRK bn	1.7	2.5	15.1	7.3	4.9	31.5
	%	5.48	7.90	47.97	23.20	15.45	100.0
2013	HRK bn	2.1	5.8	16.4	2.2	5.1	31.6
	%	6.6	18.3	52.1	7.1	16.1	100.0

Source: author's calculations based on data from the DPSS

Appendix 3 Value of executed construction works, Croatia 2008-2013 (in HRK bn and % of GDP)

Year	GDP in HRK bn	Total construction sector, value in HRK bn	% of GDP	Construction procurement value in HRK bn	% of procurement in construction sector value
2008	343.4	27.8	8.1	8.4	30.2
2009	328.7	24.4	7.4	21.8	89.3
2010	323.8	17.9	5.5	9.8	54.7
2011	328.7	16.8	5.1	9.4	56.0
2012	327.0	16.0	4.9	9.1	56.9
2013	326.8	15.1	4.6	10.0	66.2

Source: author's calculations based on data from the Croatian Bureau of Statistics and the Directorate for Public Procurement System

Appendix 4 Contracting authorities with contracts for the procurement of works equal to or greater than HRK 7,452,830, Croatia 2011-13

<i>State-owned enterprises</i>	Small enterprises	Medium enterprises	Large enterprises	Total
<i>2011-2013</i>				
Number of enterprises showing profits	9	15	5	29
Cumulative profits (HRK)	8,797,156	219,358,113	1,536,235,858	1,764,391,127
Value of public procurement, works contract/s (HRK)	550,201,469	4,156,165,111	722,135,139	5,428,501,719
Number of employees 2011	718	3,013	10,745	14,476
Number of employees 2012	714	2,974	10,686	14,374
Number of employees 2013	688	4,377	9,472	14,537
Number of enterprises showing losses	5	8	7	20
Cumulative losses (HRK)	-27,906,384	-283,976,120	-1,776,307,228	-2,088,189,732
Value of public procurement, works contract/s (HRK)	352,236,618	475,137,378	1,109,985,501	1,937,359,497

Number of employees 2011	587	1,143	17,312	19,042
Number of employees 2012	599	1,277	16,349	18,225
Number of employees 2013	569	1,250	15,666	17,485
Total state-owned enterprises	14	23	12	49
<i>Private-owned enterprises 2011-2013</i>	Small enterprises	Medium enterprises	Large enterprises	Total
Number of enterprises showing profits	45	38	12	95
Cumulative profits (HRK)	102,736,738	660,582,809	636,070,612	1,399,390,159
Value of public procurement, works contract/s (HRK)	1,141,415,544	3,414,113,397	1,692,565,885	6,248,094,827
Number of employees 2011	1,772	4,779	6,089	12,640
Number of employees 2012	1,831	4,751	6,117	12,699
Number of employees 2013	1,926	4,899	6,003	12,828
Number of enterprises	11	14	6	31

showing losses				
Cumulative losses (HRK)	-154,537,039	-278,685,954	-1,938,344,411	-2,371,567,404
Value of public procurement, works contract/s(HRK)	484,331,279	688,838,137	1,121,360,903	2,294,530,320
Number of employees 2011	942	1,811	5,691	8,444
Number of employees 2012	509	1,651	4,362	6,522
Number of employees 2013	427	1,414	3,626	5,467
Total private-owned enterprises	56	52	18	126
TOTAL ENTERPRISES	70	75	30	175

Source: author's calculations based on data received from the Directorate for Public Procurement System and Financial Agency

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ABSTRACT

Germany has the highest public procurement expenditure in the EU, with an average of 370 billion euros a year between 2009 and 2013. The main objective of this report is to shed some light on the inner workings of the German public procurement system by providing a general overview of its historical development, the current trends in procurement spending and assessing potential risks for corruption. Given that Germany has two parallel procurement systems active at the time, one for contracts above the EU thresholds and one for the contracts underneath these limits, each one of them is evaluated separately. The lack of high quality tender-level data for the case of Germany made it impossible to base the risk assessment on objective indicators. Therefore, this report relies on different sources of data to determine the size of the procurement spending in the country, the manner in which it is allocated and the potential risks of corruption. The study concludes that the public procurement system in Germany – especially the one in place for contracts underneath EU thresholds – is vulnerable to corruption given its complex legislation that damages nation-wide competition, the lack of transparency in the awarding process, a clear or unified national legislation and the low utilization of e-procurement platforms.

LIST OF ACCRONYMS

BKA	Federal Criminal Police Office
BMWi	Federal Ministry for Economic Affairs and Energy
CAN	Contract Award Notice
CoC	Control of Corruption
CPI	Corruption Perception Index
DVA	German Committee for Public Procurement and the Award of Contracts in Construction
EC	European Community
EU	European Union
GG	German Basic Law
GWB	German Act Against Restraints on Competition
IfM	Institut für Mittelstandsforschung
OECD	Organisation for Economic Co-Operation and Development
RVA	Imperial Committee for Public Procurement
SektV	Sector Regulation
TED	Tenders Electronic Daily
TI	Transparency International
VgV	Public Procurement Rules
VOB	Contracting Rules for Public Construction Contracts
VOF	Rules on Public Procurement and the Award of Contracts for Freelance Services
VOL	Contracting Rules for Services
WB	World Bank

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I. INTRODUCTION

The present report takes a look at Germany's legal system and analyses the available data in order to provide an inside view of the inner workings of the German public procurement system. Doing this for the particular case of Germany is highly relevant given the size of the German economy and the size of its procurement sector. According to National Accounts Statistics from the Organisation for Economic Co-Operation and Development (OECD), government procurement represents around a third of Germany's general government expenditure. The size of the sector is not the only reason why Germany is a highly interesting case. Transparency International's (TI) Corruption Perception Index (CPI) and the World Bank's (WB) Control of Corruption (CoC) indicator usually rank Germany among the least corrupt countries in the world. The ANTICORRP project first policy report, *Anticorruption Report Vol. 1* (Mungiu-Pippidi et al. 2013), also ranks Germany as a country with low resources to fuel corruption and high constraints to control it, but recent events have drawn the public eye to Germany's construction sector and its procurement system.

In past years, scandals related to big infrastructure projects exploding in costs and not being ready on time have emerged in a country that was previously praised for its efficiency and punctuality. Some of the most memorable examples include the Berlin-Brandenburg Airport (BBI) set to open in June 2012 and now delayed until at least 2016 and the *Elbphilharmonie*, Hamburg's shot at building an iconic concert hall that was supposed to be completed in 2010, but remains unfinished five years after the deadline and has more than doubled in cost. On top of the delays and the escalating costs in some major projects, the official statistics of the German Federal Criminal Police Office (*Bundeskriminalamt*- BKA) also show that obtaining public contracts is the number one reason for offering bribes since 2009. 64% of all bribery cases in 2013 were linked to this purpose and another 5% were intended to buy competitive advantages (Bundeskriminalamt 2013).

Putting the current scandals aside, studying Germany's public procurement system and assessing its potential risks for corruption and government favouritism is a particularly relevant task given the amount of public money involved. Germany has the highest public procurement expenditure in the EU, which averaged 370 billion euros a year between 2009 and 2013. Despite having relatively similar-sized economies, this figure is 30% higher than in France and 40% higher than in the United Kingdom, Europe's second and third biggest economies after Germany. German procurement spending, however, is particularly hard to track. The lack of available data makes it very difficult to answer even some of the most basic questions about the sector, such as the composition of the spending, the number and value of contracts awarded or even the number of contracting authorities in the country. A study by the *Institut für Mittelstandsforschung* (2008) estimates that there are around 30,000 contracting authorities in Germany, but the EU's Annual Review of Public Procurement estimates that there are only between 15,000 and 20,000 contracting entities in the country.

These reasons make Germany an interesting case study and emphasise the need to look deeper into its procurement system and gather evidence that can help reveal its inner workings

in order to determine whether the stories of Berlin's airport and Hamburg's concert hall are simply isolated cases or the visible symptoms of a deeper problem. The main objective of this report is to provide a general overview of the procurement sector in Germany, its development, current trends and potential risks for corruption. The report is divided into four sections: the first part offers a short summary of the German legal framework, its origins and the influence of the European Union (EU) on it. The second section provides an overview of the current public procurement trends in the country. It relies on different sources of data to quantify the size of the procurement spending in the country, the manner in which it is allocated and the most commonly used awarding procedures in the country. This section also discusses the quality of the data available and its problems. The third part of the report assesses the potential risks of corruption and government favouritism in the procurement process by considering the strengths and weaknesses identified in the previous sections. The final section offers a summary of the findings in the report.

1. Legal Framework

This section provides a short historical overview of the origin and development of public procurement regulation in Germany. The purpose of this section is to explain how the current system came to be and how the EU has affected Germany's public procurement system. This part also describes how Germany has adapted its legal framework to comply with European legislation.

1.1 *Historical development of procurement laws*

The regulation of public procurement has a long-standing tradition in Germany. The first laws in the sector date back to the 16th century and include the "Instruction on the fortress Ingolstadt" of 1542, the "Construction Order for Hamburg" from 1617, the "*Submissionspaketen of Mannheim*" from 1699 and the "Prussian building regulations" of 1724. The first comprehensive procurement directives, however, were issued in the 1830s for public buildings in Bavaria and Württemberg and in 1885 for Prussia (Rechten & Rübke 2014). The first draft for a unified contracting law dates back to 1913 and was prepared by a parliamentary commission. The draft included important innovations such as the obligation to assess the suitability of candidates and the adequacy of the proposed prices. These measures were intended to put an end to the often-predatory price-competition. This legislation never saw the light due to the beginning of World War I and a second attempt to adopt the imperial framework law on public procurement after the war also deemed fruitless. However, given the practical importance of the topic, the then Imperial Government of Germany set up the Imperial Committee for Public Procurement (*Reichsverdingungsausschuss- RVA*), which published the Contracting Rules for Public Construction Contracts (*Verdingungsordnung für Bauleistungen- VOB*) in 1926 and the related Contracting Rules for Services (*Verdingungsordnung für Leistungen- VOL*) in 1936 (Rechten & Rübke 2014).

The VOB and the VOL standards gained importance after the end of World War II (Rechten and Rübke 2014), particularly in the early post-war years, as they constituted the basis for the reconstruction of Germany. Since then, the German Committee for Public Procurement and the

Award of Contracts in Construction (*Deutscher Vergabe- und Vertragsausschuss für Bauleistungen*- DVA) has the task to revise and amend the public procurement regulations in Germany. The DVA is an unincorporated association, whose members include representatives from the public sector (federal ministries, provincial ministries and municipal associations) and from the private sector, including the construction industry. This committee is supposed to keep a fair balance between the interests of the contracting authorities and of the service providers. Similar bodies exist in order to revise the VOL, as well as the Rules on Public Procurement and the Award of Contracts for Freelance Services (*Vergabe- und Vertragsordnung für freiberufliche Dienstleistungen*- VOF) issued in 1997.

1.2 *The influence of the EU on the German public procurement system*

The influence of the EU on the German public procurement sector began in the 1970s. The then European Community (EC) introduced several measures to harmonise the legal public procurement framework across its member states: The procedures for awarding public supply contracts were co-ordinated with Directive 77/62, which introduced three fundamental principles: contracts had to be advertised community-wide, discriminatory technical specifications were prohibited and tendering and award procedures had to be based on objective criteria. Similar principles of transparency and non-discrimination were applied to the awarding of public works contracts with Directive 71/305. These directives, however, did not replace national tendering procedures and practices with a set of common rules.

Directive 88/295 amended all previous public supplies directives and made open tendering procedures the norm and negotiated procedures were allowed only in exceptional circumstances. Moreover, purchasing authorities were required to publish advance notices of their annual procurement programmes as well as details of each award decision. Moreover, with the first Remedies Directives, 89/665 (relating to public works and goods contracts) and 92/13 (relating to public utilities), Member States were required to ensure rapid and effective judicial review of decisions by contracting authorities. The directives also introduced the "attestation procedure" as a way for contracting authorities to certify the compliance of their purchase procedures and practices with procurement law.

The harmonisation of Member States' public procurement procedures was completed with the introduction of directive 2004/18/EC regarding the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts. The EU public procurement directives only apply for contracts above a certain threshold, which is why it is more appropriate to speak of a codified EU public procurement law rather than a German one in these cases. However, the National legal framework still applies to public contracts that are under the applicable threshold. The adjustments made to the German legal system in order to accommodate the EU directives occurred using a somewhat unusual procedure: The German Federal Government initially met the changes requested by the EU through a purely budgetary approach: Public procurement was regulated from a budgetary perspective. The principles of economy and efficiency in public spending included in the Budget Law, would translate into the

necessity of guaranteeing competition among bidders, as well as the selection of the cheapest and best offers. The details regarding the procurement procedures were laid down in the VOB, VOL and VOF. As a result, additional legislation was not deemed necessary. This is the so-called "budgetary solution" (*Haushaltsrechtliche Lösung*). However, since the contracting rules established in the VOB, VOL and VOF did not have legal value, bidders were not able to derive any legal protection from them.

As one of the main objectives of the EU directives was to reduce the room for discretion in the award of public contracts and to protect the bidders' rights, the European Court of Justice (ECJ) and the European Commission considered Germany's "budgetary solution" insufficient given that bidders did not have the right to take the contracting authority to court the case of a breach of the procedures outlined in the VOB, VOL and VOF (Dauelsberg 2009). This led Germany to reform its public procurement system in 1999 and adopt what is known as the "anti-trust solution" (*Kartellrechtliche Lösung*). The new procurement system was created through the modification of the German Act Against Restraints on Competition (*Gesetz gegen Wettbewerbsbeschränkungen- GWB*) and the creation of the Public Procurement Rules (*Vergabeverordnung- VgV*). The GWB was changed to include general principles that would guarantee transparent award procedures, equal treatment for all bidders and the obligation to accept the economically most advantageous bid, but most importantly, it granted bidders the right to demand the contracting entities to observe the relevant procurement rules. Since the GWB does not contain specific procedures to regulate the procurement process, these were introduced by the VgV, which on top of establishing a few specific procedures for the procurement process, turned the VOB, VOL and VOF into legally binding regulations.

Since 1999, the GWB and the VgV together with the VOB, VOL and VOF, constitute the core of the German public procurement system. They have been subject to various modifications in response to more recent EU directives, such as the 2004/18/EC on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts and the Public Procurement Remedies Directive (2007/66/EC) with regard to improving the effectiveness of review procedures concerning the award of public contracts. In order to implement the Directive 2004/17, the German government also enacted the Sector Regulation (*Sektorenverordnung- SektV*) (Authority for the Supervision of Public Contracts 2010).

1.3 *Legal framework for domestic procurement*

As shown in the previous section, the EU has had a big impact on the German legal public procurement framework. It is important to mention, however, that most of the reforms apply only to contracts that need to be advertised at EU level, i.e. those tenders above a certain threshold (around 130,000 euros for goods and service contracts and five million euros for public construction contracts). For the case of Germany, the rules that apply for contracts below the EU thresholds are very different from EU laws and therefore need to be explained separately. The large differences in the systems are the result of the origin and historical development of the procurement legislation, as well as of Germany's strong federal structure. These elements

combined resulted in two parallel systems of awarding public contracts and a complex national legal framework that can vary from state to state and from one municipality to the next (Rechten & Rübke 2014).

The main difference between the European and the domestic procurement systems in Germany is that the GWB and the VgV do not only apply for contracts below the EU-defined thresholds. In these cases the Budget Laws of the federal, state or local governments become the legal framework regulating the procurement process. Budget laws in Germany include the principles of transparency, economy and cost-effectiveness as the main guidelines for public spending, but the specific procedures regarding the awarding of public contracts are not described here and therefore vary greatly across the country: federal and state financial regulations stipulate that the award of contracts must be preceded by an open tender and that they must be conducted in accordance to the rules stated in the VOL, VOB and VOF.

At the local level, however, the respective municipal regulations or municipal budget regulations provide only rudimentary principles for public contracting: some municipalities also apply the VOB for construction projects, the VOL for goods and services and the VOF for professional services, but others apply partial or modified versions of them or do not apply them at all and allow contracting authorities to develop their own awarding policies. According to Rechten & Rübke (2014), however, since the VOB, VOL and VOF were developed by representatives of both the contracting authorities (federal, state and local authorities) and the bidders (business associations and chambers of commerce), the rules contained in them are largely consented and accepted and therefore are used in public procurement across the country even where the law does not oblige the parts to apply them. Nevertheless, since the use of the procurement rules contained in the VOB, VOL and VOF is based on internal decrees and on the Budget Law, which are simply internal public administration laws, violations against them cannot be taken to court unless they infringe the principle of equality before the law, which is embedded in article 3 of the German Basic Law (*Grundgesetz*- GG). This means that an incorrect choice of procurement procedure does not necessarily lead to an infringement of the award rights of an unsuccessful bidder. The chosen procurement procedure must diminish the chances to get the award for a bidder's rights to have been infringed and for litigation to be possible.

The situation described above presents obvious challenges when assessing potential corruption risks, especially at the national level. Germany's method of awarding contracts below the EU thresholds has sparked criticisms from several fronts: The European Commission and the German chapter of TI, for example, have warned against several risks, such as the insufficient legal protection for bidders and the lack of transparency in the award process. Moreover, as explained before, in the case of national contracts, the rules of the game change from state to state and sometimes even from one municipality to the other and the observation of the procedures contained in VOB, VOL and VOF, which are legally binding at European level, can become a non-binding, informal agreement when awarding contracts within the domestic market. Whether Germany will replace its complex procurement law system with a unified procurement law as many other EU Member States have done, is still an open question.

2. Public procurement trends in Germany

As revealed in the previous section, the German public procurement system is characterized by a strong degree of fragmentation due to the country's strong federal character and the influence of the EU, which has re-shaped the manner in which contracts are awarded above a certain threshold. The procurement process for contracts underneath these thresholds, however has been left behind and as a result Germany's "budget" and "antitrust solutions" now have to co-exist and the legally binding procurement rules that apply at the European level are not applicable at the domestic one. This could be a source of concern for many, but Rechten and Rübke (2014) claim that since the contracting rules were formulated and agreed upon by representatives of the public and the private sectors, they are widely applied and respected across the country. This section analyses the available data in order to assess whether or not the implementation of the European and the national procurement frameworks leave room for the occurrence of corruption or favouritism in the country. It is necessary to note, however, that data quality and availability constituted a major obstacle to do this.

One of the objectives of this section is to collect empirical evidence to assess the extent of corruption and government favouritism in the German public procurement system, particularly for the case of the construction sector. But before this, it is necessary to discuss some of the data gaps and data quality issues mentioned above. This section is therefore divided in three parts, the first one is about data quality and the current data gathering procedure that prevails in Germany. The second part presents an analysis of the procurement trends above EU thresholds derived from the Tender European Daily (TED) Database and the third part relies on diverse sources to paint a picture of what happens in the awarding process underneath the threshold.

2.1 *Data quality and availability for Germany*

After gathering all the available statistical data on procurement from the BMWi and the European Commission some of the challenges of analysing the trends of the German public procurement system became apparent. Answering basic questions such as the total value or volume of procurement in the country was not possible since the official procurement figures from the Federal Ministry for Economic Affairs and Energy (*Bundesministerium für Wirtschaft und Energie*- BMWi) are incomplete. The data published by the BMWi are simply aggregated values of contracts awarded by sector (goods, services and works) and level of government (central and local). Moreover, the BMWi tables report mostly tenders above the EU thresholds. As a result, EU and OECD estimations had to be used to calculate the total volume of procurement.

Despite great effort, no tender-level data could be obtained for contracts below the thresholds. Further research revealed, however, that the failure to obtain this data was simply due to the fact that Germany lacks an appropriate procedure to compile and publish this information and that such data does not currently exist. An evaluation conducted by Kienbaum (2014) on the current data collection practices in the framework of public procurement confirms that the information on contract awards below the EU thresholds do not currently exist in a TED-like database that

would allow for their analysis. Moreover, this study also finds that the current data collection process is overly complex and inefficient, which results in low quality data.

According to Kienbaum (2014), the current data collection system is labour-intensive and error-prone (Kienbaum 2014). In the current top-down collection process, the BMWi has to request the information from each federal and state ministry to put together the aggregated statistics, which generates excessive workloads for all parties involved. The results of the study conducted by Kienbaum (2014) on request of the BMWi, reveal that the Ministry usually contacts state and local contracting authorities one by one in order to obtain their data. On top of this being a labour-intensive task, the quality of the data submitted by the state and local authorities is often poor. Time and personnel constraints do not allow for an extensive verification of the data and most of the time only obvious mistakes or omissions are spotted. In case of errors, the BMWi has to contact the local and state authorities again and wait for an answer. Moreover, there is no information regarding how many contracting authorities submit their reports to the BMWi, as there is no monitoring mechanism for non-response rates (Kienbaum 2014).

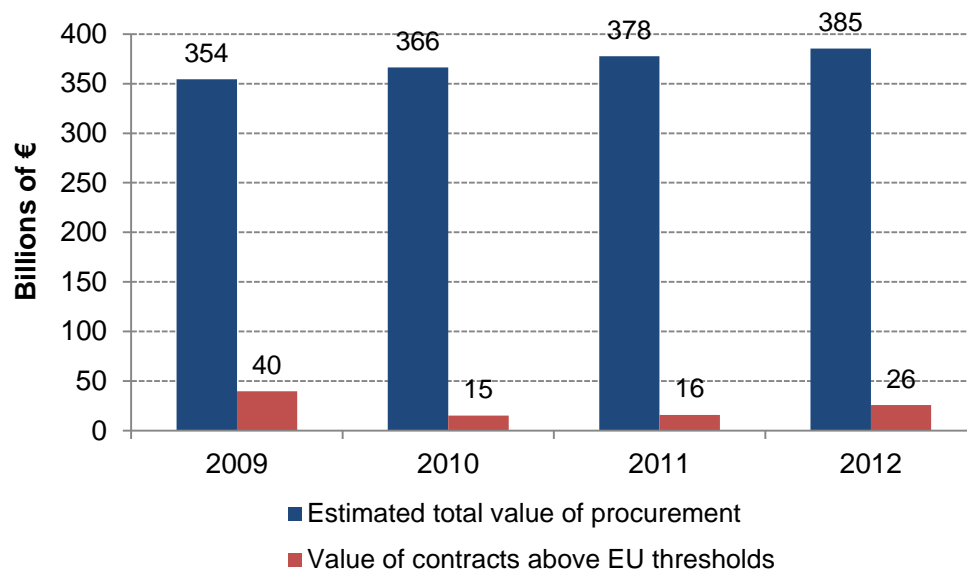
This data collection process has been widely criticized as inadequate (Transparency International Deutschland 2011; European Commission 2013; Kienbaum 2014) because it has negative effects on the data compiled and makes it virtually impossible to gather the information on contracts underneath the EU thresholds, which constitute the bulk of the procurement value and volume. A simple indicator captures the low quality of the German public procurement data: the number of contract award notices (CAN) in the TED database that includes the value of the contract. In 2011, according to the 2013 Annual Public Procurement Implementation Review of European Commission, Germany ranked among the bottom five countries in this indicator, with less than half of the CANs including their value. Although the quality of the TED data for Germany seems to have improved over the past couple years, more than a third of the 115,000 CANs included in the TED still do not include information regarding their value.

Despite data collection problems and their obvious effects on data quality, the TED database can still offer some insights regarding contract awards above the EU thresholds. The following section provides an analysis of this data and although the results might not be completely accurate, the large number of contracts included in the database is still enough to provide a general depiction of the main trends.

2.2 *Trends in procurement spending above the EU thresholds*

The level of spending on public procurement in Germany is estimated to be somewhere between 300 and 500 billion euros a year (Kienbaum 2014, European Commission 2014b). Using the EU's estimations as a baseline, the value of the contracts above EU thresholds comprises only a small fraction of total procurement. **Figure 1** shows that, with the exception of the year 2009, the data provided by the BMWi does not account for more than 10% of the total estimated value of procurement. This implies that the bulk of the contracts awarded in Germany are granted following the national and not the European procurement legislation. Despite this fact, no data is available for contracts underneath the thresholds, as Germany's legal framework does not require contracting entities to keep tender data in a centralized database.

Figure 1 Total value of reported contracts vs. total estimated value of procurement (2009-2012)

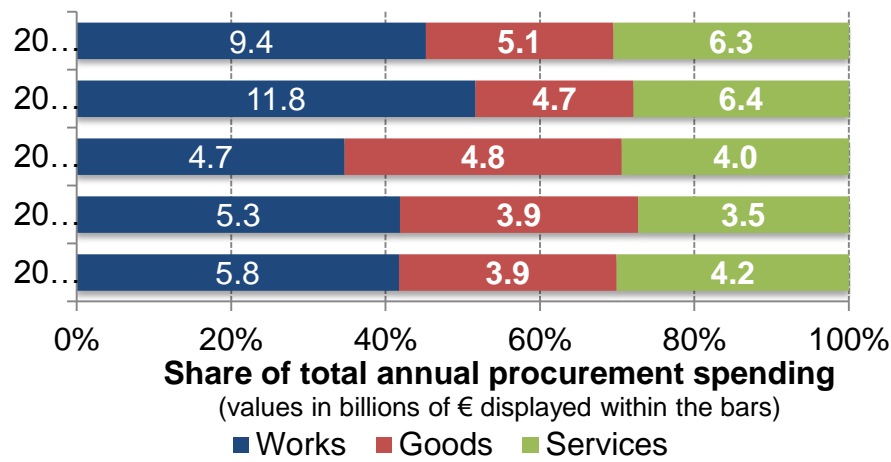


Source: BMWi and EU Public Procurement Indicators 2012

An important characteristic of German procurement spending is that it is highly de-centralised. The available statistics from the BMWi show that the local and state authorities are responsible for two-thirds to three quarters of the procurement spending above EU thresholds (BMWi 2014). This figure is even higher in the construction sector, where central government procurement accounts only for 10% of the total procurement spending.

The data published by the BMWi also reveals that procurement spending goes mostly to infrastructure. **Figure 2** shows that over 40% of the total spending goes to the construction sector. It also shows a dramatic increase in procurement spending in this sector between 2011 and 2012, when it more than doubled by going from 4.6 to 11.8 billion euros. Overall, the value of infrastructure contracts above EU thresholds has tripled since 2005. Although the value of EU-level tenders for goods and services have also grown steadily, infrastructure remains the biggest target for procurement funds in Germany.

Figure 2 Composition of total procurement spending (2009-2013)

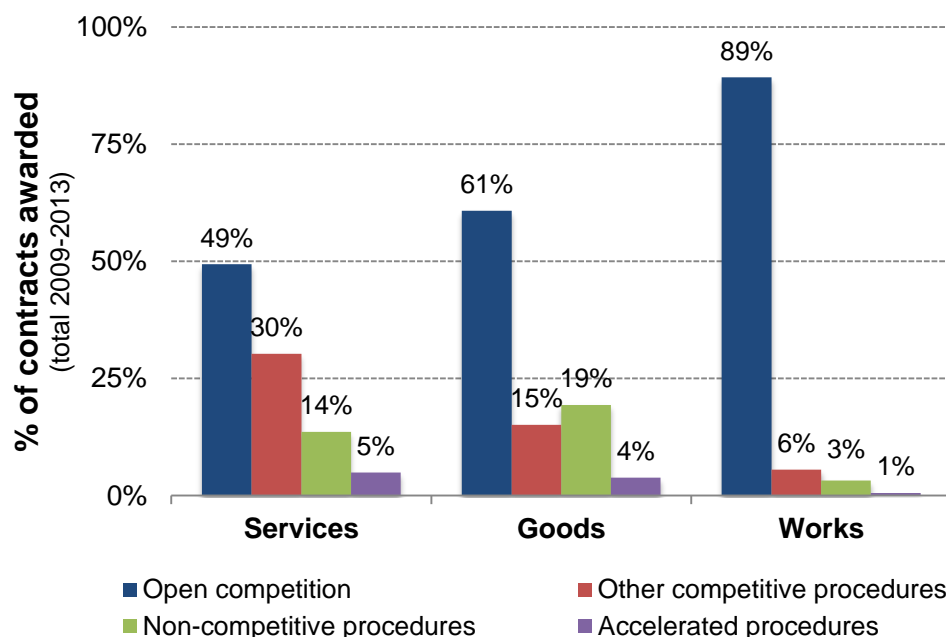


Source: BMWi

One of the objectives of this report is to take a closer look at the way in which contracts are awarded in order to detect risks of corruption and possible cases of government favouritism. The overall assumption here is that open or competitive procedures are less prone to corruption than non-competitive ones, as the latter make it easier to favour some bidders over others. The TED Database can be used to get an overview of the awarding procedures most commonly used in Germany. This allows checking whether or not a restricted or other non-competitive awarding procedures are being commonly used, thus opening the door for discretionary allocation of public funds.

Figure 3 shows that most of the contracts contained in the TED database are assigned through competitive mechanisms. However, there are differences across sectors: 89% of all infrastructure contracts awarded between 2009 and 2013 were assigned through open competition and another 6% through a competitive dialogue or a competitive negotiation. In the case of the purchase of goods, 61% of contracts were awarded through open competition and 15% through other competitive methods. Open tendering is least used for the award of professional service contracts: open tenders were used in only 49% of the cases, other competitive methods such as competitive dialogue or a competitive negotiation were used for another 30% of contracts.

Figure 3 Contracts awarded by type of procurement procedure (2009-2013)

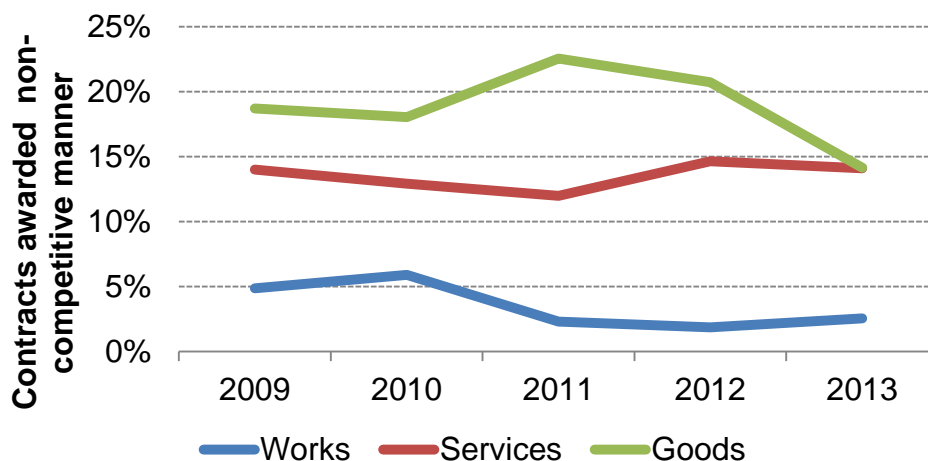


Source: TED Data

These results portray Germany under a positive light in terms of the type of procurement procedure chosen. The fact that almost 90% of all infrastructure contracts between 2009 and 2013 were awarded through an open tender would suggest that the risks of government favouritism in this particular sector are fairly low. These risks seem to be higher among the purchase of goods and the hiring of professional services, where 20 and 14% of contracts, respectively, are awarded through restricted or non-competitive procedures. The results from the TED database also reveal that the infrastructure sector has consistently had the lowest levels of non-competitive awarding procedures since the data is available (See **Figure 4**).

The practice of giving unfair preferential treatment to one person or group at the expense of another is the definition of favouritism. Bribes are usually the currency used by companies to buy political connections that will grant them preferential treatment. In comparison to smaller firms, large companies possess more financial resources to do this. According to the 2014 OECD Foreign Bribery Report, for example, big companies are more likely to bribe than SMEs (OECD 2014: 8). The same OECD report also reveals that more than half of the cases of international bribery documented were intended to secure public contracts (OECD 2014: 8). Given that over 40% of the total spending in public procurement above the EU thresholds in Germany goes to the construction sector, it is worth analysing whether this sector presents symptoms of favouritism.

Figure 4 Share of non-competitive procurement methods in EU-level contracts (2009-2013)



Source: TED Data

Since public contracts are supposed to be awarded competitively, finding a reduced number of companies constantly benefiting from them can indicate that there are underlying factors affecting open and free competition in the sector. **Table 1** displays the total value of public contracts obtained by some of Germany's top ten biggest construction companies between 2009 and 2013. As can be observed, the total value of these contracts does not exceed 5% of the total procurement spending in the sector. Even when expanding the list to include the contracts obtained by the top 15 companies in the sector, their market share only amounts to a maximum of 11% of the spending. This evidence therefore suggests that there is a healthy, competitive market for construction contracts above the EU thresholds in Germany. It is also worth mentioning that none of the 100 richest Germans obtained their fortunes by competing in the construction sector: Families Goldbeck and Bauer – owners of the companies of the same names listed in **Table 1** – are among Germany's wealthiest, but not even close to the top positions. The top positions in the list of wealthiest people in the country are occupied by people from a variety of sectors such as the pharmaceutical, automotive, insurance, software, transportation, retail and fashion industries, but there is no mention of construction moguls.

The findings derived from the TED data portray the procurement process in Germany as a relatively low-risk environment for corruption with the majority of contracts being awarded competitively, declining trends in the use of non-competitive procurement methods and with the biggest enterprises in the country taking only less than five percent of market in the construction sector. Nevertheless, it is necessary to bear in mind that the results reported in this section originate from contracts that exceed the EU thresholds, which make up for only a small fraction of the full picture. Due to this reason and the fact that the legal public procurement framework that applies below the EU threshold is significantly different these results cannot be transposed to the national level. The following section analyses the procurement system for contracts below the EU thresholds and checks for potential red flags.

Table 1. Total value of contracts awarded to German top construction companies by year

Company	2009	2010	2011	2012	2013
Bauer	4,864,941	-	1,748,238	3,519,454	281,425,339
Bilfinger	105,547,243	24,984,947	47,956,809	24,014,326	25,606,515
Ed Züblin	32,423,624	17,948,613	20,783,096	1,908,264	33,720,799
Goldbeck	28,087,907	13,752,882	24,200,000	2,763,757	16,652,333
Hochtief	35,469,892	15,386,859	-	330,442,016	90,447,355
Siemens	28,679,976	26,801,434	25,873,181	103,466,749	8,397,717
Share of total obtained by top construction companies	4.04%	1.87%	2.58%	3.93%	4.84%

Source: TED Data

2.3 Trends in procurement underneath the EU thresholds

Evaluating the public procurement system below the EU thresholds is a challenge for the case of Germany since there is no database containing similar information to what can be found in the TED data. The lack of reliable statistics is a known problem and stems from the fact that contracting authorities are not legally bound to keep a publically accessible record for contracts underneath the thresholds. As a result of this, it is currently impossible to replicate the methodology used in the previous section to identify potential risks of corruption. As an alternative approach to the analysis of raw procurement data, this section will try to shed some light on what goes on behind the scenes of the domestic awarding processes by looking at a different type of evidence that, despite not being based on factual data, might at least point at red-flags in the sector.

The first source of information that can help draw a picture of the inner workings of the public procurement system in Germany is the Flash Eurobarometer 374 survey “Businesses’ attitudes towards corruption in the EU”. This survey was carried out between February and March of 2013 with the primary objective of understanding the level of corruption perceived by businesses in different sectors. To do this, companies were asked about corruption in a range of areas including the management of public tender and public procurement processes. Given that Germany is consistently ranked by TI’s CPI and the WB’s CoC indicator as one of the least corrupt countries in Europe and around the world – both TI and the WB rank Germany in position 6 in the EU and among the top 15 globally – one would expect the business community in the country to perceive illegal practices in procurement to be rare. However, this is not the case: according to Eurobarometer results, Denmark, Finland, Estonia and the United Kingdom

are always among the countries with the lowest levels of perceived corruption in public procurement, but Germany is nowhere near these four countries.

Table 2 below shows the percentage of respondents that believe that the listed illegal procedures such as conflict of interest in the evaluation of bids, unclear evaluation or selection criteria or abuse of certain procedures to either accelerate the awarding procedure or use non-competitive procedures are widespread in Germany. Just to provide some additional perspective, the average for the EU27 as well as the position that Germany occupies within the 27 EU Member States are also reported. As can be seen from the results in **Table 2**, the German business community is critical of the manner in which contracts are awarded in the country: a majority of the respondents believe that collusive bidding and the involvement of bidders in the design of contract specifications are widespread practices in Germany. 44% of respondents also believe that amendments to the contracts terms often occur after the conclusion of the procurement process. This figure coincides with the EU average and places Germany in the worst performing tercile in the region. It is also worth noting that almost half of the respondents in Germany also believe that tailor-made specifications and conflict of interest in the evaluation of bids are widespread practices in the country.

Table 2 Percentage of respondents who perceive illegal practices in procurement to be widespread in Germany (2013)

Illegal practices	Germany	EU27 average	Rank
Specifications are tailor-made for particular companies	48%	57%	9
Conflict of Interests in the evaluation of bids	47%	54%	11
Collusive bidding	54%	51%	15
Unclear selection or evaluation criteria	43%	51%	9
Involvement of bidders in the design of specifications	52%	48%	20
Abuse of negotiated procedures	28%	47%	6
Abuse of emergency grounds to justify use of non-competitive or fast track procedures	42%	46%	14
Amendments of the contract terms after conclusion of the contract	44%	44%	19

Source: Flash Eurobarometer 374

Despite showing that the procurement might not be as risk-free as suggested by the evidence derived from the EU TED database in the previous section, business surveys such as the Eurobarometer used above are often criticised for their subjectivity and measurement errors: if respondents have not had a personal experience with corruption in the past, their answers will be purely “attitudinal” and their opinions will be mostly determined by individual factors such as their level of education, political beliefs, etc. In order to avoid this, it is desirable to combine perception data with more objective evidence. Luckily, the Courts of Auditors from Berlin, Saxony and Thuringia have conducted in depth procurement audits in the past three years. Evidence of systematic breaches of the procurement rules and procedures by the contracting authority or other type of misconducts in the awarding process could help validate the evidence provided by the perception indicators.

At first sight, the reports by the different state auditing courts reveal that there is a widespread lack of knowledge regarding the procurement rules, which often leads to breaches in the awarding of contracts. This evidence speaks directly against the notion that procurement rules in Germany are widely applied. In the case of Berlin, for example, the Court of Auditors found that contracting authorities often ignore the thresholds that call for open tenders and award contracts through restricted procedures. This was the case in more than 10% of the procedures checked (82 out of 788) (Rechnungshof von Berlin 2014: 114). There were also cases of contracts that due to their value would have had to be awarded competitively, but were divided into smaller ones to be awarded directly or through restricted procedures (Rechnungshof von Berlin 2014: 116). It was also determined that the process of selecting the appropriate awarding procedure or authorizing the providers was not properly documented 35% of the time (Rechnungshof von Berlin 2014: 117).

The 2012 audit for the state of Saxony, for example, revealed that although the municipalities in this state are obliged to publish the results of contracts granted awarded through restricted procedures and to inform about direct awards, 56% of the municipalities failed to do so either because they were not aware of this obligation or because of high workloads and lack of personnel (Sächsische Rechnungshof 2012: 15). The audit also determined that 40% of municipalities lack a directory of providers and therefore award contracts based on recommendations of independent professionals or of neighbouring municipalities (Sächsische Rechnungshof 2012: 14). Finally, the Court of Auditors of Thuringia also noted in 2014 that many municipalities are not familiar with the procurement regulations (Thüringer Rechnungshof 2014: 48): while the bigger municipalities are aware of the applicable legal framework and their responsibilities, the smaller ones often lack this knowledge. The figures speak for themselves: a fifth of the municipalities in the state are not familiar with the GWB and the majority of them do not know that there are specific regulations for the construction sector.

The irregularities found by the local Courts of Auditors should not be interpreted as cases or symptoms of corruption. Many of the findings listed above might be indeed linked to a lack of knowledge of the legal framework, shortage of personnel to carry out all the necessary tasks to document the procurement process, etc. However, they should be a source of concern as they provide a fertile ground for corruption and favouritism to sprout. It is hard to generalize based

only on auditing reports from three states. However, the fact that all of them find that contracting authorities are not familiar with the legal framework and fail to comply with their obligation to keep and publish the necessary information regarding the choice of procuring procedure, as well as the choice of provider confirm the notion that procurement underneath the EU thresholds happens under a high degree of opacity.

II. CORRUPTION AND FAVOURITISM RISK ASSESSMENT

For the purpose of this report, Mungiu-Pippidi's (2011) notion of corruption as an equilibrium between opportunities and constraints will be used as a framework to assess the degree of risk of corruption encountered in the German public procurement system. According to this author's theory, corruption is the result of the existence of power and material resources and the absence of legal and normative constraints. Different levels of resources and constraints therefore result in distinctive levels of corruption. The following section considers the findings of the previous parts and categorizes them in terms of opportunities and constraints in order to assess the potential risks for corruption and government favouritism within the German public procurement system. Since the analysis of the TED data for Germany did not reveal any red flags, the following section focuses mostly on the corruption risks that can be found in the award of public contracts at the national (i.e. below the EU) thresholds.

1. Corruption opportunities and constraints

Opportunities for corruption derive from two main sources: power discretion (how power is distributed among government structures and how competition for access to power takes place) and material resources (potential rents) (Mungiu-Pippidi 2011). Given that public procurement is a sector where the public and the private interests collide, it is particularly attractive for rent-seeking activities. This factor is exacerbated by the amount of money allocated through public procurement. As mentioned before, almost a third of the total German government spending is allocated through public procurement. The temptation to resort to illegal practices to secure government contracts can be high and this is proven by the fact that according to the BKA most of the bribes paid in Germany are indeed intended to secure public contracts or buy competitive advantages.

The section that describes the legal public procurement framework showed that Germany has a strong federal and de-centralized system in which most of the contracts are awarded through the local and state authorities. In many cases decentralization can be a tool to fight corruption, as it helps reduce power concentration in the decision-making process. In this case, however, the lack of legally binding procurement regulations that apply to all contracting entities across the country gives local and municipal authorities enough leeway to change the rules to favour certain providers. Even if the *Länder* or municipalities are not actively seeking to favour certain providers, fair and open competition can be threatened by the existence of multiple procurement regulations at the national level, as potential bidders will face additional costs to compete for tenders when they have to get acquainted with a different state or local legislation. The Court of Auditors of Saxony, for example, reported that in the year 2012, 60% of the public contracts

were awarded to contractors within the same or a neighbouring municipality, another 27% to contractors outside of the municipality, but in the same district and another 9% to bidders outside their district, but with a seat in Saxony. The same Court of Auditors also reveals that there is a rotation of providers in almost 87% of the municipalities (Sächsische Rechnungshof 2012: 13-14). Without more specific data, it is impossible to assess whether this rotation happens in a competitive manner or whether it responds to different criteria.

Other opportunities of corruption hiding behind Germany's fractioned and complex legal framework at the national level is the large room for discretion when choosing the means of tender publication or the procurement procedure itself: Many contracting authorities often favour local newspapers or bulletins over the centralized and more widely accessible government website bund.de (Institut für Mittelstandsforschung 2008) and the selection of procurement method –as pointed out by different local Courts of Auditors– are often biased towards restricted procedures.

Finally, the legal protection for bidders in Germany is weak, which makes it easier for contracting entities to abuse their power: the review system in Germany only applies to contracts above the EU thresholds. Below these thresholds, bidders are generally restricted to administrative complaints or civil claims for compensation against the awarding body. According to the German Chapter of Transparency International (2011), there is no reason not to grant bidders the same rights below and above the thresholds, as is the case in most other European countries.

On top of the increased opportunities for corruption that exist in the design and operation of the public procurement system for contracts below the EU thresholds in Germany, the constraints side of the equation also seem weak at the national level. Constraints on corruption can be either legal or normative. The former can be present in the form of specific anti-corruption legislation or oversight and control institutions. These constraints help alter the incentives to corrupt behaviour by making it more costly. The latter, on the other hand, are associated with the level of acceptance of corruption among the actors involved in a political system, especially in the case of civil society, the media and voters (Mungiu-Pippidi, 2010), who can act as anti-corruption watchdogs and increase the costs of corruption in terms of political capital and reputation.

The analysis of the legal framework revealed that there are not particularly strong constraints on corruption for contracts below the EU thresholds. The main problem is the complete lack of transparency in contract awarding at the national level. The EU encourages Member States to publish tenders underneath the EU thresholds in the TED database as a good practice. Germany, however, has the lowest publication rate across the EU. Between 2009 and 2013, the publication rate did not exceed 1.4% of GDP, while the regional average is consistently above 3%. This also places Germany far behind the leaders of the pack, i.e. Latvia, whose published tenders account for almost 9% of GDP, Estonia (8%) or Hungary (7.5%) (European Commission 2014b). Even the similar sized economies of Europe –France and the United Kingdom– publish three to five times more contracts than Germany. The current data collection and procurement information system might be the reason why Germany is not able to provide more information, but this has an obvious and significant negative impact on transparency and increases the risks

of corruption by obstructing bidders, media or civil society organizations to monitor procurement decisions.

The task of scrutinizing the awarding of public contracts seems to fall solely in the hands of the federal and state courts of auditors, which given the nature and the scope of their tasks are not able to conduct systematic, in-depth analysis of the procurement spending on a regular basis. As a result, misconducts or mistakes like the ones identified by the courts of auditors of Berlin, Saxony and Thuringia can only be detected after the contracts have already been awarded and, in many cases, after the goods have already been bought or the projects concluded. The lack of publicly accessible information and documentation supporting the choice of providers or of the procurement procedure also makes it difficult for contractors to assess the lawfulness of the procedure. For this reason, access to public procurement information needs to be improved, particularly for national contracts.

The central website of the public administration (www.bund.de) is the ideal platform to achieve this. However, e-procurement platforms in Germany are severely underutilised, as their usage is not mandatory. According to the 2013 OECD Government at a Glance Report, Germany – together with Greece and Spain– has the lowest level of electronic procurement in the OECD with only 7% of the tendering processes happening through online platforms and less than 20% of firms using the available electronic resources to access documents and specifications (OECD 2013). The use of the e-procurement could bring several advantages, by tackling several issues at the same time: it could enhance competition by ensuring that public tenders reach a maximum number of potential bidders while increasing the transparency of the awarding process by improving the traceability of procurement spending and of the decision-making processes. It is therefore important to promote the use of the heavily underused e-procurement platforms in the country. This could help document procurement procedures and improve the data-collection process, which is currently labour intensive.

III. CONCLUSIONS

Taking advantage of the available data, this report managed to gather some evidence on the potential corruption risks in German procurement sector. However, since the German procurement system is ruled by two different sets of legislations, one for contracts above the EU thresholds and one for contracts below, each of these two branches has different level of corruption risks associated to them. On one hand, the system in place for the award of contracts at a European level seems to work fine. The evidence gathered from the TED database reveals that most of the contracts in this category are awarded in a competitive manner. The use of restricted or non-competitive procurement procedures are the exception and open tenders remain the rule in infrastructure, as well as in the purchase of goods and services. The national system, however, is not as seamless as one would expect from a country usually regarded as corruption-free by all major corruption indices. Applying the notion of corruption as the equilibrium between opportunities and constraints (see Munigu-Pippidi 2014), the German procurement sector appears to be a particularly high-risk one for contracts below the EU

thresholds as opportunities for corruption are high and the existing constraints leave a lot to be desired.

Despite the lack of hard data that could help assess whether corruption risks are widespread in the national procurement system, this report gathered evidence from different sources to assess this. The results show that the current awarding process at the national level operates like a black box: once the bidders submit their proposals, the decision-making process is untraceable and bidders are left with incomplete information and without any legal protection to monitor the process. The lack of legally binding procurement regulations at the national level can be confusing for bidders and contracting entities. The current situation where public procurement is regulated by the state level and through internal administrative laws can damage competition as it imposes additional costs to bidders used to somewhat different procedures. The fact that the best practices contained in the VOB, VOL and VOF are not legally binding at the national level also increases the risks of corruption.

Reports by the local Courts of Auditors of Berlin, Saxony and Thuringia as well as the perceptions of the business community also suggest that there are favourable conditions for corrupt practices to sprout: There is a lack of knowledge of the applicable procurement rules among many contracting entities, which leads to the breach of procedures in many occasions. This situation combined with the lack of transparency in the awarding process of contracts below the EU thresholds might be fuelling the high perceptions of corruption in the procurement process. Unifying the legal framework at the national level, improving the legal protection of bidders, taking advantage of the already existing web portals for procurement and investing in the creation of a centralized database to allow the follow-up and monitoring of awarding procedures could greatly reduce the risks of corruption in the German public procurement system.

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ABSTRACT

This report aims to document and to investigate the extent and the determinants of government favouritism in EU funded infrastructure development. It uses a variety of qualitative and quantitative research methods. While predominantly relying on the analysis of contract-level quantitative data on Hungarian public procurement, it also provides a discussion of the institutional framework and particular cases based on document analysis and interviews.

It finds that public procurement of infrastructure from national or EU Funds is a hotspot for corruption in Hungary just like in the other countries investigated by ANTICORRP Work Package 8. However, corruption is not pervasive everywhere and even high-level political influence has its limits. While the economic environment has varied greatly, public procurement spending on infrastructure followed a political logic with elections, EU funding cycles, and political power games playing a crucial role. It has proven to be one key public resource up for grabs for corrupt elites. Controls of corruption in public procurement in general are weak: not only is effective transparency very limited and declining rapidly since 2010, but also institutional remedies are likely to be controlled by the current governing party.

As a result of extensive public resources available, weak controls, and a complex regulatory environment facilitating close cooperation between bidders and public bodies, corruption is widespread in infrastructure provision. Political connections, far from having a uniform impact, are effective in facilitating rent extraction only when organisational integrity is weak and both the bidders and contracting entities are politically controlled. In micro-cosmoses of high integrity, political connections are ineffective at best, but may even handicap companies.

ACCRONYMS

CPV	Common Procurement Vocabulary
CRI	Corruption Risk Index
FIDESZ	Alliance of Young Democrats (Fiatal Demokraták Szövetsége)
MSZP	Hungarian Socialist Party (Magyar Szocialista Párt)
PCI	Politically Connection Index
PP	Public Procurement
SRI	Supplier Risk Index

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I. INTRODUCTION

European Union Structural and Cohesion Funds (EU Funds) are designed to decrease regional imbalances especially in terms of per capita GDP. To this end, the EU devoted roughly a third of its budget in 2007-2013, or 347.4 billion EUR¹. Much of this redistribution (75.5 billion EUR²) is spent on transport and infrastructure development in the least developed member states and their regions as lack of sufficient physical infrastructure, predominantly transport infrastructure, is considered to be one of the main impediments to poorer regions catching up to the EU average.

Despite spending such vast amounts, growth effects of EU Funds are far from clear. Some authors suggest that quality of institutions and the resulting spending efficiency exercise a decisive impact on whether EU Funds are effective in reaching their main goal of lifting growth rates (Becker, Egger, & Ehrlich, 2012). This should come as no surprise, given the numerous corruption cases reported by the media all across the EU and inspected by audit bodies. Many of these suggest that misuse of funds is happening at a large scale without much regard to economic rationality or stated public goals. But without an assessment on corruption's impact on development in key areas such as infrastructure and fiscal deficits, we cannot understand how and why development works or fails.

Nevertheless, up until now there is a considerable lack of research looking into EU Funds spending on infrastructure from the perspective of misuse of funds, corruption, and government favouritism. Furthermore, what research there is predominantly uses macro aggregates which are prone to ecological fallacy and by definition cannot take into account the diversity of phenomena on the ground. The available micro-evidence on EU Funds from a governance perspective paint a dim picture (Dimulescu, Pop, & Doroftei, 2013; Fazekas, Chvalkovská, Skuhrovec, Tóth, & King, 2013).

In order to address the above scientific and policy questions, this report aims to *document and to investigate the presence, the magnitude and the determinants of government favouritism in EU funded infrastructure development*.

In order to keep such a broad goal tractable, it is broken down into three key research questions:

- How is government favouritism taking place in EU-funded public procurement in Hungarian infrastructure development? What is its magnitude and structure?
- What are the institutional controls of government favouritism in EU-funded public procurement in Hungarian infrastructure development?
- What are the resources of government favouritism in EU-funded public procurement in Hungarian infrastructure development?

EU funded infrastructure development takes place almost exclusively through public procurement as development projects are realised by contractors which, by law,

¹ European Commission, 2008. Regional Policy—Inforegio. See: http://ec.europa.eu/regional_policy/sources/docoffic/official/repor_en.htm

² European Commission, 2008. Regional Policy—Inforegio. See: http://ec.europa.eu/regional_policy/archive/funds/cf/index_en.htm

have to compete for contracts, hence the focus on public procurement. Approaching government favouritism as a balance between controls of and resources for corruption helps organise the empirical material by relying on widely used theories.

Due to the high volumes of data available, only a subset of public spending transactions is investigated. First, only publicly announced public procurement data is analysed which makes the study particularly geared towards high stakes and high risk corruption. Second, the period 2005-2012 is looked at as more recent data is not fully processed for analysis. This still provides ample variation in terms of government in power and broader economic conditions with change of government in 2010 and the onset of the financial crisis in 2008. Third, infrastructure development is equated with the construction sector as identified in the Common Procurement Vocabulary (CPV) with divisions 44 - construction structures and materials; auxiliary products to construction (excepts electric apparatus), 45 - construction work, and 71 - architectural, construction, engineering and inspection services. This means that construction sector in public procurement includes a range of services, commercial, as well as construction activities in a narrow sense.

The report is structured as follows: first, a brief theoretical background is spelled out predominantly focusing on concepts directly amenable to measurement. Second, the material stake and the power discretion in public procurement construction in general and in EU funded public procurement construction in particular are discussed. Third, institutional controls of government favouritism are enumerated both in terms of legal norms and actual practice. Fourth, various corruption risk measures are discussed in the domain of public procurement. Finally, preliminary conclusions are drawn.

II. Theory

Corruption in public procurement in general and in the construction sector in particular can have a profound effect on public finances, democratic accountability, and government quality. This is because it allows for 1) concentrating vast fortunes, 2) very quickly 3) in a few hands 4) and with little effective oversight. Public procurement of infrastructure typically involves a few large contracts worth millions of EUR each where even a tiny percentage of corrupt rent translates into fortunes. Such contracts can be awarded in a short time span and payments quickly authorised if the 'right' technical specifications are used. Contract performance is often done by one or only a handful of companies even for the biggest contracts allowing for effective control of rent extraction by corrupt networks. Public procurement of infrastructure typically concerns complex and in many ways unique products (e.g. a new highway) with little room for benchmarking and easily establishing overpricing and low quality. In addition, such investment decisions are down to key officials in governments and public administrations. Uniqueness and legally mandated discretion make oversight cumbersome and costly.

Due to high concentration of corrupt rents, negative effects of corruption in public procurement go beyond simple loss to the budget through higher prices. It also implies:

- misguided selection of investment projects: procuring products and services based on where rent extraction is most profitable rather than on which bring most public value,
- spending structure distortion: lack of spending on maintenance in order to increase the incidence of large investment projects most profitable for corrupt groups, and
- distorted political competition: as rent extraction is tied to controlling key government positions, rents earned are typically reinvested into political competition.

Government favouritism and public procurement corruption are two closely associated concepts. People naturally favour their own family, clan, race or ethnic group: treating the rest of the world fairly is a matter of both social learning and resources (Fukuyama, 2011). In only a handful of countries the principle of universal open access to public resources has been established firmly in practice; while in many more countries this norm has been legislated while practice deviates to a large degree (Mungiu-Pippidi, 2006; North, Wallis, & Weingast, 2009; Rothstein & Teorell, 2008). Still, in either case, impartial treatment of citizens and open access to public resources are expected to be the norm, in particular within the EU. This leaves us with a clear benchmark against which favouritism and corruption can be assessed.

Government favouritism in public procurement takes place as an exchange between multiple parties, the public side typically delivering lucrative contracts for private companies in return for monetary payments, counter-favours, or votes (Piga, 2011). The exchange does not necessarily imply individual benefits as it can be collective entities benefiting, for example, a company benefiting from procurement contracts donating to a political party foundation which finances election campaigns.

The above definition of government favouritism is identical to the definition of institutionalised grand corruption in public procurement as long as the powerful group in question is able to carry out corrupt transactions in a recurrent and stable manner (Fazekas, Tóth, & King, 2013).

III. Data

1. Public procurement data

The main database derives from Hungarian public procurement announcements from 2005-2012 (this database is referred to as PP henceforth). The data represent a complete database of all public procurement procedures conducted under Hungarian Public Procurement Law. PP contains variables appearing in 1) calls for tenders, 2) contract award notices, 3) contract modification notices, 4) contract completion announcements, and 5) administrative corrections notices. As not all of these kinds of announcements appear for each procedure, we only have the variables deriving from contract award notices consistently across every procedure.

These documents are published in the Public Procurement Bulletin which appears on a weekly basis and is accessible online³. As there is no readily available database,

³ See: <http://www.kozbeszerzes.hu/adatbazis/keres/hirdetmeny/> (in Hungarian)

we used a crawler algorithm to capture every announcement publicly available. Then, applying a complex automatic and manual text mining strategy, we created a structured database which contains variables with clear meaning and well-defined categories. As the original texts available online contain a range of errors, inconsistencies, and omissions, we applied several correction measures to arrive at a database sufficient quality for scientific research. For a full description of database development, see Fazekas & Tóth (2012a) and Csizmás, K., Fazekas, M. & Tóth, I. J. (2014) in Hungarian and in somewhat less detail Fazekas & Tóth (2012b) in English.

A major limitation of our database is that it only contains information on public procurement procedures under the Hungarian Public Procurement Law as there is no central depository of other contracts. The law defines the minimum estimated contract value for its application depending on the type of announcing body and the kind of products or services to be procured (for example, from 1 January 2012, classical issuers have to follow the national regulations if they procure services for more than 8 million HUF or 27 thousand EUR). By implication, PP is a biased sample of total Hungarian public procurement of the period, containing only the larger and more heavily regulated cases. This bias makes PP well suited for studying more costly and more high-stakes collusion where coverage is close to complete.

As contract award notices represent the most important part of a procedure's life-cycle and they are published for each procedure under the Hungarian Public Procurement Law, their statistics are shown to give an overview of the database.

Out of the 118,537 awarded contracts announced in the Hungarian Public Procurement Bulletin throughout 2005-2012 only 78,594 were analysed in most calculations due to five distinctive, but sometimes overlapping reasons (Table 1):⁴

1. Repetitions,
2. Corrections,
3. Unsuccessfulness,
4. Cancellations, and
5. Framework contracts.

First, Hungarian announcements above the EU threshold have to be published both at the Journal of the European Union (TED) and the Hungarian Public Procurement Bulletin. However, the announcements appearing in TED also appear according to a special format in the Hungarian Public Procurement Bulletin. This leads to a duplication of announcements with only slightly different information content. Second, those announcements which were later corrected by a full, repeated announcement were also excluded from our sample for most analyses.⁵ More work is needed on this

⁴ In fact, we should extend our data with one sample referring to centralised procurement whereby issuers do not procure on their own rather through a centralised body. Unfortunately, we do not yet have detailed data on who bought and how much from this central public procurement body. For the moment, we account for centralised procurement as one other issuer without knowing the details of the flows of goods and services between individual issuers and the central body. Data acquisition is in progress.

⁵ As many corrections do not appear completely anew, rather a specific correction is published which explains which parts of the original announcement were wrong and what the correct information is, we inputted the correct data to the corrected announcements. This introduces a slight bias to our sample as correct information appears to be available in our data earlier than it was in fact for the public. As this only concerns 128 contract

aspect as corrections are not referenced in a standardised fashion in many cases. Third, those announcements or parts of announcements which were contract award notices, but awarded no contract were also excluded. Unsuccessfulness or invalidity are explicitly marked in the announcements; however, as there was no winner named in a great number of announcements, it is unclear if these are actually invalid announcements or if data is simply missing. As crucial information is often missing, we did not exclude these notices. Fourth, cancellations refer to those announcements which were announced as valid and correct, but subsequently had to be withdrawn or modified due to court decisions or withdrawal of the winner. Finally, framework contracts are awarded in two stage whereby winning the contract at the first stage only implies the possibility of bidding for contracts within the framework leading to actual work and payments. Hence, contract awards referring to the first stage of framework contracts are excluded in order to avoid double counting contract values.

Table 6 Main statistics of the analysed data – contracts

	2005	2006	2007	2008	2009	2010	2011	2012	Total
Total number of contracts observed	5413	9455	6888	12696	21130	28630	17443	16882	118537
Total number of repeated contracts	0	0	0	3503	6932	5626	995	4786	21852
Total number of corrected contracts*	0	0	0	0	4	81	43	0	128
Total number of unsuccessful contracts	675	1134	507	1152	2137	3766	1766	1696	12833
Total number of cancelled contracts	7	123	101	986	1249	1597	353	183	4599
Total number of framework contracts	0	249	501	705	993	687	369	956	4460
Total number of non-repeated, correct, valid, non-cancelled, and non-framework contracts	4731	7952	5796	6812	10921	17927	14070	10385	78594
Combined value of non-repeated, correct, valid, non-cancelled, and non-framework contracts (million EUR) *	1128	3086	4365	4591	4611	3850	1836	1290	24756

2. Data on companies

Our data on firms comes from the so-called Amadeus database supplied by a commercial company data provider Bureau van Dijk⁶. The database consists of 463049 unique, non-repeated firms (each observation is one firm) identified by their tax ID. Apart from data on the firms' structure (legal status, size of company, etc.),

award announcements, we consider this to be of relatively minor importance (there are additional corrections for other types of announcements which we still need to take into account).

⁶ <https://amadeus.bvdinfo.com/version-20141118/home.serv?product=amadeusneo>

activity (primary line of business) or location, the dataset contains information on variables such as profit margin, number of employees, operating turnover and the likes between 2003 and 2011. In total, there are nine time-varying variables and each is supposed to have nine years of data, that is each firm (observation) is supposed to have 81 time-varying entries. However, unfortunately on average 57.8 entries are missing out of the 81 resulting in a 71.35% missing rate. Luckily, the missing rate of the operating turnover variable that we will need the most is slightly lower. Here the number of missing entries (out of the 9) on average is 5.2, meaning a 58.19% missing rate.

3. Data on political connections

In the analysis below, we use information on companies' political connections as political officeholders owning or managing firms which win in public procurement can serve as a proxy for government favouritism. In this context political connection simply refers to a dummy variable (0-1) that indicates whether a firm has or had either an owner or manager who is or was a politician.

In order to obtain the database on political connections we made the following steps: first, we obtained the full list of registered owners and managers of the companies winning in public procurement (we could identify at least one owner or winner for about 85% of winning companies). And we also obtained the full list of elected officials at the national and local levels as well as key appointed officeholders (Table 2).

Table2. List of institutions and positions of the political office holder database, 2010-2011

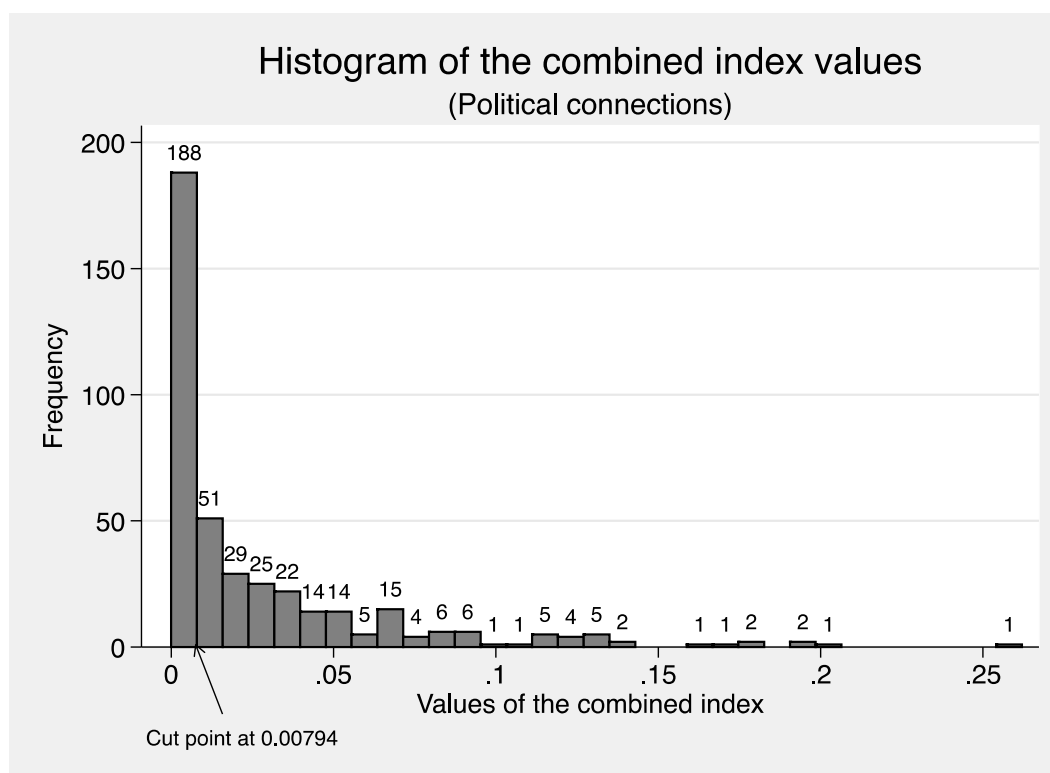
Institution	Position
Ministries	minister, secretary of state, vice-secretary of state, ministerial councilor,
Constitutional court	members and leaders
County courts	president, vice- president
Supreme court	President, vice-president, spokesperson
Prosecutors' Office	Chief prosecutor, vice-chief prosecutor, spokesperson
Municipalities	Major, vice-major, notary
County governments (new "kormányhivatal" too)	president, vice-president, notary
Regional police	Chief
National police headquarters	Chief, vice-chief, spokesperson
Minority governments	president, vice-president, head of office, head of secretary
National medical service	Chief doctor, chief pharmacist
National Healthcare Fund	Director, vice-director
Army headquarters	Marshal, Vice-marshal
Treasury	President, vice-president, head of finances
Tax Administration	President, vice-president, spokesperson
Office of the president	President of the state, heads of every bureau of the office
State Audit Office	President, vice-president, chief director, director of finances

Regional Development Councils	presidents, member of governing committee
Office of the parliament	Head of office, heads of offices
Ombudsmen offices	Ombudsmen, heads of offices
National headquarters of Prisons	National chief, national vice-chief,
Competition Authority	President, vice-president, head of secretary
Central statistical office	president, vice-president
Other regulatory agencies and background institutes	top-management (2-3 positions)

Note: The full list of institutions and positions can be obtained from the data provider; the government owned MTI Hungarian News Agency, which maintains a database of the most significant political office holders of the country for more than 20 years. For more information see: <http://mkk.mti.hu/>

Second, we matched the names (and other data) of politicians and firm owners and managers. The matching was done between more than 35000 owners/managers of winning firms and more than 10000 political officeholders based on full name. Third, to establish the identity of individuals and validate the matching, we collected further information and carried out further matching procedures. We checked the matched persons' birth date, mother's maiden name, and location of birth. For those names where we lacked data, we checked their photos available from reliable sources such as company websites and political parties' web pages. As there were names left whose matching could not be certainly established with these methods, we executed a statistical matching procedure based on the rarity of the names (calculated from the number of name occurrences from all the available names in the two initial databases) and the geographical distance between the firm and the political institution associated with the names. Then, we normalised the two indices (between 0 and 1) and combined them with simple multiplication, meaning that the final index measuring the goodness of match also ranged between 0 and 1 (0 meaning a most probable match, while 1 indicating the less probable one). A positive consequence of the multiplication in our case is that if one of the indices is 0 (i.e. the two institutions are located in the same settlement or the names occur only once in each database) and the other one is missing, we can still calculate the combined index. Once this combined similarity index was created, we determined a cut point above which name matching is determined only a coincidence rather than indicating truly identical persons. To determine the cut point, we chose a threshold for both normalized indices (name occurrence and settlement distance) separately. For the distance variable we selected 50 kilometres, since that is the longest distance that still classifies as commuting according to the Hungarian Central Statistical Office. (The normalized value of 50000 metres is 0.0794.) We determined the cut point value for the normalized name occurrence at 0.1 under which we can find those names which are highly idiosyncratic. Thus, if the combined index does not exceed $0.0794 \cdot 0.1 = 0.00794$, we declare that a political connection is present in the corresponding company (Figure 1).

Figure 1 Histogram of the combined index values of political connections



The company database used for validating name matching consists of 484 unique firms with judging finally only 273 firms as having reliable political connections. There are 23 companies that had a certain match based on the first two matching procedures, consequently 461 firms that had to be statistically matched in order to determine the existence of political connections. Table 3 summarizes our data on political connections for those 461 cases where statistical matching was necessary. Combined index is only available if either both components are available or if one is missing but the other one is equal to zero (since $0 \cdot missing = 0$). We can deduct from the table that at 88% of the cases the combined index is available and only 3% of these cases have one of the normalized indices missing. Table 4 summarizes the data availability for statistical matching: 41% of the data is below cut point out of all available data from layer 3 matching.

Table 3 Data availability for matching political connections based on the combined index

		Layer 3 type (statistical) matching			Layer 1 and 2 type matching	Total
		Only normalized distance data available	Only normalized name occurrence data available	Both indices available		
Combined index availability	Available	2*	10*	393	0	405
	Not Available	0	56	0	23	79
Total		2	66	393	23	484

**Where only one statistical matching data is available and the combined index is also available, the one available index is necessarily equal to zero.*

Table 4 Data availability for statistical matching

	Only normalized distance data available	Only normalized name occurrence data available	Both indices available	Total
Below cut point	2	10	176	188
Above cut point	0	56	217	273
Total	2	66	393	461

IV. MATERIAL STAKE

This section looks briefly at the resources available for corrupt rent extraction. Increasing the stakes up for grab is one principal means for corrupt groups to increase their wealth. The other major strategy is turning off controls, which is discussed below. These two major determinants of equilibrium corrupt rent extraction are simultaneously modified by corrupt groups, hence they shall be understood in light of each other. We first provide overview of the overall public procurement spending structure then we turn our attention towards the beneficiaries of public procurement contracts.

Total announced public procurement spending in Hungary relative to the GDP between 2005 and 2012 is reported in Figure 2. Average relative public procurement in all sectors was 3.6% of GDP throughout the observation period, however with considerable variability. Public procurement levels were negligible at the beginning of 2005 but started to increase rapidly during the second half of the first MSZP government. The growth reached its peak during the second MSZP government (8.2%) but slowed down notably during the period, maintaining a 5.1% average until the beginning of the Fidesz government. The Fidesz government – starting from the

second quarter of 2010 – cut back public procurement expenditure substantially by 2.2% points of GDP. These varying spending shares result from a wealth of factors among which a few are more dominant: GDP fell substantially in 2009 and it still hasn't reached its pre-crisis peak; total government spending contracted likewise, and an increasing portion of spending avoided transparency regulations and publication in the official public procurement journal.

Figure 2 Total procurement relative to GDP

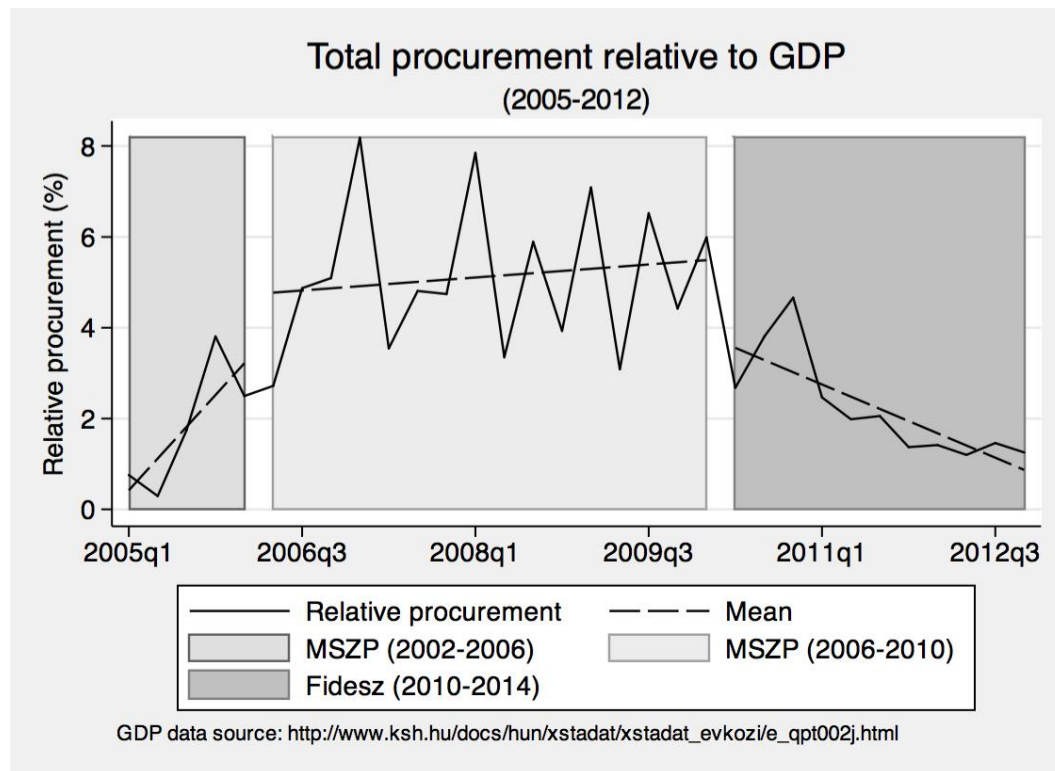


Figure 3 shifts the focus from total public procurement to public procurement construction projects in Hungary during the same seven-year spell. Both the patterns as well as the magnitude of public procurement are very similar to Figure 2 in terms of GDP which implies that construction public procurement tracks other sectors' public procurement.

Figure 3 Construction procurement relative to GDP and public expenditure

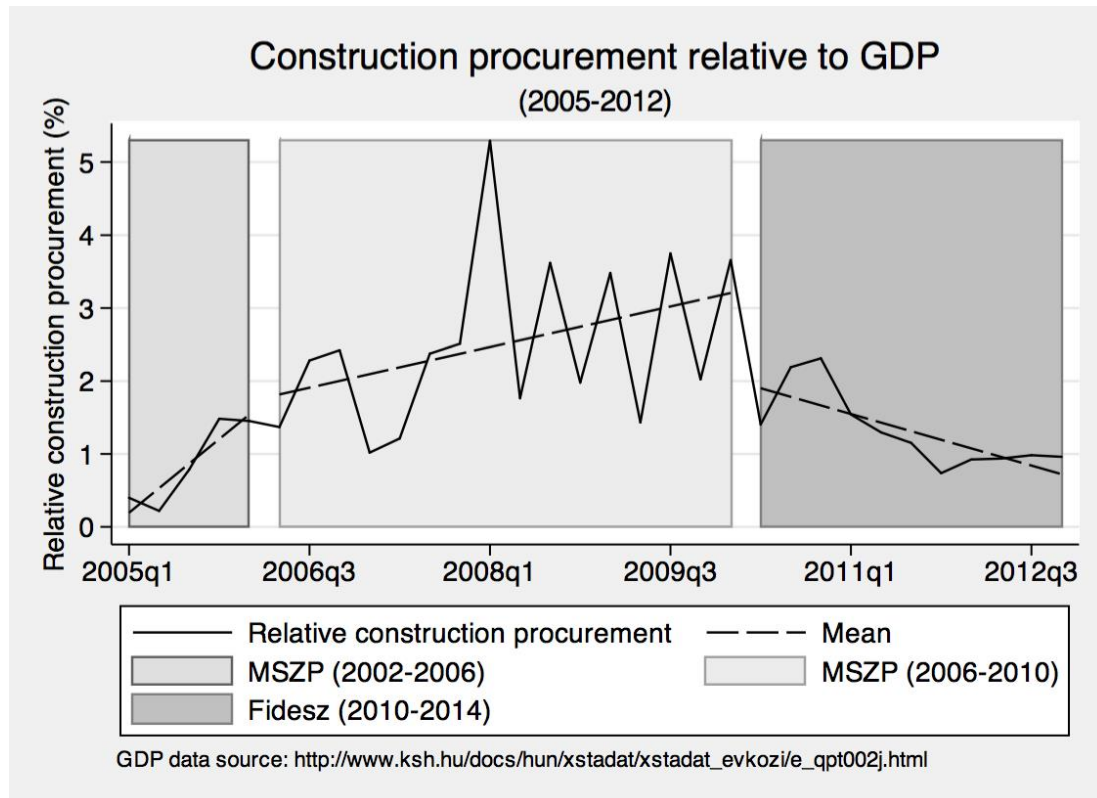


Figure 4 presents construction public procurement volumes relative to total public procurement volumes. The trend seems to be the opposite of what we have seen before: decreasing relative construction public procurement in the first MSZP government, reaching the minimum during the second one and growth during the Fidesz government. Combining this information with the previous Figures, one can conclude that these trends are due to the faster expenditure growth/decrease on public procurement of fields other than construction. On average construction amounted to more than half of the total public procurement (59.1%) with 15.7% standard deviation and a minimum of 7.9% during the second MSZP cycle and the maximum of a 100% during their first cycle, while public procurement in other fields than construction varied 18% over 2005-2012, meaning that procurement spending in construction was more stable than non-construction over time.

Table 5 shows the correlation between types of public procurement (total, construction sector and sectors other than construction) and GDP. We can see that of all the public procurement, aggregates of construction correlates most strongly positively with GDP, while sectors other than construction correlate with GDP negatively.

Table 5 Correlations of types of public procurement and GDP

	Total PP	Construction	Other than construction	GDP
Total	1			
Construction	0.8441	1		
Other than construction	0.8746	0.4783	1	
GDP	0.0386	0.1496	-0.0720	1

Figure 4 Share of construction procurement in total public procurement

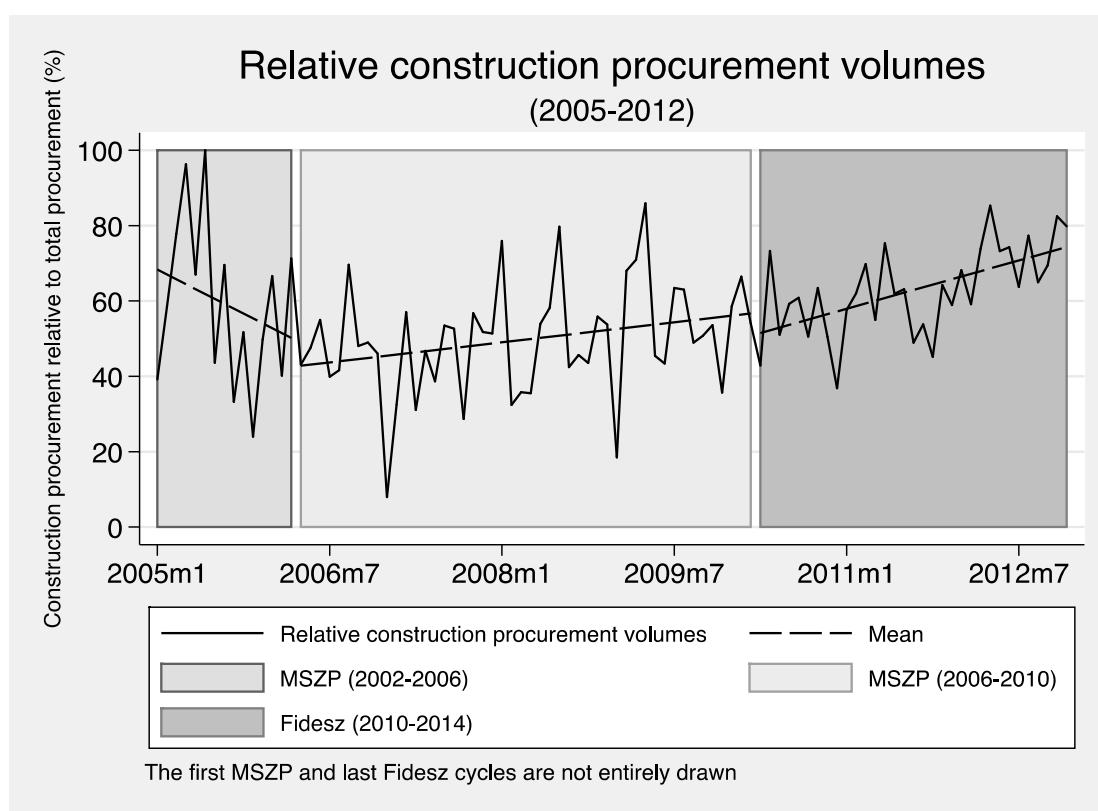
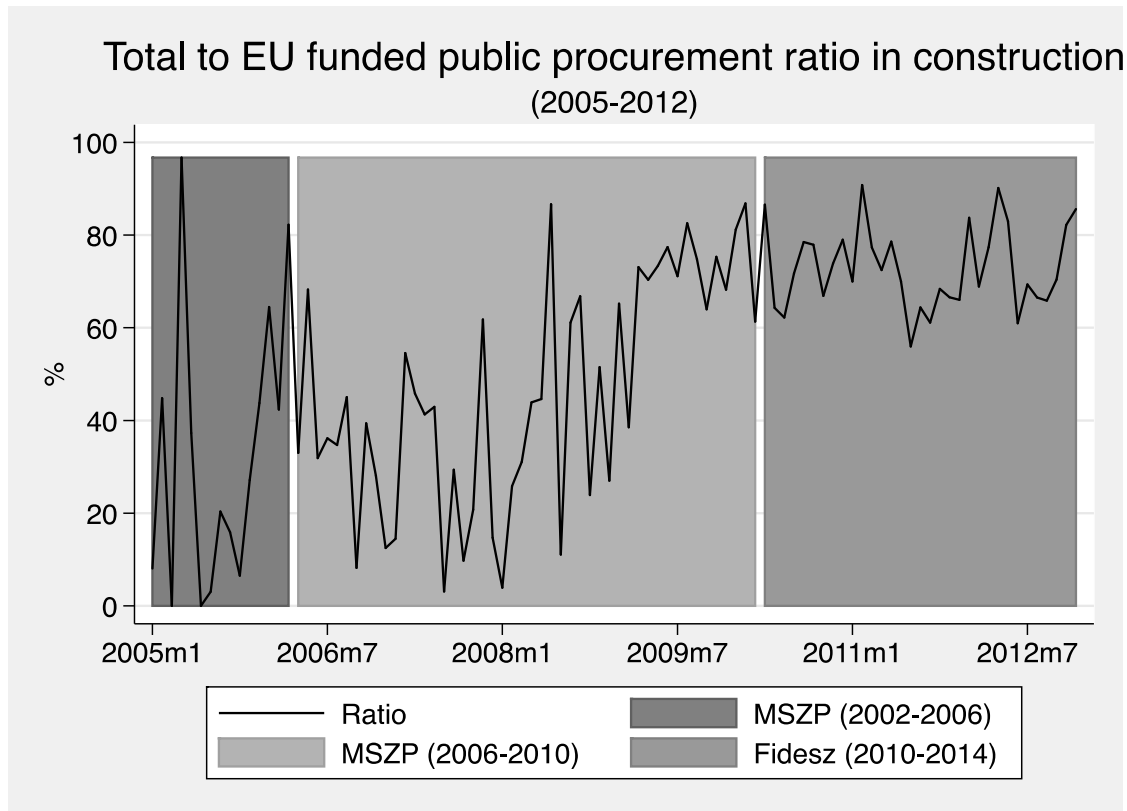


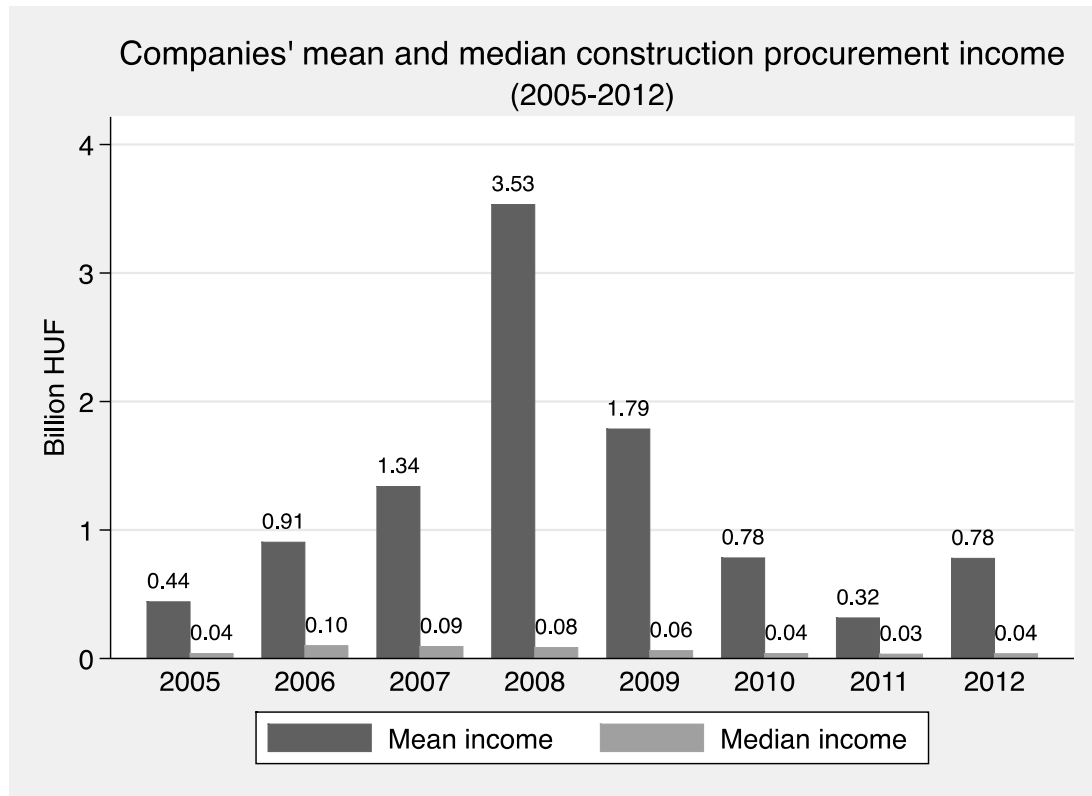
Figure 5 looks at the value of EU funded public procurement tenders in construction relative to the non-EU funded construction public procurement tenders in Hungary. The figure indicates that until the beginning of 2009, the share of EU funded public procurement in construction was much lower and more volatile compared to the following period with a mean of 35.0% and 73.18% and a standard deviation of 23.45% and 8.41% respectively.

Figure 5 Total vs. EU funded construction procurement volumes



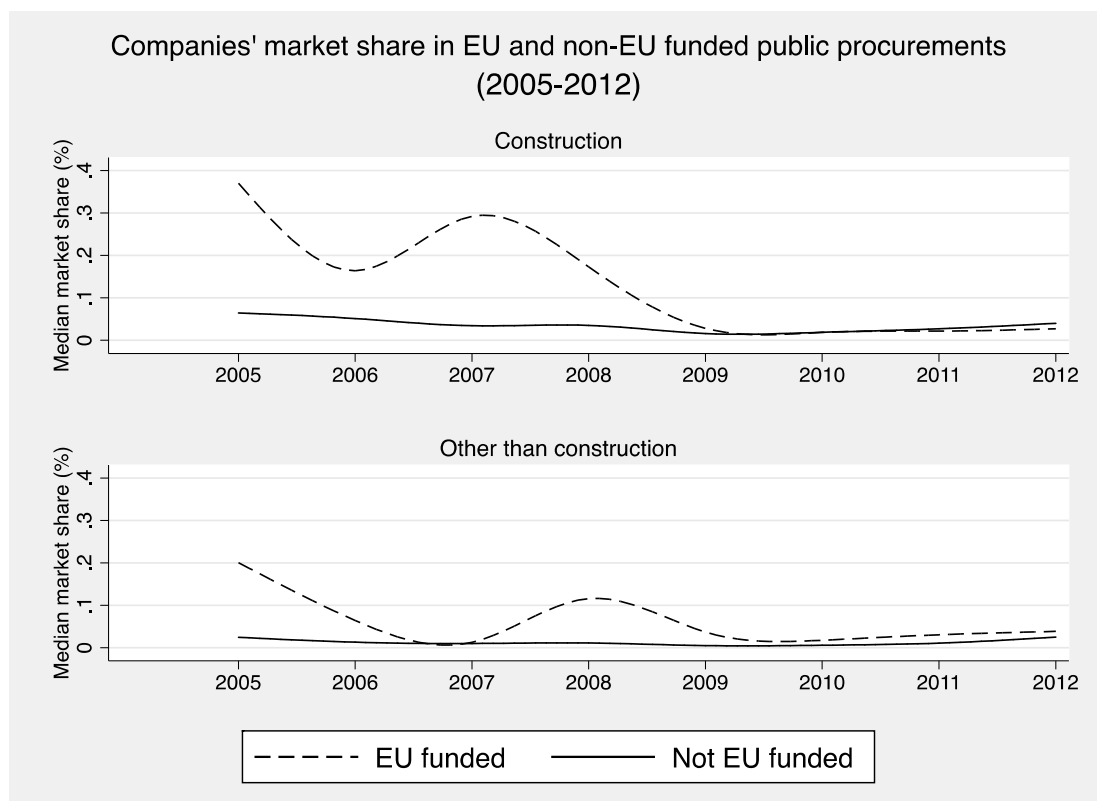
Turning to companies winning public procurement tenders, Figure 6 shows an initially increasing mean of public procurement income of companies in construction, that drops by half after 2008 and keep on decreasing almost until the very end. The initial discrepancy between the mean and median values, suggesting an uneven distribution of companies' public procurement incomes, closes somewhat after 2009. The drastic expansion of the typical procurement income of suppliers coincides with the expansion of overall spending on construction. Under competitive circumstances with low barriers to entry, a sustained and vast expansion of spending in a market increases market entry, hence lowering the average or typical procurement income per company. However, we observe a very different phenomenon in Hungary. Instead of more companies entering the market, it is the already active companies which deliver more public works. Hence, it is likely that there are effective entry barriers which could be technological, administrative or political, i.e., corruption-related. When looking at the effect of political connections and corruption on companies' procurement market success in section VI, we will explore this point in detail.

Figure 6 Mean and median construction procurement incomes



In Figure 7 one can investigate the market shares of winning companies in both the construction sector and in other sectors, where market share for each winning firm is calculated as the ratio between the company's total contract value won and the value of all tenders. The median values are below 0.5%, meaning that an average company wins less than 0.5% of the total public procurements disbursements from 2005 to 2012 if the procurement is EU funded and even less when they are non-EU funded. Despite the slight difference between the medians, the difference is significant (Two-sample Wilcoxon rank-sum test, $z = -5.053$, $p = 0.0000$), meaning that EU funded construction procurement market shares are more concentrated than the non-EU funded.

Figure 7 Companies' market share in EU and non-EU funded public procurement (2005-2012)



Because of the distribution of public procurement income to total turnover ratio is highly uneven (see Figure 8), we will use median instead of mean to characterize changes over time. Figure 9 shows a growing share of public procurement income in turnover of a median company over 2005 to 2011. While the share is only 6.9% in 2005, it exceeds one third of the turnover in 2009. The rapid hike in companies' dependence on public procurement and then its slight decline coincide with the rapid growth of public procurement spending after 2006 and the steep drop in spending after 2010. During the same period, total turnover of construction companies observed remained unchanged. This raises a range of hypotheses: first, throughout 2005-2010, EU funded expansion of public procurement spending may have given rise to clientelistic networks predominantly feeding on public money rather than private market competition; Second, these networks may have been capable of maintaining their incomes even in times of spending contraction using connections.

Figure 8 Histogram of procurement income to turnover ratio

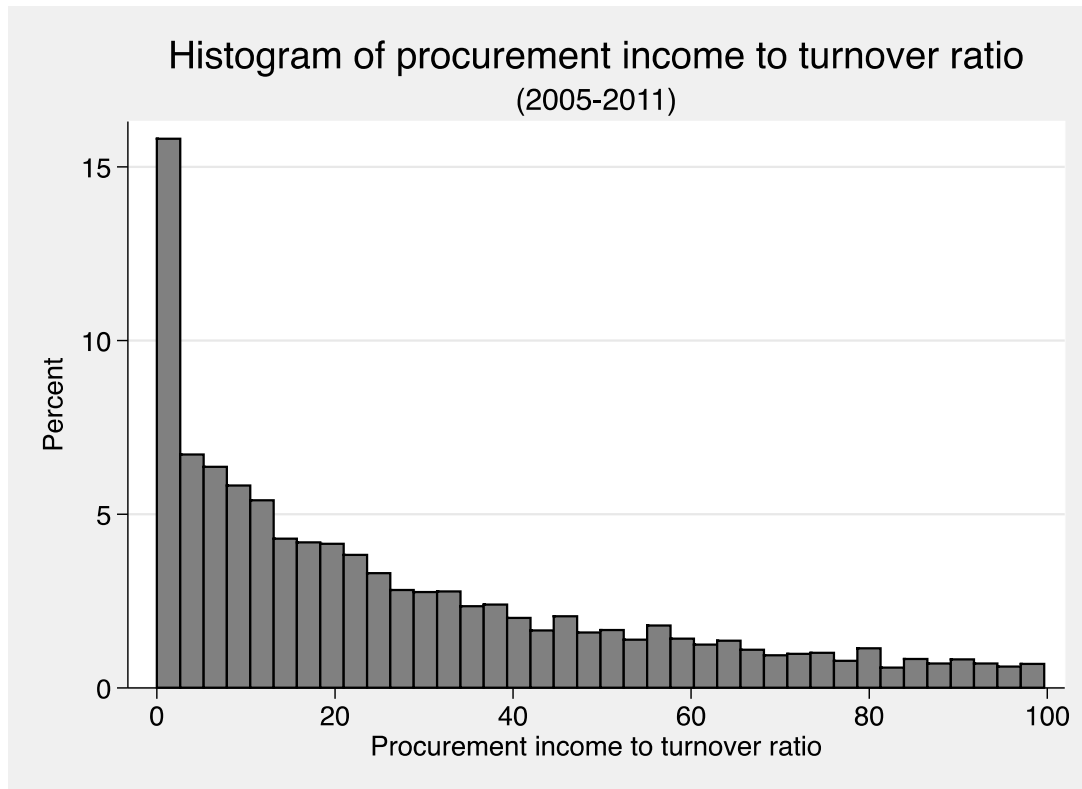
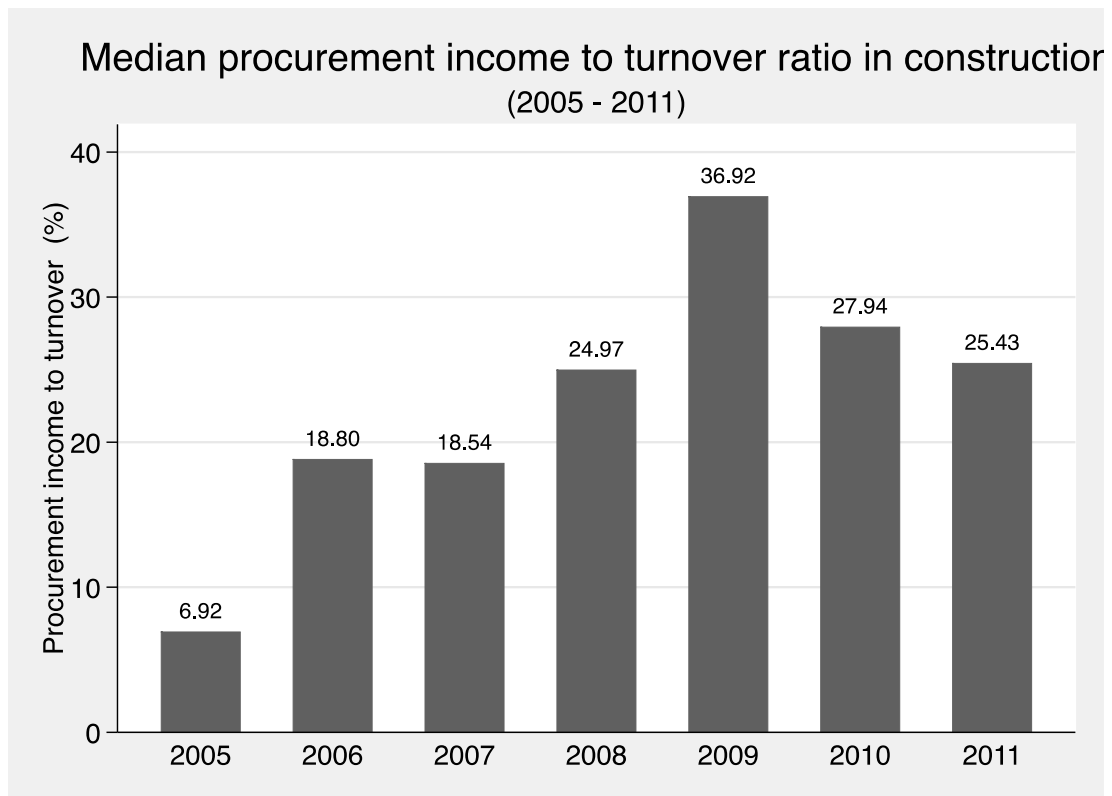
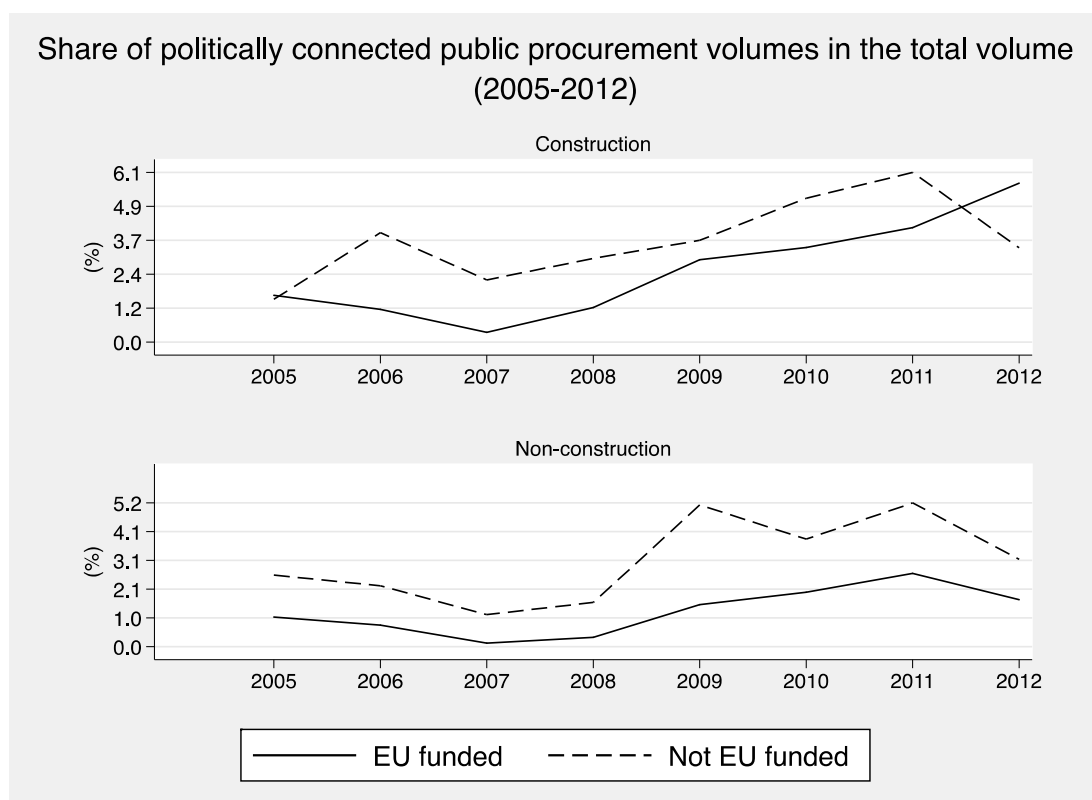


Figure 9 Median procurement income to turnover ratio in construction



The average public procurement tender volume in construction from 2005 to 2012 if a company had a political connection was 77.7 million HUF, while it was 104.6 million HUF if a company did not have a politically affiliated manager, director or owner. In sectors other than construction these numbers are 89.0 and 61.7 million HUF respectively. Figure 10 indicates the share of politically connected public procurement tender volumes compared to the total volume for every year during this spell. The average share in the construction sector for the whole timespan is 3.62 for non-EU funded public procurement compared with 2.57 for EU funded public procurement. The same numbers for sectors other than construction are 3.1 and 1.26 respectively. The ratios over the eight years show that in almost every year the share of politically connected tenders are higher when the tender is non-EU funded. Furthermore, the share of politically connected tenders are generally higher in the construction sector, however the average share of politically connected procurement volumes is higher in the non-EU funded non-construction sector category than in the EU funded construction sector.

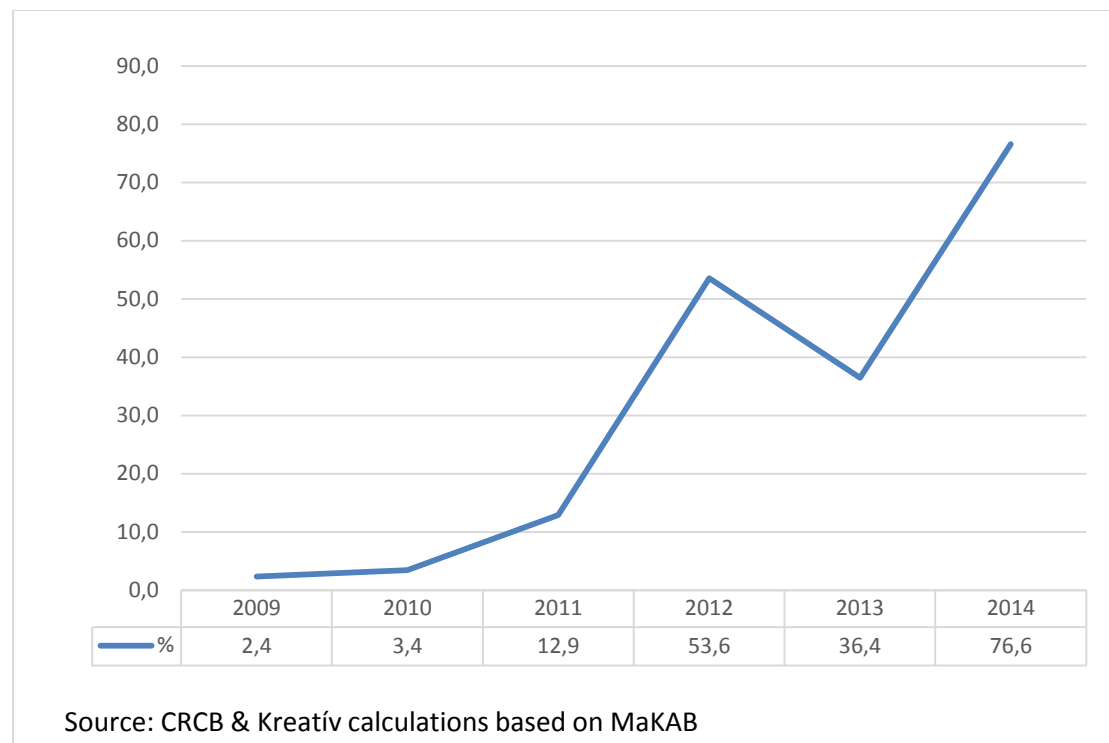
Figure 1017 Share of politically connected public procurement volumes in the total volume



The overall low amount of public procurement income controlled by politically connected firms is due to the restricted nature of identifying political connections: considering only direct links (politician owning or managing a company) and defining the identity of persons and the matching of different names in a conservative way. Detailed work focusing on one sector and unearthing the complex web of political connections can reveal a picture of much more substantial political inference into public procurement markets. For example, recent in-depth investigation of political connections in the communications services market revealed that the governing

party's business allies have steadily increased their market share to reach as high as 75% (Figure 11) (Bátorfy – Fazekas – Tóth, 2014).

Figure11. Share in total public procurement income of companies linked to Fidesz, 2009-2014, %, communications services, N=1005



V. CONTROLS: NATIONAL PUBLIC PROCUREMENT LEGISLATION AND PRACTICE

The Hungarian Public Procurement Law (2003. évi CXXIX törvény a közbeszerzésekről [in force before 2012] and 2011. évi CVIII Törvény a közbeszerzésekről [in force after 2012]) have remained in compliance with the Public Procurement Directive (Directive 2004/98/EC, OJ L 134, 30.4.2004, p. 114) by and large. As a crucial aspect of transparency and the scope of the data analysed above is the set of minimum thresholds for the applicability of the Hungarian Public Procurement Law (Table 6). Note that Hungarian thresholds are well below the Public Procurement Directive's thresholds.

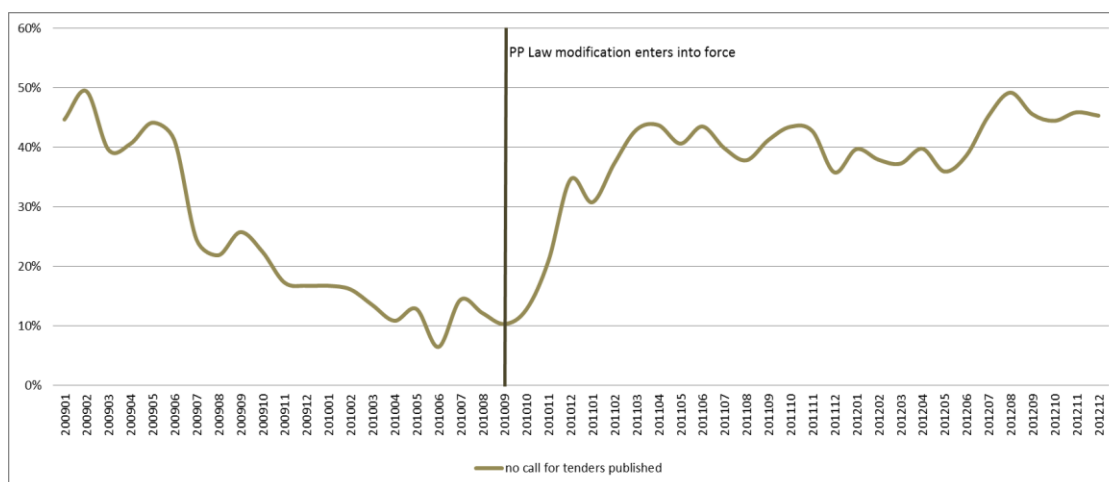
Table 6 Procurement thresholds, million HUF, national Public Procurement Regime

		2009	2010	2011	2012	2013	2014
General Issuers	Goods	8	8	8	8	8	8
	Public Works	15	15	15	15	15	15
	Public works concession	100	100	100	100	100	100
	Services	8	8	8	8	8	8
	Services concession	25	25	25	25	25	25
Utilities	Goods	50	50	50	50	50	50
	Construction	100	100	100	100	100	100
	Services	50	50	50	50	50	50

Underpinning its support for open spending, at least on the surface, the Hungarian government joined the Open Government Partnership in 2012 and concluded an action plan in February 2013 detailing its commitments as part of this partnership (Government of Hungary, 2013). While this action plan reinforces a number of anti-corruption measures already planned or ongoing, it also introduces new commitments bearing consequences to government decision making 1) improving the transparency and accessibility of budget data; 2) enhancing the quality and accessibility of public procurement data; and 3) further advances the public availability of information on the decisions and contracts regarding the use of public assets and funds. While the implementation of some of these actions is still pending, taken together, they represent a chance for significantly moving ahead.

In spite of these positive developments, the Hungarian government has also taken a range of steps towards decreasing transparency and open competition in public procurement both of which considerably contribute to corruption risks. Crucially, changes to the Public Procurement Law made less transparent procedure types more easily available to issuers of tenders (*2010. évi LXXXVIII. törvény a közbeszerzésekről szóló 2003. évi CXXIX. törvény módosításáról*, 2010) which drastically decreased the proportion of procedures with call for tenders published in the Hungarian Public Procurement Bulletin (Figure 12). In addition, the requirement, unique in Europe, to publish contract completion announcements which disclose the final contract value and completion data has been removed effective from 1st of January 2012.

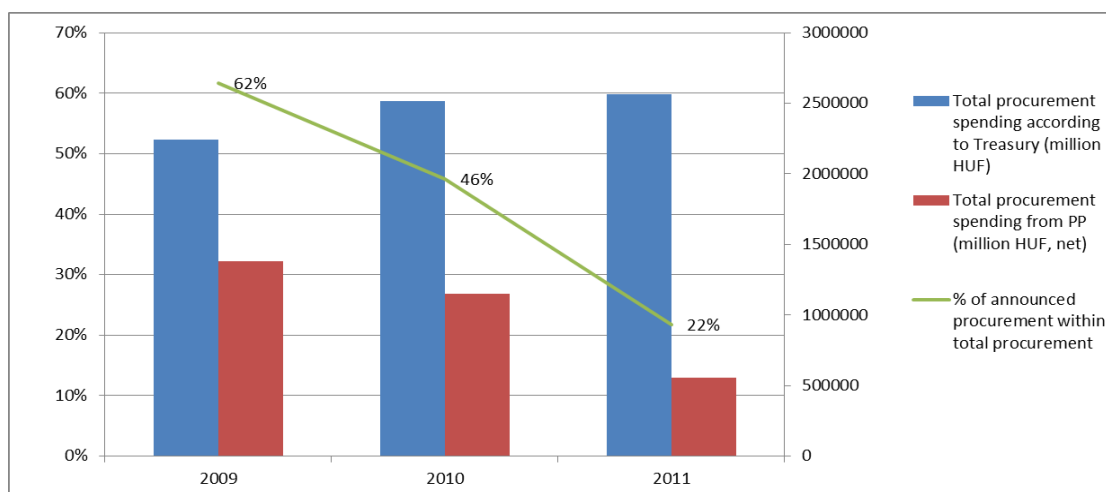
Figure12. Proportion of contracts awarded without a prior publication of a call for tenders in the Hungarian Public Procurement Bulletin, 2009-2012



Source: own calculations using data from Fazekas, Tóth, & King (2013a)

Moreover, the proportion of public procurement spending announced in the Hungarian Public Procurement Bulletin (which also publishes all the Hungarian announcements in the Official Journal of the European Union) within total procurement spending has also decreased since 2010 (Figure 13). Decreasing transparency in public procurement constitutes a considerable risk to integrity across OECD countries (OECD, 2009).

Figure 13. Public procurement spending announced in the Public Procurement Bulletin and total public procurement spending, 2009-2011



Source: (Fazekas, Tóth, & King, 2013b)

Notes: for details of calculating total procurement spending from Treasury annual budget accounts see: (Audet, 2002; European Commission, 2011). The ratio reported is only an estimation as spending as announced in PP refers to the total lifetime of the contract while Treasury accounts contain only the spending accrued in a given year. Further reason for imprecision of the ratio is that the set of institutions submitting accounts to the Treasury and those subject to the Public Procurement Law are somewhat different.

The obligations of contracting authorities – including the appointment of award boards and evaluation committees – are laid down in the Act CVIII of 2011 on Public Procurement. In the relevant sections (Article 22. (1)-(5)) the law states the following: (1) while preparing the contract award procedures, the contracting authorities must

specify all the members who will attend the procedure, meaning the person (or body) of the award board and the body of the evaluation committee as well. (2) The aforementioned members must possess adequate competence in the adequate field of the procurement, in public procurement in general, in law and in finance. (3) The contracting authority must set up an evaluation committee body of at least three competent members who will evaluate the tenders based on prescribed requirements and then provide an expert's opinion and a proposal of decision towards the award board. (4) Finally, the person who makes the ultimate decision (and cannot be part of the evaluating committee) chooses the applicant who shall fulfill the contract. There is very little to no information on the actual composition of award boards making the assessment of these regulations impossible. While a few scandals of apparent conflict of interest in the press serves as a biased guidance, it can be hypothesized that in line with public procurement corruption risks measured, award board compositions carry further risks.

A standard feature of public procurement laws across Europe is the options for applying exceptions on the grounds of national security grounds. While these exceptions are justified in a range of circumstances they carry the potential to decrease the transparency of public procurement spending. In Hungary, the Public Procurement law allows for cases of national security concern to the publication of a call for tenders and give account of how the contract is executed afterwards (9. § (1) a), 2011. évi CVIII. törvény a közbeszerzésekről). Until October 2013 this rule of exception was applied 126 times. (444.hu, 2014, compiled from the original documentation of the Parliamentary Committee on National Security) Between October 2013 and September 2014 there were additional 29 cases. 30.14 billion HUF (~98 million EUR) was spent on these 29 cases.

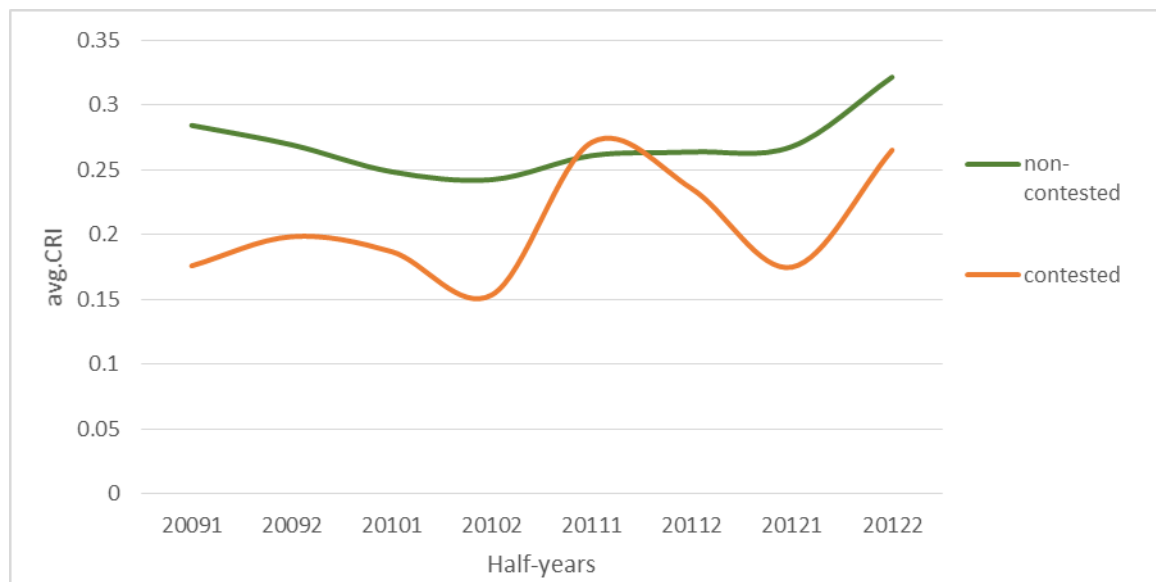
Next, we introduce some of the examples that show a pattern when issuers have seemingly abused this rule of exception.

- First, the Ministry of National Development in 2014 asked for 12 billion HUF (~39 million EUR) to maintain and develop the National Toll System. The reason to apply the law on the procurement tender was that the new system would probably connect to a police database.
- Next, still in 2014 the Prime Minister's Office was able to apply the rule to their procurement tender to *plan* the modifications of their new offices in the Buda Castle for 800 million HUF (~2.6 million EUR).
- Furthermore, the Hungarian Police concealed the details of their energy efficiency development procurement tender of their office building for the value of 4.23 billion HUF (13.76 million EUR).
- Also, the Parliament covered up the procurement procedure for the *planning* of the renovation of the *facade* of the Federation of Technical and Scientific Societies for 200 million HUF (~650000 EUR).
- Finally, the Directorate General of Public Procurements and Sustenance applied the rule in order to conceal the details of their public procurement of the cleaning services of public institutions, a value of 108.5 million HUF (~350500 EUR).

A key curb on corruption in public procurement is the courts, in particular the Public Procurement Arbitration Court which serves as a first instance court and it blocks contract signature by default until a decision is reached. This makes the Arbitration Court highly influential, but also an ideal target for capture. Interview evidence points at direct political pressure on Arbitration Courts at least in high value construction cases. Quite tellingly, the different regional Courts have not managed to agree on even a single synthesis decision making legal practice highly variable. Interviewees quoted exactly the same tendering practice judged as lawful by one Court while as unlawful by another.

One indication of insufficient controls by Arbitration Courts is how government turnover influences their supposedly impartial activities (Figure 14). For tracking signs of partiality, we use the Corruption Risk Index (CRI) which tracks the prevalence of red flags in the contracting process (for more details see below). On the one hand, during normal times - that is without government change - the Arbitration Court tends to deal with lower corruption risk cases meaning that the cases with many red flags are missed. On the other hand, for a few months after the May 2010 government change in the first half of 2011, the Arbitration Court has concentrated on high corruption risk cases which is a distinctly different approach from before or after. While this is no direct evidence of political pressure on courts as companies filing complaints exercise a sizable impact on the functioning of the Arbitration Court, it does underlie the possibility of politically driven judiciary in the field of public procurement.

Figure 1418. Average Corruption Risk Index (CRI) of tenders with and without Arbitration Court judgment, 2009-2012, N_{court}=1 386; N_{no-court}=51 858



Taken together, the above evidence demonstrates that Hungarian governments have followed highly variable paths since 2005. The technocratic MSzP government has seen a slight, but steady improvement in transparency of public procurement spending, while the Fidesz government radically decreased spending transparency in a number of key aspects from openness to competition to a reasonable use of security exceptions.

VI. DETECTING GOVERNMENT FAVOURITISM IN PUBLIC PROCUREMENT

Detecting government favouritism is notoriously difficult, especially in environments where corruption is the norm rather than the exception. In such environments, favouritism is not only hidden, but it is also able to use legal means to hide its true nature.

Reflecting the challenges of measurement and the diverse nature of favouritism in government contracting, three main approaches are employed, each of which looks at the same phenomenon from a different angle, using different indicators:

- Using the Corruption Risk Index (CRI) for assessing the prevalence and structure of red flags in the tendering process. CRI is used for tracking corruption risks over time as well as comparing corruption risks across sectors.
- Tracking political connections of tender-winning companies (PCI) and measuring the impact of such connections on the likelihood of winning tenders. Combining PCI with CRI within the same analytical framework validates each of the indicators as well as sheds some light on the corruption techniques used by powerful political elites.
- Identifying public procurement supplier risk indicators (SRI) and tracking the prevalence of such risks over time. Corruption risks present in company structure are suitable guides for understanding the technologies used for corrupt rent extraction by corrupt networks.

1. Tendering process related corruption risks

The Corruption Risk Index (CRI) captures the probability of government favouritism to occur in public procurement tendering using a range of elementary red flags (Fazekas, Tóth, & King, 2013). The list of red flags used in this composite indicator and their weights are reported in Table 7.

Table 7. Component weights of CRI reflecting variable and category impact on corruption outcomes, normed to have an overall sum of 1

variable	component weight
single received/valid bid	0.096
no call for tenders published in official journal	0.096
procedure type	
ref. cat.=open procedure	0.000
1=invitation procedure	0.048
2=negotiation procedure	0.072
3=other procedures	0.096
4=missing/erroneous procedure type	0.024
relative length of eligibility criteria	
ref. cat.=length<-2922.125	0.000
1= -2922.125<length<=520.7038	0.024

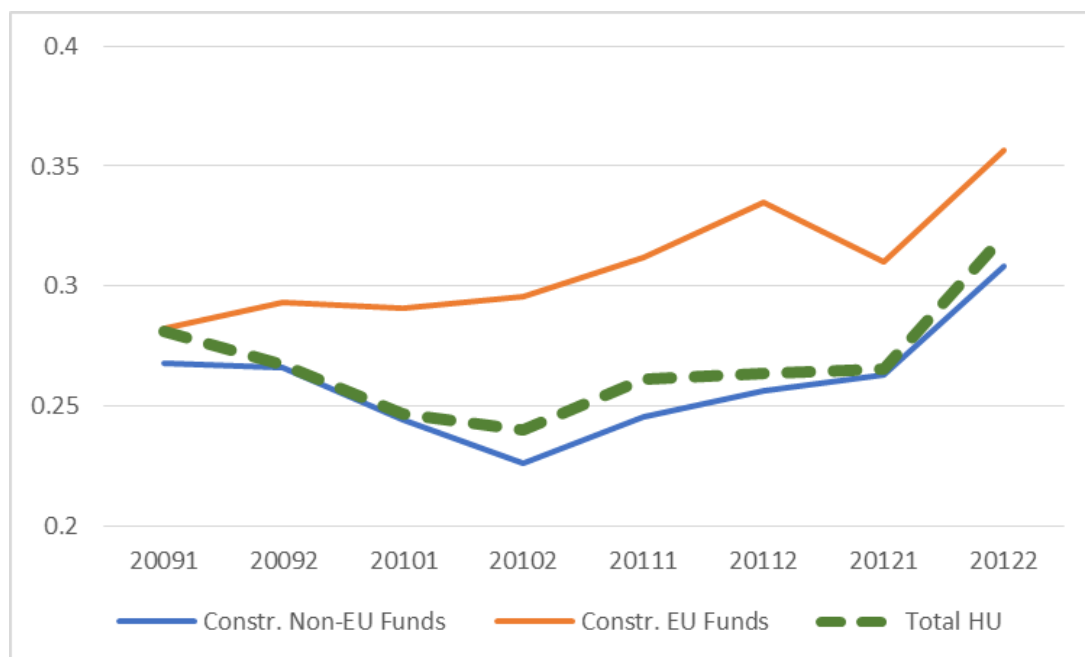
2= 520.7038<length<=2639.729	0.048
3= 2639.729<length	0.072
4= missing length	0.096
short submission period	
ref.cat.=normal submission period	0.000
1=accelerated submission period	0.048
2=exceptional submission period	0.072
3=except. submission per. abusing weekend	0.096
4=missing submission period	0.024
relative price of tender documentation	
ref.cat.= relative price=0	0.000
1= 0<relative price<=0.0004014	0.000
2= 0.0004014<relative price<=0.0009966	0.096
3= 0.0009966<relative price<=0.0021097	0.064
4= 0.0021097<relative price	0.032
5=missing relative price	0.000
call for tenders modification(only before 01/05/2010)	0.096
weight of non-price evaluation criteria	
ref.cat.= only price	0.000
2= 0<non-price criteria weight<=0.4	0.000
3= 0.4<non-price criteria weight<=0.556	0.048
4= 0.556<non-price criteria weight<1	0.096
5=only non-price criteria	0.000
procedure annulled and re-launched subsequently	0.096
length of decision period	
ref.cat.= 44<decision period<=182	0.000
1= decision period<=32	0.064
2= 32<decision period<=44	0.032
4= 182<decision period	0.096
5= missing decision period	0.000
contract modified during delivery	0.096
contract extension(length/value)	
ref.cat.= c.length diff.<=0 AND c.value diff.<=0.001	0.000
2= 0<c. length d.<=0.162 OR 0.001<c.value d.<=0.24	0.096
3= 0.162<c. length diff. OR 0.24<c.value diff.	0.000
4= missing (with contr. completion ann.)	0.048
5= missing (NO contr. completion ann.)	0.000
winner's market share	0.096

Source: PP

Note: If the call for tenders or contract fulfilment announcements are missing, the index is reweighted to only reflect the available variables (i.e. proportionately increasing the weight of observed variables).

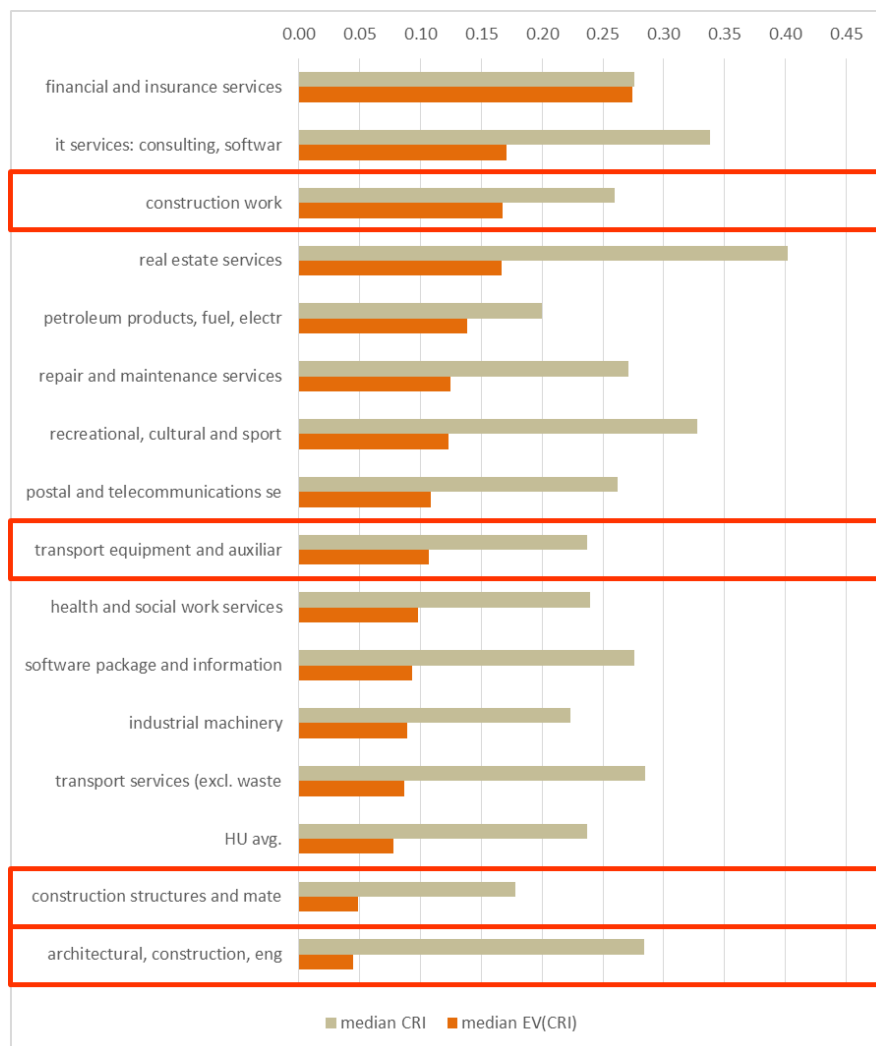
Tracking the trends of corruption risks in the construction sector allows us to understand the relative corruption performance of construction and EU Funding in the sector compared to the country as a whole and to various national governments. Figure 15 highlights that the CRI of construction closely tracked overall trends in CRI in Hungary with gradual improvements under the technocratic Bajnai government, then about half a year of transitory period, while since 2011 constant and occasionally dramatic deterioration of the corruption situation. Most notably, EU funded public procurement in the construction sector has always underperformed both non-EU funded construction the public procurement as a whole.

Figure 15. Average Corruption Risk Indices per half-year in Hungary, 2009-2012, EU Funded and non-EU Funded public procurement of construction



In order to understand corruption risks in construction and especially what their magnitudes mean, we can look at CRI in all the major sectors of public procurement in Hungary throughout 2009-2013 (Figure 16). It is immediately apparent that the construction sector itself is highly diverse in terms of construction risks with construction works displaying one of the highest average risks while construction structures and material, a very standardised market, is one of the lowest risks. In addition, the median CRI in the construction works sector is only towards the average of the country, while the median expected value of particularistic resource allocation (contract value*CRI) is among the top three highest corruption risk areas. This points at the fact that what makes construction really high corruption risk is that there are so many high value contracts awarded.

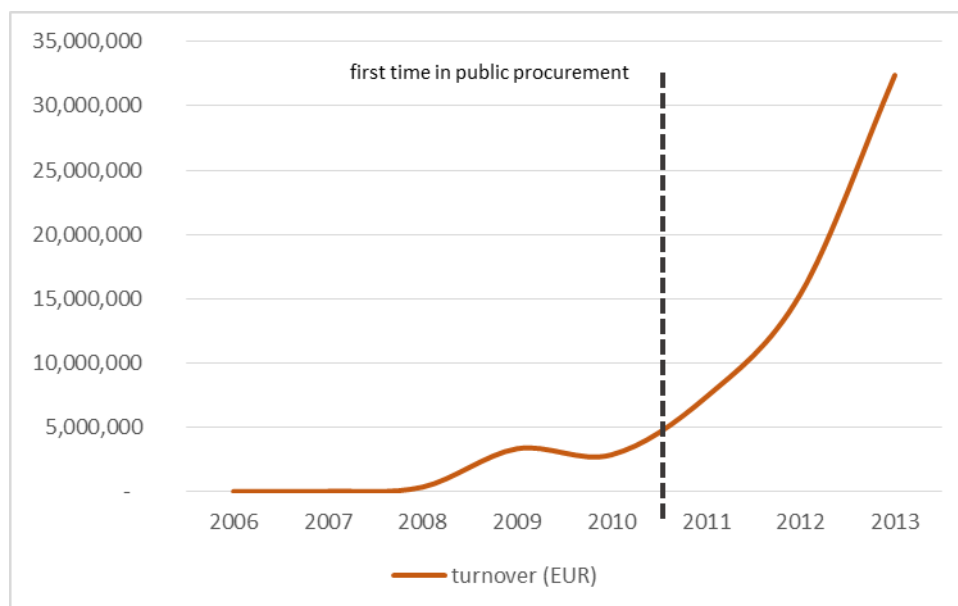
Figure16. Median CRI scores and median expected values of particularistic resource allocation (EV(CRI)), by main markets, 2009-2012, total public procurement, Hungary



2. Exploring the role of political connections in public procurement success

Anecdotal evidence of political connections leading to public procurement success and rapid wealth accumulation are plenty in the Hungarian media. One particular example is the mayor in the home village of Viktor Orbán, the prime minister since 2010. His construction company in operation since 2001, Mészáros és Mészáros Ltd., earned very little income until the change of government in 2010 with no public procurement contract whatsoever. However, since 2011 turnover and profitability have skyrocketed, coinciding with the first public procurement successes of the company and the change of government (Figure 17). While such successes of politically connected persons prove nothing on their own, they prompt the analysis below and the patterns to be identified with statistical analysis.

Figure 17. Annual turnover of Mászáros és Mászáros Ltd. 2006-2013, EUR



Source: <http://atlatszo.hu/2014/06/03/a-joisten-a-szerencse-es-orban-viktor-szemelye-igy-vagyonosodott-meszáros-lorinc/>

In order to formally assess the effect of political connections on company success in public procurement, we have run a set of logistic models explaining the winning of a tender. The results are in Table 9 and Table 10. In both tables the independent variable is a binary variable that is equal to one if a firm won the tender and to zero if a firm lost. The overall structure of the two tables is similar except that Table 8 does not consider the Corruption Risk Index (CRI) of the tender while Table 9 does. Regressions were run on the full sample including both the MSzP and Fidesz governments while differentiating between the construction sector and all other sectors. No separate analysis of governments is conducted as further work is needed to track key political officeholders' business assets in both periods to an acceptable quality.

The independent variables are as follows: Our key variable, political connection (as discussed before) is a binary variable that takes the value 1 in case a firm's director, owner or manager is also a politician and 0 if not. The coefficient of the political connection variable is positive throughout the whole set of models in Table 8, meaning that an average firm with political connections has a higher chance of winning a public procurement tender than an identical firm without political affiliation both in construction and sectors other than construction. For example, models (1) and (2) show that over 2008-2011 in the sectors other than construction, an average firm has 16% and 21% higher chance of winning a tender respectively, compared to an identical firm without political connection. Note that the impact of a firm's political connection on its chances of winning is higher in construction than in the other sectors.

The Corruption Risk Index measures tender-wise corruption risk in a continuous scale from 0 to 1. We decided to exclude CRI from the first set of models in Table 8, because we wanted to show that political connections have a sizeable effect already on their own. In the second set of models (Table 9) we run the same set of models for the whole period in the construction, but by three equal quartiles of CRI. The point

of splitting up the sample into three was to determine whether political connections have a uniform impact over winning chances or not. If the impact is not uniform, Hungarian public procurement is only partially captured by high-level political interests. In Table 9, to our surprise, the effect of political connections on company success strongly co-varies with the level of CRI in the tendering process (the share of politically connected winners is by and large the same across the three subsamples). In low CRI tenders, that is in high integrity public organizations, political connections have a negative, albeit insignificant impact on winning chances. While in high CRI tenders, that is in low integrity public organizations, political connections have an overwhelming impact: politically connected firms *are 65% more likely to win than their non-connected counterparts*. This is three times larger than observed on the whole sample. These findings imply that while political connections are pervasive across the whole public procurement sector in Hungary, they are able to corrupt the tendering procedure in selected cases.

Table 8 Logit marginal effect models (without Corruption Risk Index)

	For all years (2008-2011)	
	(1)	(2)
	Other	Construction
<i>Dependent variable: Winning the public procurement tender</i>		
Political connection	0.167 (1.89)	0.212* (2.06)
Same location	0.00732 (0.28)	0.340*** (12.16)
Nr. of applicants	-0.0349*** (-16.37)	-0.0566*** (-21.95)
Tender market share	-0.0259*** (-51.08)	-0.0604*** (-35.50)
Firm size		
Medium	0.210*** (6.34)	-0.169*** (-5.29)
Medium-large	0.0809* (2.02)	-0.285*** (-6.64)
Large	0.174** (3.03)	-0.720*** (-9.28)
Missing data	0.191*** (4.00)	-0.503*** (-7.83)
Constant	0.612*** (19.92)	0.464*** (15.29)
N	34072	32349
R ²	0.227	0.216

t statistics in parentheses, * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

Table 9 Logit marginal effect models by tertiers of Corruption Risk Index, all years (2008-2011), construction sector only

	(1) Low CRI	(2) Medium CRI	(3) High CRI
<i>Dependent variable: Winning the public procurement tender</i>			
Political connection	-0.127 (-0.59)	0.138 (-0.6)	0.647* (-2.51)
Same location	0.250*** (-3.8)	0.515*** (-7.57)	0.257*** (-3.58)
Nr. of applicants	-0.0449*** (-6.87)	-0.0781*** (-11.68)	-0.108*** (-12.69)
Tender market share	-0.0909 (-0.87)	-0.167 (-1.80)	-0.522*** (-6.68)
Firm size			
Medium	-0.0221 (-0.31)	-0.199** (-2.68)	-0.418*** (-5.24)
Medium-large	-0.256* (-2.33)	-0.0702 (-0.68)	-0.340*** (-3.31)
Large	-0.499* (-2.43)	-0.697*** (-3.50)	-0.481* (-2.45)
Constant	-0.0935 (-1.22)	0.493*** -6.7	1.511*** -19.29
<i>N</i>	4047	4059	4484
<i>R</i> ²	0.015	0.043	0.059

t statistics in parentheses * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

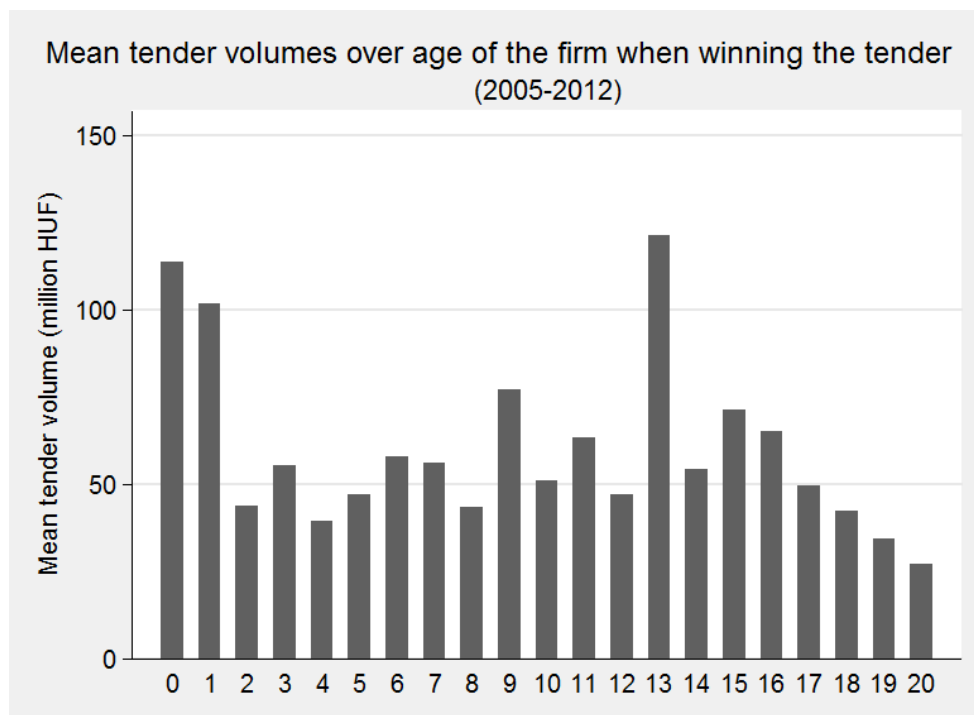
3. Supplier corruption risks

While no comprehensive discussion can be offered, a set of novel corruption risk indices can be demonstrated on Hungarian data which point at the possibility of a Supplier Risk Index (SRI) following a similar logic to CRI, but focusing on winning company characteristics.

A set of risks are associated with company age at the time of winning a tender; that is whether a company is particularly young when it wins a procurement contract or whether the company was founded at a particular time which makes it likely linked to a new government.

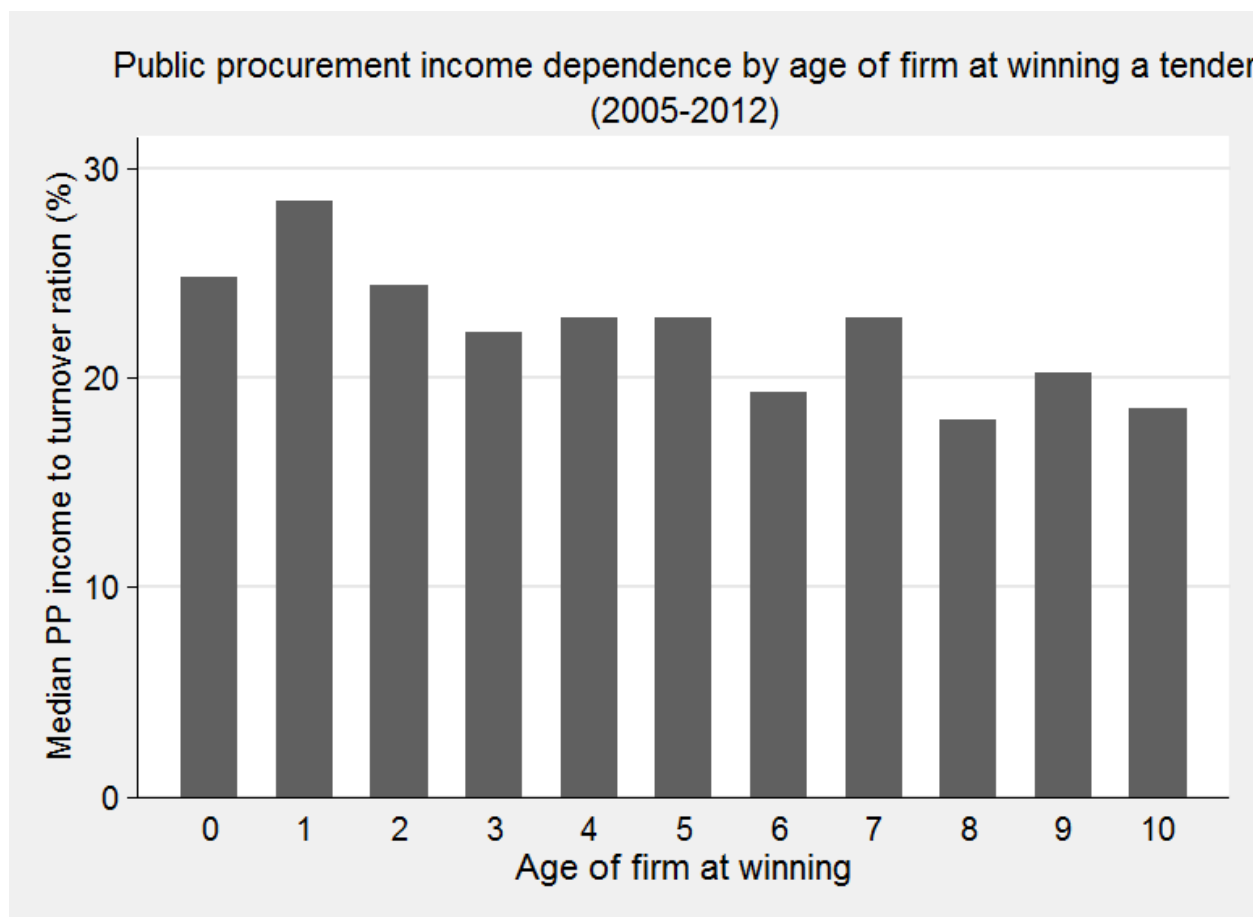
Some companies win more contracts than others which is normal in any well-functioning market with older, more experienced, and larger companies typically winning more. However, what we see in Hungary is a pattern distinctively different from this general expectation (Figure 18). First, particularly young companies (existing for 1 or less years) have very high average contract volumes; that is they win a lot more than most other companies. This is surprising predominantly because for fresh companies the administrative burden and the bureaucratic complexities of public procurement are expected to be prohibitive. However, the alternative explanation is that some of these firms have been specifically founded for extracting corrupt rents. Second, one other typical age stands out: 13 years which are quite surprising in a purely economic context. Nevertheless, in a political interpretive frame, they make a lot of sense: 13 years have passed between the first and second Fidesz government entering office (first Fidesz government entering office in 1998; second Fidesz government entering office in 2010).

Figure18. Mean tender volumes over the age of firm at the time of winning, 2005-2012



What makes very young companies have a considerably higher corruption risk is that their dependence on public procurement income is higher implying that they have less alternative income sources to resist corruption if they chose to do so (Figure 19).

Figure 19. Ratio of public procurement income to total annual turnover, 2005-2012



VII. CONCLUSIONS

Public procurement of infrastructure from national or EU Funds is a hotspot for corruption in Hungary just like in the other countries investigated by ANTICORRP Work Package 8. However, corruption is not pervasive in every corner and even high-level political influence has its limits.

While no comprehensive review of public procurement of infrastructure could be offered here, a few selected and intimately intertwined conclusions have emerged:

- Access to public procurement markets, especially EU Funded contracts, is difficult due to administrative as well as political reasons. It is a business limited to a trusted few either due to corruption or capacity to compete.

- While the economic environment has greatly varied, public procurement spending on infrastructure followed a political logic with elections, EU funding cycles, and political power games playing a crucial role.
- Controls of corruption in public procurement in general are weak: not only is effective transparency very limited and declining rapidly since 2010, but also institutional remedies are likely to be controlled by the current governing party.
- As a result of extensive public resources available, weak controls, and a complex regulatory environment facilitating close cooperation between bidders and public bodies, corruption is widespread in infrastructure provision. However, it affects larger contracts much more than smaller contracts making the sector only moderately corrupt in terms of share of corrupt transactions, and highly corrupt in terms of share of corrupt spending.
- Beyond the sheer amount of corruption, the structure of rent extraction, favouritism, and political pressure on spending organisations points at a dynamic landscape. Political connections, far from having a uniform impact, are effective in facilitating rent extraction only when organisational integrity is weak and both the bidders and contracting entities are politically controlled. In micro-cosmoses of high integrity, political connections are ineffective at best, but may even handicap companies.

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ABSTRACT

Improving infrastructure in Romania has been a significant project in the past 25 years. Unfortunately, although large amounts of public funds were spent in the construction sector from 2007 to 2013 (an average of 6.6% of GDP), the physical results in terms of project quality and completion do not match this investment. One of the explanations for this is that public contracts were awarded to companies based on corrupted practices or political connections, the focus being on redistributing public money and not achieving high quality construction works.

The present research points to the fact that statistical data analysis can be used in detecting corruption. The practice of single bidding and the tendency to establish political connections exist in the entire public procurement market. Nonetheless, non-EU funded contracts present a higher corruption risk. Only 1 out of 7 contracts receiving European funding were awarded to a single bidder, as opposed to 1 out of 4 contracts financed by the state budget. Still, 1 out of every 3 contracts won by a politically connected firm involved European funding. Data analysis also concluded that the number of contracts awarded per company can be explained by single bidding and the existence of a political connection in 44% of the cases. The agency-capture analysis revealed that favouritism in public procurement occurs especially at the local level and in state-owned companies. Most of the companies that “captured” contracting authorities are politically connected firms.

At the same time, the case studies give an account of how firms’ owners go to great lengths to consolidate a network of relationships with high ranking officials so as to keep their doors open and contact political elites, but also various state institutions whose activity can favour or disrupt their companies’ economic well-being.

ACCRONYMS

AADR	Agency for Romania's Digital Agenda
ANI	National Integrity Agency
ANRMAP	The National Authority for the Regulation and Monitoring of Public Procurement
CPV	Common Procurement Vocabulary
CVM	Cooperation and Verification Mechanism
CNADNR	Romanian National Company of Motorways and National Roads
DNA	National Anticorruption Directorate
EC	European Commission
EU	European Union
FOIA	Freedom of Information Act
GCI	Global Competitiveness Index
GDP	Gross Domestic Product
GEO	Government Emergency Ordinance
IMF	International Monetary Fund
IPP	Institute for Public Policy
MDRAP	Ministry of Regional Development and Public Administration
MT	Ministry of Transport
SEAP	Electronic Public Procurement System
PP	Public Procurement
PPP	Public-Private Partnership
PSD	Social Democratic Party
SAR	Romanian Academic Society

VAT

Value Added Tax

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Figure 16. Agency captures by type of contracting authority

I. INTRODUCTION

Investigative journalists and Romanian public opinion have always claimed that public funds for infrastructure are granted only to favourite companies and squandered. Romania managed during its 25 years transition to build only 695 km of highways (Ministry of Transport, 2015). Also, the absorption rate of Community funds in the transportation sector was among the lowest in the first full EU budgetary cycle since Romania's accession compared to other categories of structural and cohesion funds¹, and by 2015, after eight years of membership, Romania still struggles to determine which projects should become a priority.

If effectiveness in building public infrastructure has not improved after Romania's accession, the effectiveness of anti-corruption seems to have grown. The media counted in March 2015 that in the last two years alone, no less than five market leaders in the public construction sector have ended up in jail (Nelu Iordache, Dan Beşciu, Theodor Berna, Alexandru Horpos, Vlad Vameşu), and criminal investigations were initiated vis-à-vis others, after a long period of apparent impunity (Ziarul Financiar, 2015).

As part of Romania's EU accession process, dedicated anti-corruption agencies were created, such as the National Integrity Agency (ANI) aiming at enforcing conflict of interest legislation and the National Anti-corruption Directorate (DNA), a special criminal prosecution agency. The 2001 Freedom of Information Act (FOIA, Law 544/2001) has been effectively implemented and new measures to increase public procurement transparency were introduced. Moreover, building upon an auction system named eMarket in use from 2002 to 2006, an Electronic Public Procurement System (SEAP) was introduced in 2007.

However, these measures came under threat in the first years of EU membership since there was a pushback against the wave of reforms. There were attempts to curtail the powers of the two anti-corruption agencies, public administration was again severely politicized and, instead of decreasing, the clientelistic distribution of public funds grew steadily (Mungiu-Pippidi, 2008). The DNA's activity in the past three years disclosed details of high corruption cases in which the Romanian state lost hundreds of millions of Euro. It showed that the public procurement (PP) sector is the main medium through which public officials, once elected, redistribute funds to their political clientele and fund their political parties (Piga, 2011). However, systematic evidence is missing and the increasing number of arrests show that while anti-corruption is more effective,

¹ In the 2007-2013 budgetary cycle, the Transport Operational Programme had the highest financial allocation (4,42 billion Euro) among all the programmes under the structural and cohesion funds category, but, at the end of 2013, it had the second lowest absorption rate (19%) behind the Operational Programme for Increasing Economic Competitiveness (14%). In addition, at the end of 2012, only these two programmes suffered from a de-commitment procedure and the largest sum (138 million Euros) was subtracted from the Transport Programme, thus decreasing the overall financial allocation available. This programme also comes in second (57 million Euros) when referring to debt claims and financial corrections incurred from 2008 to 2013 and which affect the EU financial allocation for the transport sector (Dimulescu, Pop, 2014).

its deterrent effect is not yet felt. Many public contracts continue to be awarded to party donors² through uncompetitive procedures such as the so-called negotiation without prior publication of a participation notice, leading to single bidding (Simina, 2014). Also, most of the Romanian billionaires in the Forbes magazine's top 100 businessmen earned their fortunes from public rents rather than innovation or superior competitiveness (Ancutescu, 2014).

According to the Global Competitiveness survey, businesspeople perceive Romania as one of the worst countries when government favouritism and wastefulness of government spending are concerned. Transparency in policymaking has been decreasing a few years in a row. The other indicators show practically no evolution over the years, from an already poor (**Table 1**). Despite the change in the number of countries evaluated in the World Economic Forum's Global Competitiveness Index (ranging from 120 to 148, depending on the year), in the *2nd pillar: Infrastructure*, Romania has never ranked better than the 84th place, a position held back in 2006-2007 when only 120 countries were being evaluated. At the moment, out of 144 countries, Romania ranks in the 85th position in the same pillar. The prosecutors' findings in cases pertaining to public procurement crimes support the results of the abovementioned perception-based survey.

Table 1. Global Competitiveness Index - 1st pillar. Country Ranking (1-148 countries)

Series	2014-2015	2013-2014	2012-2013	2011-2012	2010-2011	2009-2010	2008-2009	2007-2008	2006-2007
1st pillar: Institutions	88	114	116	99	81	84	89	94	88
1.03 Diversion of public funds	82	114	115	96	84	75	80	86	88
1.07 Favouritism in decisions of government officials	114	137	128	115	123	117	113	116	103
1.08 Wastefulness of government spending	116	134	114	107	110	112	111	116	101
1.12 Transparency of government policymaking	86	115	136	140	137	128	124	126	118
2nd pillar: Infrastructure	85	100	97	95	92	110	105	100	84

Source: *The World Economic Forum*

The construction sector is especially important since public spending in this particular domain accounts for 58% of total public procurement. An equally important note is that the 2014 Cooperation and Verification Mechanism (CVM) report of the European Commission (EC COM (2014) 37 final) pointed out that Romania has made improvements over the years in fighting corruption, but that the PP sector is particularly vulnerable to such risks, especially at the local level where administrative capacity is weak. Thus, the opportunities for corrupt practices, such

² Previous studies analyzing party financing with a focus on Romania have emphasized cases of political campaign donors being rewarded after the elections with public contracts (Gherghina & Chiru, 2012; Volintiru & Gherghina, 2014). In the present report the issue of party donations which take on a form of pre-electoral bribes and kickbacks is examined in greater detail and using micro-level public procurement contract data from the construction sector from 2007 to 2013.

as awarding contracts based on government favouritism are high, especially in the construction sector.

The perception of businesspeople, journalists and ordinary citizens interviewed by the Eurobarometer coincides with the assessment of high risks of corruption. This report tests this perception by statistical means in the area of public infrastructure (construction sector), which is allegedly the most prone to corruption. The report uses Romanian public procurement data from 2007 to 2013 and it reviews national procurement patterns in procurement legislation and practice. Detecting corruption risk in public procurement is achieved through descriptive and inferential data analysis, noting the differences between EU funded public procurement and nationally funded public procurement. To trace the particularistic links which may influence public resources allocation (Mungiu-Pippidi, 2014) we use both quantitative and qualitative methods (two case studies). Finally, we list some options on how to tackle access to public procurement information and help limit corruption.

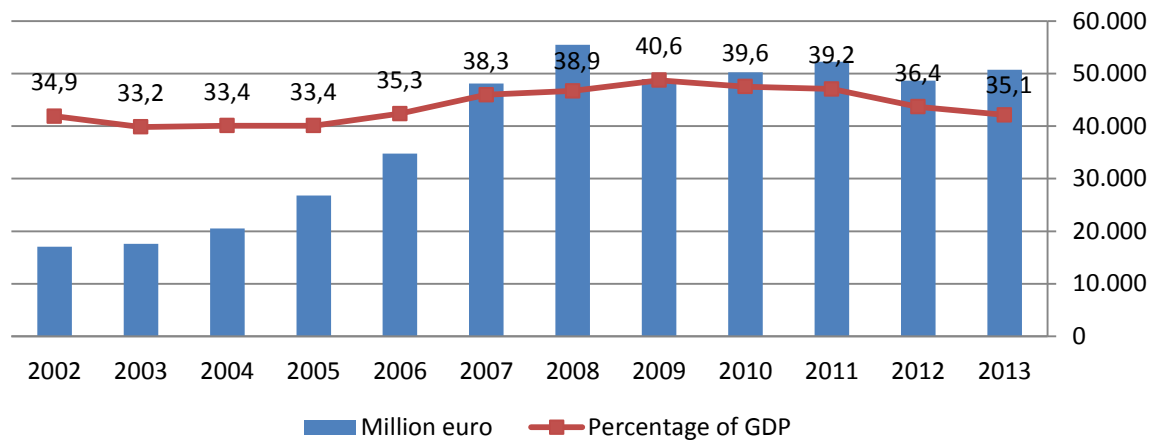
II. MATERIAL STAKE: PUBLIC PROCUREMENT IN ROMANIA

1. General view – the public procurement market

The necessary information on the specific national level indicators was obtained through a FOIA request sent to the National Authority for Regulating and Monitoring Public Procurement (ANRMAP) which answered in over 30 calendar days. Furthermore, although several projects had been publicly announced, until the completion of this country report, no Public-Private Partnerships (PPPs) were signed. Therefore, the following analysis of national level data on procurement relies entirely on the registered public procurement contracts in SEAP, the e-procurement portal. However, at least a third of public institutions did not use SEAP back in 2007. The number of users has gradually increased and, by the end of 2014, 14,721 contracting authorities were registered in SEAP (from 9,591 in 2007).

The existing official data shows that public spending increased continuously until 2008. Only the world economic crisis, combined with the European debt crisis, put an end to its growth rate in terms of absolute value (million Euros) – see Figure 1. As a percentage of GDP, total general government expenditure reached 40.6% in 2009, and slowly declined to 35.1% in 2013.

Figure 1. Total general government expenditure



Source: EUROSTAT

The three consecutive years that registered the highest government expenditure – 2007, 2008 and 2009 – are electoral years when quality of governance decreased (**Table 2**). For example, before each electoral campaign, the government decided to augment salaries and social expenditures above the state budget sustainability level (SAR, 2010).

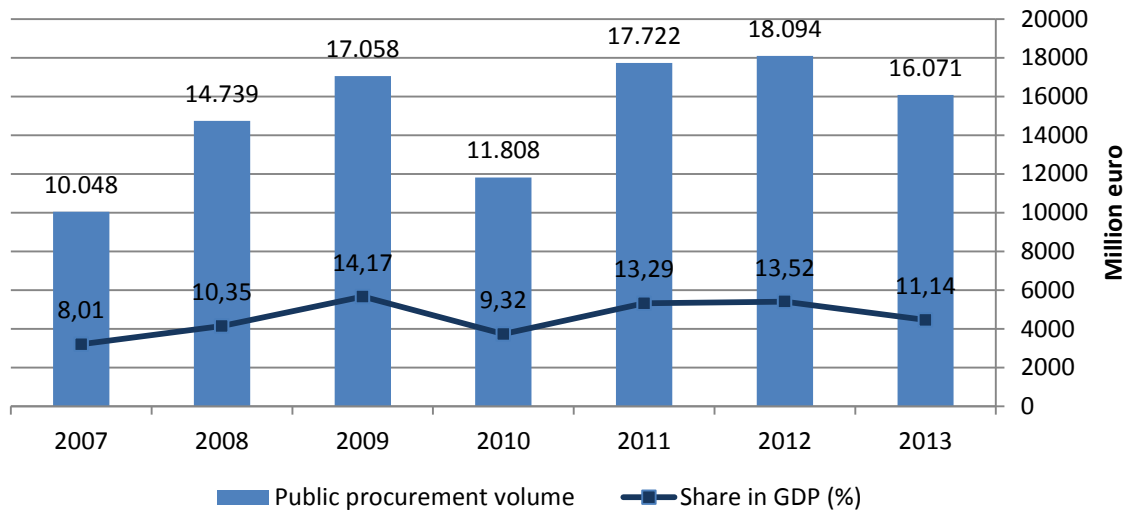
Table 2. Electoral years in Romania

YEAR	2007	2008	2009	2010	2011	2012	2013
Type of Elections	European	Local, National	European, Presidential	-	-	Local, National	-

Source: own compilation

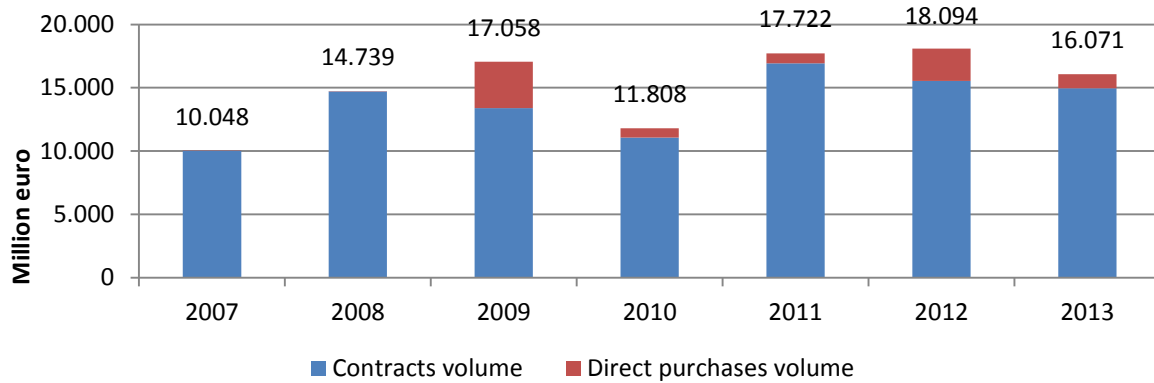
Government expenditure stabilized at around 50 billion Euros in the last four years of the period under scrutiny. In contrast, public procurement (at least the volume declared in SEAP) reached a first peak of 17 billion Euros in 2009 (14% of GDP), when the country was already facing economic crisis (**Figure 2**). While the Romanian economy contracted by 7.1% (negative GDP growth rate) in 2009, the augmentation in public procurement spending also coincided with a much higher total value of direct purchases (**Figure 3**). It may be that the simplified procedure of direct purchases, in which authorities freely chose the supplier of goods, services and works (see section III), was used to help certain favourite firms face a more difficult economic environment. Another scenario implies that public procurement at the time was greatly influenced by both the presidential and European elections in 2009 and by the need to finance companies that contributed to these election campaigns.

Figure 2. Total procurement volume and its share in GDP



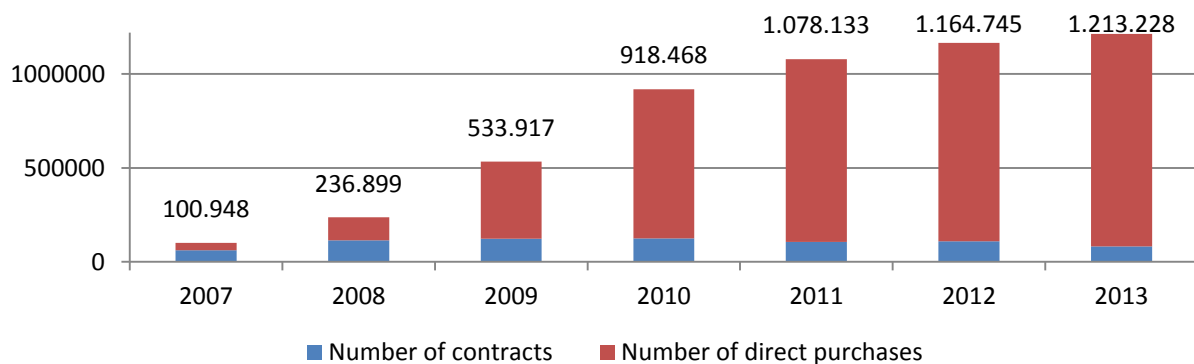
Source: EUROSTAT, ANRMAP and own calculations

Figure 3. Total public procurement volume



Source: ANRMAP and own calculations

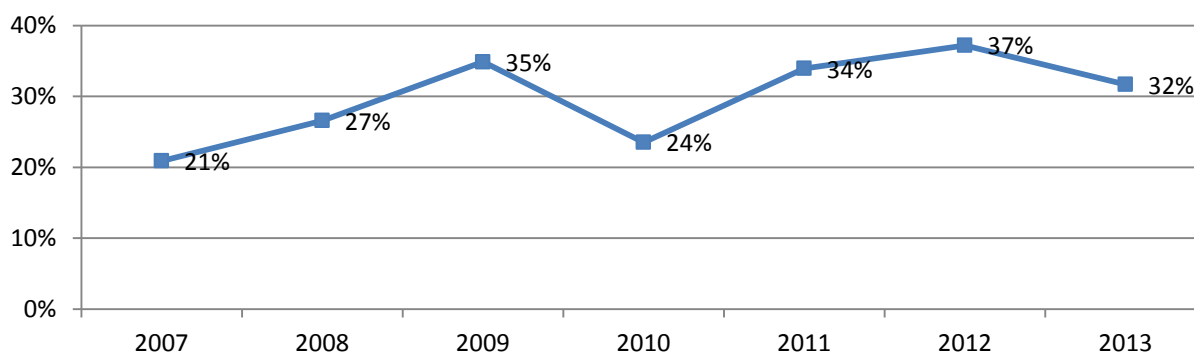
Figure 4. Number of public acquisitions



Source: ANRMAP and own calculations

The declared value of public procurement contracts stalled in 2010 despite a growing number of contracts and direct purchases from year to year (**Figure 4**). The law was modified in 2009, when the threshold for direct purchases was raised to 15,000 Euro (from 10,000 Euro). One explanation for the phenomenon might be the impact of austerity measures combined with the end of the presidential and European electoral campaigns (resulting into a smaller demand for public contracts from political sponsors). Romania signed a stand-by Agreement with the International Monetary Fund (IMF) in 2009. At the time, government expenditure was slowly decreasing in absolute value, as public wages were being cut due to austerity measures. However, Romania barely implemented some of the IMF requirements and only mimicked economic reform during the 2009-2012 period (SAR, 2013). After 2010, public procurement returned to its 2009 share in total general government expenditure (**Figure 5**).

Figure 5. Share of PP in total general government expenditure (%)



Source: EUROSTAT, ANRMAP and own calculations

In terms of the number of public procurement contracts, starting with 2008 there were over 100,000 contracts signed almost every year: the SEAP platform recorded over 122,000 contracts in 2009 and 2010, while in 2013 the number dropped to 81,000 (Figure 4). Declared

direct purchases progressed from 38,710 acquisitions in 2007 to over 1.1 million procurements in 2013. It followed closely the growing number of contracting authorities that registered in SEAP: from 9,591 public entities at the beginning of 2008 to 11,551 at the end of 2009, and 13,515 in 2012. In the last two years, over two thousand contracting authorities entered the electronic public procurement system (totalling 14,721 entities in 2014).

2. Public procurement in the construction sector

In this report, the definition of public procurement in the construction sector considers the Common procurement vocabulary's (CPV) 44, 45 and 71 divisions³ which cover all products and activities (works and services) concerning constructions. Thus, evaluating public procurement at sector level by making use of SEAP data includes in the analysis all contracts falling under these three CPV divisions.

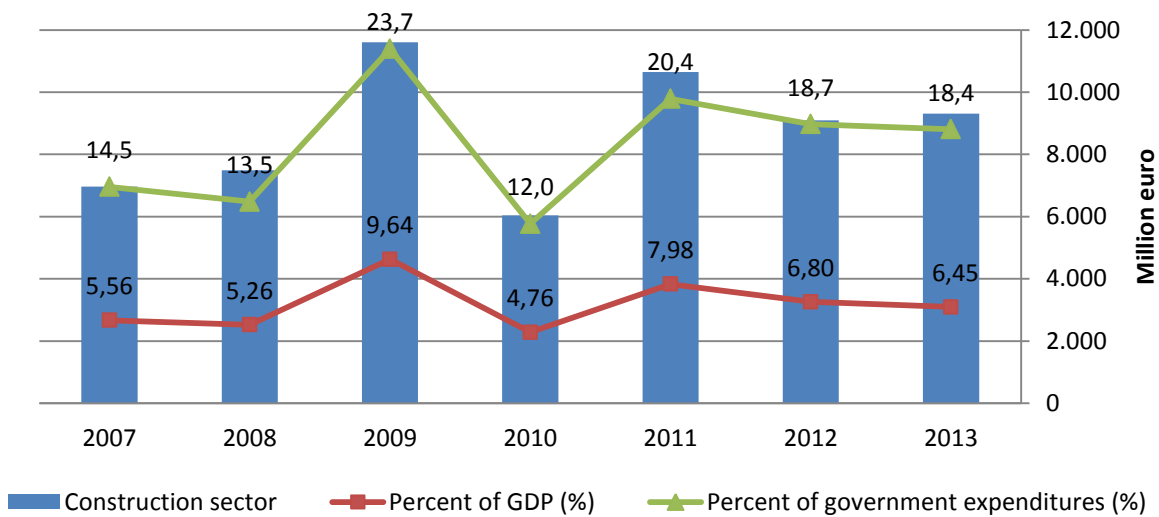
Public spending in construction reached nearly 7 billion euros in 2007, peaked at 11.6 billion euros in 2009 (the year of European and presidential elections) and one year later dropped to 6 billion euros. Afterwards it surged again to 10.6 billion euros (2011) and in the following two years it settled to around 9.1 billion euros. By comparing public procurement in the construction sector with total public procurement, one concludes that the general trends are closely followed at the sector level. Despite the economic crisis, 2009 represents the peak, both in absolute value and in percentage – share of GDP and share of total government expenditure (**Figure 6**).

Two explanations may arise. One is that maybe the additional number of contracting authorities registered in SEAP brought a relevant increase in the volume of declared procurement without more spending actually taking place. But it may also be that procurement spending was kept up by politically connected companies that were either in financial difficulties or in need of funding in electoral years and which find alleviation in public contracts. The increasing number of contracting authorities registered in SEAP and of direct purchases can hardly explain the huge sum spent in the construction sector only in 2009, over 3 billion euros, compared to all the other years (**Table 3**), which suggests that elections (presidential and European) taking place in that year might have played a role.

Although the number of contracting authorities registering in SEAP kept growing in subsequent years, the share of construction procurement in government expenditures or in GDP never returned to its 2009 level. Austerity measures had an impact on the 2010 construction related contracts, but as noted before, the IMF requirements became looser and looser in terms of public procurement. Also, the pressure of elections faded away until 2012.

³ These particular CPV divisions refer to: 44 – Construction structures and materials; auxiliary products to construction (except electric apparatus), 45 – Construction work and 71 – Architectural, construction, engineering and inspection services.

Figure 6. Construction sector procurement - volume and share in GDP and government expenditure



Source: EUROSTAT, ANRMAP and own calculations

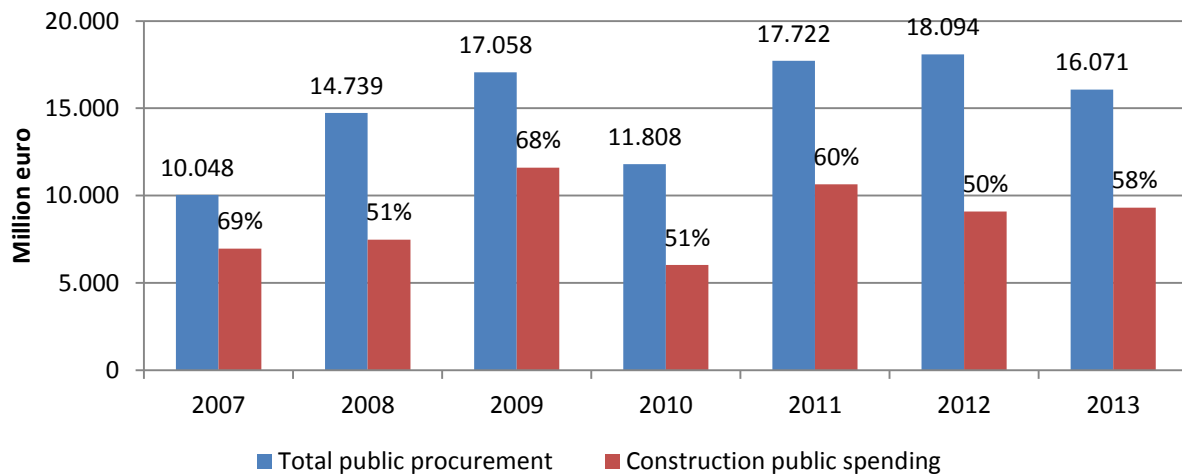
Table 3. Direct purchases volume - PP in construction sector

YEAR	2007	2008	2009	2010	2011	2012	2013
EUR million	0.040	0.618	3043.501	106.955	168.235	175.382	251.035

Source: ANRMAP

Romania is well known especially for its serious problems with road infrastructure. The GGI – sub-index 2.02 *Quality of roads* ranks Romania even worse – from 100th place in 2006-2007 to 121st place in 2014-2015. According to EUROSTAT data, the length of motorways in use scarcely progressed from 113 km in 2003 to 550 km in 2012. Currently, the length of motorways in use does not exceed 700 km. This is an extremely low number, compared to the length of national roads in Romania – around 17,000 km according to official Ministry of Transport (MT) statistics (Ministry of Transport, 2015). Thus, the important share of construction spending in total procurement, an average of 58% (**Figure 7**), is explained by the country's need to modernize its infrastructure.

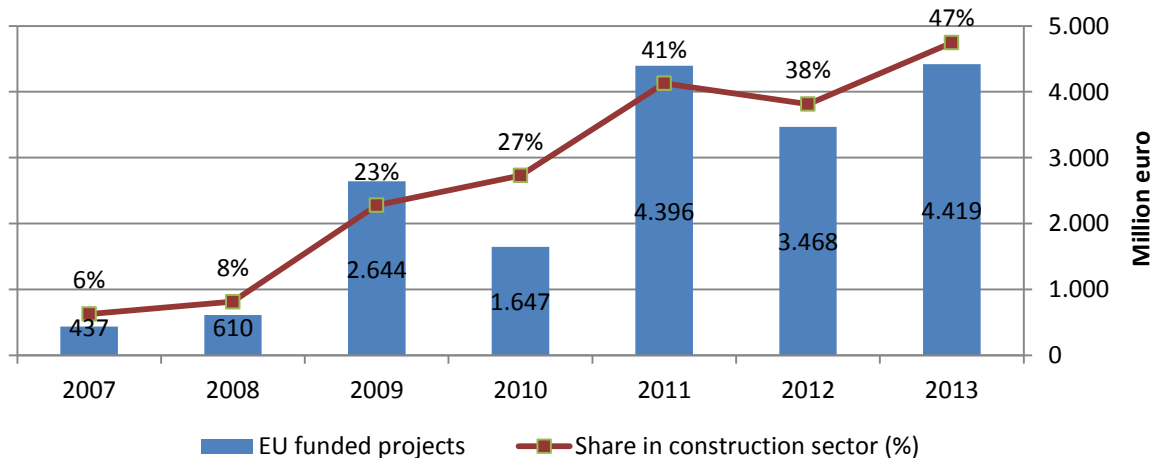
Figure 7. Share of construction spending in total procurement (%)



Source: ANRMAP and own calculations

The state budget allocations for road infrastructure are insufficient to build all the necessary motorways. Many infrastructure projects thus received a boost along with the infusion of European funding. The growing share of EU funded contracts in the overall construction sector, from 6% in 2007 to over 47% in 2013, is not random (**Figure 8**). Romania had problems in accessing and spending EU funds in the first years of membership (2007 and 2008). It had to gradually accelerate its absorption rate so as not to lose the allocated money for the 2007-2013 programming period. The small number of EU funded procurement contracts in construction is illustrative of the state's poor capacity in absorbing EU funds earmarked for this sector – from a couple of hundred at the beginning of the programming period to over 1300 in the last years (**Table 4**). One explanation may be that regulations and controls are more demanding for this category of funds.

Figure 8. Public procurement in the construction sector – European funding



Source: ANRMAP and own calculations

Table 48. Number of PP contracts in construction sector

YEAR	No. EU funded contracts (a)	Total no. of contracts (b)	Share (a/b)
2007	259	13,196	2%
2008	261	21,176	1%
2009	722	17,746	4%
2010	1000	15,450	6%
2011	1667	13,123	13%
2012	1333	10,409	13%
2013	1303	7,503	17%
TOTAL	6545	98603	7%

Source: ANRMAP and own calculations

3. Firm level analysis of the construction sector

Romania's construction sector seems at first glance a non-concentrated market divided between many domestic companies and an important number of international companies. From 2009 to 2013, the number of international companies in the Romanian top 100 construction firms grew from 27 to 35, and their profits surged. In 2009 multinational firms made up 16% and in 2013 the figure reached almost 65% of the total profit. At the same time, Romanian companies' average turnover for these five years was close to 68.3%, ranging from 70.9% in 2009 to 59.8% in 2013. This is a sign of low efficiency in activities run by domestic companies compared to international companies (Table 5). All in all, national firms prevail in the overall construction sector (private and public markets combined), which is not surprising. Nevertheless, the number of international companies and their profits indicate fierce competition on the market.

Table 5. Top 100 construction companies in Romania

YEAR	TOTAL TOP 100		DOMESTIC FIRMS		INTERNATIONAL FIRMS		TOP 100	
	TURNOVER* (million EUR)	PROFIT* (million EUR)	Turnover out of total Top 100 (%)	Profit out of total Top100 (%)	Turnover out of total Top 100 (%)	Profit out of total Top100 (%)	No. RO firms	No. INT firms
2009	4657.37	309.93	70.9%	83.2%	29.1%	16.8%	73	27
2010	4130.73	190.79	74.2%	98.8%	25.8%	1.2%	74	26
2011	4510.70	300.10	72.9%	63.5%	27.1%	36.0%	70	30
2012	4547.17	73.48	63.8%	97.0%	36.2%	3.0%	67	33
2013	4065.95	240.22	59.8%	35.4%	40.2%	64.6%	65	35

Notes: * Exchanged into EUR using average yearly exchange rate, not corrected for inflation

Source: OCTAGON CONTRACTING & ENGINEERING

Table 6. Number of winners

	Total PP winners	EU project winners
Total no. of companies	1484	691
Out of which international companies	145	107

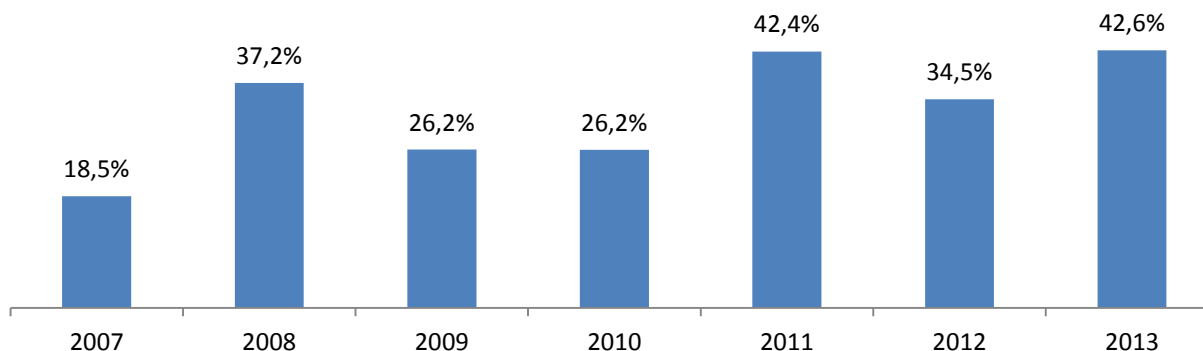
The database used in the analysis and described in Section IV contains 1484 winning companies for the period January 1st 2007 – December 31st 2013, out of which 145 are international firms (9.8% out of total number of firms). Over 46.5% of all firms have won an EU funded project in the construction

Source: own calculations

sector in the researched period. Out of the 691 companies that participated in public procurement in the construction sector and won EU funded contracts over 1 million euros, 107 were international companies (**Table 6**).

More than 73% of the international companies present on the public procurement construction market⁴ compete with national firms for EU funds. For the entire 2007-2013 period, EU contracts account for 37.1% of total public procurement, with international companies holding a high share on this specific market segment (almost a third on average). In the same year, 2011, when one of the highest shares in EU funded public procurement contracts won by international companies was recorded, the largest number of international companies was active on the market (see **Figure 9** and **Table 7**).

Figure 9. EU funded public procurement projects in the construction sector - share of contracts (by value) won by international companies



Source: own calculations

⁴ In this context the public procurement market consists of contracts over 1 million euros.

A large number of firms with very small market shares⁵ make up the public procurement construction market involving contracts with a value of over 1 million euros. A market selection based on whether public procurement winners have signed a contract involving EU funding in the years 2007-2013 is shown in **Table 7**. The number of companies that compete in the public procurement sector involving EU funded projects increased as the market became more transparent and the absorption rate of European funds had to be augmented. Interestingly enough, domestic firms more than doubled their numbers in 2009, when international firms' market share in EU funded projects in the construction sector dropped from 37.2% in 2008 to 26.2% in 2009 (**Figure 9**). Consequently, starting from 2009 the mean market shares of national winners of public procurement contracts involving EU funds are smaller than those of international winners. The result is not surprising, as the number of domestic companies is much larger than that of their foreign competitors.

Table 7. Market share in total public procurement above EUR 1 million of EU funded projects winners in the construction sector

YEAR	Number of companies		Mean market share		Median market share	
	Domestic	International	Domestic	International	Domestic	International
2007	30	5	0.657%	0.419%	0.194%	0.335%
2008	43	16	0.695%	0.401%	0.217%	0.307%
2009	115	20	0.300%	0.396%	0.123%	0.222%
2010	190	22	0.239%	0.803%	0.134%	0.281%
2011	259	51	0.196%	0.548%	0.064%	0.119%
2012	223	32	0.220%	0.698%	0.089%	0.259%
2013	190	27	0.237%	1.129%	0.144%	0.457%

Source: own calculations

Examining the Top 10 winners by year can further our understanding on the matter (**Table 8**). Each had a market share between 1.2% and 10.7%, while their average cumulated market share amounted to 33.2%. The leader's market share gradually decreased over the years, as the construction sector became more competitive – from 10.7% to 7.4%. If at the beginning of the 2007-2013 period, the top 10 winners in the public procurement construction sector were Romanian in 90% of the cases, at the end of 2013 already seven out of ten top winners (70%) were international companies.

Table 8. Aggregated information on Top 10 companies with the largest market share (PP contracts above EUR 1 million)

	2007	2008	2009	2010	2011	2012	2013
Total market share of top 10	38.1%	31.2%	29.5%	28.6%	36.9%	37.2%	31.1%
Leader's market share	9.6%	10.7%	8.7%	10%	7.8%	8.1%	7.4%

⁵ Yearly market shares were computed without taking into account 557 framework contracts, as these types of contracts cover a longer period of time and involve large amounts of money. Also, a framework contract does not imply that the entire value of the contract will be consumed.

Total no. of contracts won by single bidding	35	37	13	15	12	5	5
No. of international firms	0	2	1	3	5	3	7
No. of companies that won EU funded project	3	5	6	5	9	7	10
No. of firms – donors to political parties	1	3	2	2	0	1	0

Source: own calculations

The average cumulated market share was exceeded in two pre-electoral years, 2007 and 2011, and in one electoral year, 2012. The year 2007, when top 10 winners accounted for 38.1% of the market, was the single year without any international companies present in the leading 10 positions. It also registered a high number of single bidding among the top companies. The practice of single bidding diminished after the first years of EU membership when a smaller number of companies with political ties seem to have managed to dominate the Romanian market, at least in the first three years of the researched period.

One would expect that leaders on the market be the ones winning EU funded contracts. However, until 2011, six or fewer per year of such companies had been awarded an EU funded contract. This opens three possibilities. First, we would expect that government favouritism would take place especially vis-à-vis national funds if the top 10 companies were politically connected. Alternatively, the top 10 companies' ability to win an EU funded contract would be hindered by the absence of political connections. But it may also be that, without any connection to politics, securing nationally funded public procurement contracts simply requires a different set of skills than the ones needed in winning EU funding. We shall test these hypotheses in section IV.

Does public funding matter for the average construction company? A brief investigation of relevant Top 45 construction companies in terms of total turnover (in 2013) that won EU funded contracts in the researched period shows that roughly one fifth of their yearly turnover depends on public spending⁶ (average for the 2008-2013 period, see **Table 9**). A small number of firms make over 50% of their revenues in connection with public procurement contracts (**Table 9**). Almost 15 companies present in the Top 45 companies do not depend at all on public contracts above 1 million euro (average for the 2008-2013 period).

Table 9. Share of public procurement contracts in the turnover of Top 45 companies – winners of EU funded projects

	2008	2009	2010	2011	2012	2013
Mean	15.8%	21.5%	20%	22.8%	23.7%	21.8%

⁶ Public procurement contracts won in consortia were not taken into account when establishing the share of public money in total turnover.

Median	5.2%	9.2%	13%	15.9%	11.1%	6.2%
Share of >=50% (no. of firms)	7	10	7	6	7	4

Source: own calculations

III. NATIONAL PROCUREMENT LEGISLATION AND PRACTICE

1. Rules of the game in Romanian public procurement legislation

To assess the process and outcome of public procurement we need to examine its regulatory framework. As a full EU member and in accordance with the Treaty on the European Union and the Treaty on the Functioning of the European Union, Romania transposed the public procurement legislation package, specifically the Public Sector Directive⁷ and the Public Services Directive⁸. The general legal framework setting out the main rules is represented by Government Emergency Ordinance (GEO) no. 34 of 19/04/2006 on awarding public procurement contracts, works concession and services concession contracts. The GEO is essentially a translation of the two European directives; it establishes the list of procedures⁹ and the steps which are to be followed in awarding a public procurement contract, including solving challenges against the acts/decisions of the contracting authority¹⁰.

Strangely enough, this regulation was issued by the Government, not by the main legislative body, the Parliament, as an emergency ordinance¹¹. Although heavily criticized throughout the years because it essentially substitutes the legislature with the executive, the issuance of emergency ordinances by the Government has become a steady practice¹².

The secondary legislation on public procurement consists in regulatory acts such as Government Decisions through which the application norms of GEO no. 34/2006 and of the GEOs which add to or modify it are described in detail. One of the problems of the Romanian public procurement field is overregulation. The existence of tertiary legislation represented by

⁷ Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.

⁸ Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procedures of entities operating in the water, energy, transport and postal services sector.

⁹ The types of award procedures which can be used are the following: open or restricted procedure, restricted accelerated procedure, competitive dialogue, negotiation with prior publication of a contract notice (negotiation), accelerated negotiation, negotiation without prior publication of a contract notice, call for tenders.

¹⁰ This GEO is not used in awarding a contract which is a result of an international agreement, when a procedure specific to international bodies or institutions takes precedence or when Union law demands a special procedure, as is the case for cross-border programs and projects.

¹¹ A GEO represents a special kind of legal measure since it may only be used in extraordinary or urgent circumstances and, as a result, it bypasses normal parliamentary debates. Its provisions are discussed in Parliament, where it can be approved or rejected via a law, but after its effects have already taken place.

¹² According to the records of the Chamber of Deputies, from 2007 to 2014, the Government issued a total number of 1057 GEOs with an average of 132 GEOs per year. Most GEOs were issued in 2008, a total number of 229, whereas the least number was registered in 2014, only 94.

Orders – which consist in interpretations of certain primary legislation provisions – issued by the ANRMAP adds another layer of legal complexity. In addition, the contracting authorities receive different “instructions” from the ANRMAP that do not have a clear legal status vis-à-vis economic operators.

This intricate legal landscape is further supplemented by norms regulating state entities that have a control function¹³ and the Government Decisions that describe the structure and functions of key institutions that sometimes overlap in monitoring and checking public procurement procedures. The main responsible body is the abovementioned ANRMAP followed by other oversight entities such as the Unit for the Coordination and Verification of Public Procurement (UCVAP), which answers to the Ministry of Finance, the National Council for Solving Complaints (CNSC), the Court of Accounts (CC) and the Department for the Fight against Fraud (DLAF). In addition, the Management Authorities and the Implementation Bodies which are charged with managing EU funds can also issue opinions on the conformity of a procurement procedure.

2. Increasing number of rules, opposing interpretations and transparency problems

In addition to the number of norms and public bodies charged with the same control and oversight functions, the smooth implementation of GEO no. 34/2006 was and still is impeded by a lack of a unitary and consistent interpretation of the existing legislation and even of similar cases. The consequences of this situation are evident especially in those cases dealing with EU funds since there are differing viewpoints coming from the monitoring and control entities, the contracting authorities and the economic operators as to the correctness of the procurement procedure and the decision of the evaluation committee. Because of an unclear, unstable, and overregulated legislative framework worsened by sometimes contradictory implementation of the rules and a lack of administrative capacity, contracting authorities and economic operators end up being sanctioned both by national monitoring and control bodies and corresponding EU institutions via financial corrections. Furthermore, public projects are placed on hold until contestations and legal disputes are settled in courts, thus leading to a waste of public resources.

Table 10. Number of GEOs modifying GEO 34/2006

TOTAL	2006	2007	2008	2009	2010	2011	2012	2013	2014
26	2	3	3	3	3	2	3	6	1

Source: own compilation based on ANRMAP legislation

¹³ Examples of such norms are GEO no. 30/2006 on verifying the procedural aspects of awarding public procurement contracts, the Law on Private-Public Partnerships no. 178/2010 or GEO no. 114/2011 on awarding public procurement contracts in the fields of defence and security.

The legislation available on ANRMAP's website mentions that a total of 26 modifying acts (six in 2013 and one in 2014) have been issued by the Government targeting the application norms of the abovementioned GEO (Table 10). Nevertheless, the numerous modifications do not seem to have been prompted by national or local elections or changes in government. Each year, except 2013 and 2014, saw approximately three modifications. In this sense, in autumn 2012, the number of changes was the subject of a warning issued by the EC when it was emphasized that "the modifications brought to the public procurement law are too frequent and [...] this can constitute a reason to initiate an infringement procedure because it points to a lack of legislative stability and it affects the business environment" (Dinca, Barbulescu, 2012).

Some of the changes brought to GEO no. 34/2006 have led to a decrease in transparency and procedural control vis-à-vis the award or contestation procedure. For instance, the thresholds under which the contracting authority has the right to directly purchase products, services or works were aligned to those present in the EU directives and were raised from EUR 5,000 (the threshold in 2006¹⁴) to EUR 30,000 excluding VAT for products or services and to EUR 100,000 excluding VAT for works¹⁵ (Table 11).

Table 119. Direct purchases threshold changes

	2006 Initial Act	2007	2009	2013 Alignment to European Directives
Threshold for direct purchases	EUR 5,000	EUR 10,000	EUR 15,000	EUR 30,000 excluding VAT for products & services, EUR 100,000 excluding VAT for works
Initial/ Modifying Act	OUG no. 34/2006	OUG no. 94/2007	OUG no. 19/2009	Law no. 193/2013

Source: ANRMAP legislation and INDACO legislation database

Another problematic legal measure was Law no. 193/2013 which took away from ANRMAP the possibility to appeal to a court of law so as to declare null and void those contracts which had been signed via vitiated procurement procedures¹⁶ and left intact only the possibility for it to issue an "infraction of regulations". The reasons could vary from the implications this had on the ANRMAP public official (conflict regarding their status) to the wish that this institution does not have this legal remedy at hand.

A controversial modification was GEO no. 51/2014 because, although it was considered by the executive as a potential solution to the contestation practice that contributed to the low

¹⁴ These thresholds were changed on several occasions via GEOs, such as GEO no. 94/2007 when the maximum value for direct purchases was raised to 10000 Euro and GEO no. 19/2009 which raised the threshold to 15000 Euro.

¹⁵ However, starting with January 1st 2013, GEO no. 77/2012 obliges the contracting authority to send SEAP, in ten days after receiving the justificatory document, a notification if it uses the direct purchase procedure which is above 5000 Euro excluding VAT.

¹⁶ ANRMAP had this legal right through GEO no. 77/2012.

absorption rates of EU funds since it delayed the signing of contracts, it was seen as limiting the possibility of stakeholders to signal problems in award procedures. The GEO stated that those economic operators that wanted to legally contest the procedure or its result were obliged to deposit a “good conduct guarantee”¹⁷ for the entire period from its initiation to the moment the CNSC or a court of law issue a decision. This legal act caused a scandal because of the lack of transparency in its elaboration and adoption – the CNSC, one of the institutions charged with its implementation, criticized the Government for not consulting it on the matter. However, the provision that the contracting entity could keep the guarantee was declared unconstitutional by the Romanian Constitutional Court in January 2015 and even the EC warned the government that it might lead to an infringement procedure due to its excessive nature.

The public procurement legislation provides various deadlines for the publication of participation, award notices etc. in SEAP and in OJUE¹⁸. Although in line with the minimum legal requirements, the obligation to submit offers in 11 days for calls for tenders or 52 days for an open procedure may be considered as an impediment for economic operators in submitting sound offers, especially for more complex projects. Therefore, the offers that are submitted within this timeframe are either of low quality or come from operators who might have had advance knowledge of the calls, leading to the suspicion that they might have been favoured by the contracting authority in question.

Romanian civil society, together with expert groups (IPP, 2013a; IPP, 2013b), have underlined a problematic aspect of the present procurement legislation, namely the fact that it offers monitoring instruments only up to the moment the contract is signed by the parties. In this sense, one cannot fully know and, therefore, assess in due time if the contract’s implementation is in line with the set requirements and if the quality of the goods, services and works is adequate. Related to this issue, the overall transparency of a procurement procedure is also reduced by the requirement to publish in SEAP the award notice after a considerable timespan (48 days) after the contract was signed.

The law allows unrestrained access to the public procurement contract because it is an administrative legal act subject to Law no. 544/2001 on Free Access to Public Information. Consequently, any interested citizen can request access to the entire procurement file¹⁹ containing the signed contract and all the other information directly related to the procurement process. However, the file is kept as long as the contract produces legal effects, but not less than five years from the day the contract was finalized.

¹⁷ The guarantee had to represent 1% of the estimated contract value (with a cap of 25,000 Euro for goods and services and 100,000 Euro for works) and, in case the contestation was rejected, the contracting authority was able to keep the sum of money.

¹⁸ Contracting authorities must publish a contract notice/award notice in the OJEU if the estimated value of the supply or services contract is equal or above the equivalent in lei of 130,000 Euro (400,000 Euro if the contracting authorities operates in the utilities sector) or if the estimated value of the works contract is equal or above the equivalent in lei of 5,000,000 Euro.

¹⁹ In assessing the conformity of a procurement procedure, the procurement file contains important pieces of information, such as the notice on determining the estimated value, the award documentation, the submitted offers, the report on the award procedure, the contestations submitted during the procurement procedure along with the decisions taken by the CNSC, etc.

Some institutions use this provision to limit public access to such documents by physically destroying or refusing to grant access to the procurement file after the aforementioned time period. Transparency is further reduced by the fact that the existence of electronic archives on public websites is rare despite the fact that Law no. 135 on archiving documents in electronic format is in force since 2007. The official justification for this weak improvement in e-government at the local level is the lack of resources, but to this one might also add the lack of political will. Moreover, in some cases, the DNA raids the headquarters of a contracting authority and seizes various contracts as evidence in on-going corruption investigations dealing with public procurement²⁰ resulting in yet another impediment in gaining access to information.

3. Who decides the distribution of public resources

One of the reasons for which the contracting authorities have not reached the best value for the money spent is the excessive use of the “lowest price” criterion. Out of all the contracts published in SEAP between 2007 and 2014, 83% have been awarded through procurement procedures using this type of condition. This particular strategy absolves the contracting authorities of the responsibility of using more complex awarding criteria which would, in turn, generate the need to organize a technical expertise stage during the evaluation step of the procurement procedure. Furthermore, it has been repeatedly pointed out that the quality of the goods, services and works is disregarded since the contract value is close to the minimum market price (IPP 2013a).

Procurement legislation, but also practice has shown that the key people who decide the winners of a procurement contract are the bureaucrats who are present in the evaluation committees, not the politicians. GEO no. 34/2006 stipulates that each contracting authority is obliged to establish a specialized in-house public procurement department. The president of the contracting authority names the members of the evaluation committees via a legal instrument called a “decision”. These members have to be a part of the specialized apparatus of the above mentioned procurement department and some remain in the evaluation committees irrespective of elections or the changes in the central government, as proven by our investigation.

In order to avoid conflicts of interest, both the members of the evaluation committees and the affiliated experts are obligated to sign a confidentiality and impartiality declaration whereby they confirm that they are not in a situation that would imply the existence of such a conflict (GEO no. 925/2006). Also, after a contract is awarded, it is forbidden for up to a year for the winner to employ persons or legal entities involved in the verification and evaluation procedure in the implementation of the contract (GEO no. 34/2006). These rules notwithstanding, an important problem arises at the local level, in public entities such as city halls of small and isolated

²⁰ During the research phase for this country report, procurement files pertaining to road infrastructure from 2007 to 2013 were requested via Law no. 544/2001 on Free Access to Public Information from all 41 Romanian County Councils and the Bucharest City Hall. After delaying granting us access to the entire set of requested information, Brasov County Council informed us that the DNA seized several procurement files which were also on the list we demanded. Almost none of the County Council archives hold a copy of the contracts or procurement files and they do not make one before such documents are seized by prosecution bodies.

Communes where specialized human and administrative resources are scarce. This lack of institutional capacity impacts the evaluation committees' creation and proper functioning. For instance, local councillors are present in these committees even though they could be considered to be in a conflict of interest since they are also the ones who vote on the contracting authority's budget, its investment plan and the budget allocation per project. Therefore, they could be suspected of directing more money towards a preferred company or that they prioritize a certain project because of direct or indirect interests.

4. Public Private Partnerships

Institutional public-private partnerships (PPP) in Romania are regulated through Law no. 178/2010, thus enjoying a specific legal framework. However, these types of contracts must comply with the basic principles of public procurement legislation. Similarly to the procurement law, the law on PPPs has been repeatedly modified by the Government as a result of criticisms coming from the EC.

In Romania, no PPP projects have been initiated since 2010 and the reasons are the institutional tug of war, faulty legislation and a lack of administrative capacity and will. The latter refers to technical problems related to the SEAP interface. The law's implementing rules do not permit the publication of the selection and award notices and their accompanying documents through any other means than SEAP, but this was made possible only in early 2013 when the Government had already started working on a new PPP law.

Discussions on this new law were carried out throughout 2013, but a resolution on the matter was not reached because of several controversial aspects that became the subject of a major bone of contention between the stakeholders before the text was sent to the Parliament in late 2013. The first major problem was the Government's initial intent to limit the types of procedures available to select offers in the previous law (open and competitive dialogue) to one which was considered to be more restrictive and less transparent (competitive dialogue). As an important side note, having competitive dialogue as a sole selection procedure was among the flaws pointed out by the EC in early 2011 vis-à-vis the 2010 PPP law²¹. Consequently, the problematic aspects, including the provision on the selection method to which the open procedure was added, were corrected via a GEO. Second, the Government would have been able to unilaterally modify or annul the contract in light of "exceptional reasons linked to national or local interest", which had all remained undefined concepts. Third, foreign or national public companies would have been able to participate as private entities in calls for tenders²². Despite having the draft law returned to Parliament for re-examination by the President in early 2014, the parliamentary majority adopted the Government's draft law in June. The new law, although having slashed two

²¹ The Romanian Government at the time received a pre-infringement warning which stated that the PPP law disregards the *acquis* and jurisprudence on public procurement and concessions. Source: GEO no. 86 from 12 October 2011 published in the *Official Gazette* no. 729 from 17 October 2011.

²² The problem stemming from that particular provision was that private companies would have been discriminated and competition distorted since the contracting authority would have been unable to disqualify the public company if it decided to submit an unusually low priced offer on grounds that it was a legal recipient of state aid (Cozmei, Pantazi 2013).

of the abovementioned problems, still included the possibility of arbitrary action by the Government against the private entity. Moreover, despite the Competition Council's advice (Competition Council, 2013), a new provision was included whereby the government would have been able to replace the private partner or the project company if they did not respect the contract obligations *without* organizing a new award procedure *only if* this situation is specifically mentioned in the award documentation and the PPP contract. Therefore, the selection of a new partner ran the risk of being non-transparent and subject to the Government's choice. Because of this particular aspect, the parliamentary opposition challenged the law at the Constitutional Court. The latter decided in July 2014 that the law is technically flawed and imprecise, thus leaving room for arbitrary action against the private partner. In addition, both the Government and the Parliament did not respect the obligation to judiciously transpose EU legislation on the matter of unilateral modification and annulment of such a contract (Constitutional Court Decision no. 390, July 2014). As a result, the law has to once more pass through the entire legislative process.

5. Conclusion

To conclude, there are no substantial differences between the European procurement legislation and the manner in which it was transposed in Romanian national laws and norms. The main differences arise in the implementation of primary legislation. The high number of orders, instructions and contestations denote the general distrust between all the actors involved and in the correctness of the procurement procedure.

The legislative modifications which have occurred in 2013 and 2014 were justified by the changes taking place at the European level, but were also a result of specific interests. The government argued that the changes were vital in securing efficient and effective results in using public resources. However, recent examples of controversy, such as the GEO obliging economic operators to deposit a good conduct guarantee and the failed new PPP law, point to the fact that legislative measures tend to be adopted without a proper public and inter-institutional debate and end up being struck down – a situation which causes delays in effectively solving problems.

In general, the national legislation and court decisions do not point to a *systematic* pattern of a particularistic distribution of resources. The corrupt practice of awarding contracts to favoured firms which may result in an overall poor implementation of a project occurs when the law is being purposefully disregarded within the contracting authority. Hence, it is of utmost importance to monitor not only the award procedure, but also the contract's realization in accordance with a set of clearly defined quality standards.

IV. DETECTING CORRUPTION RISK IN PUBLIC PROCUREMENT

1. Data collection

To identify patterns in public procurement awards and test the hypotheses outlined in the previous sections, the present analysis of corruption risks in procurement draws on several sources. Data extracted from the electronic procurement portal was enriched with regional and

local level data retrieved by FOIA requests sent to local contracting authorities active in the road infrastructure sector. The information on which firms are political party donors was gathered from the Official Gazette of Romania. Additionally, a list of companies receiving favourable treatment according to national and local media and whose managers or owners were under investigation or indicted by prosecution bodies was compiled. Furthermore, statements of interests and assets of individuals in charge of procurement boards were examined, as well as Trade Register data (profit, turnover) on the companies belonging to Top 100 businessmen and on the Top 60 construction sector companies.

The necessary contract level information for compiling the present data-driven section as well as part of section II.3 (firm level analysis) was gathered by purchasing a subscription that allowed direct access to the SEAP server and downloading pieces of information which subsequently had to be transposed into a reusable database format²³. A considerable amount of time was needed to download the need files and even more time to build and clean the database of errors which would have distorted the research results²⁴. The resulting database comprises 6064 contracts found under the CPV classification codes 44, 45 and 71, each with a total value above 1 million euros. The time period taken into consideration is January 1st 2007 – December 31st 2013. For each contract the following variables have been gathered and used in the investigation: winner's name and tax ID, winner's country, name of the contracting authority, type of procurement procedure, type of contract (framework contract or not), award criterion, type of bid (with electronic auction or not), number of submitted offers, subcontracting allowed or not, contract signature date, contract value and estimated value (in Romanian Lei in most cases, but in USD and EUR as well; excluding or including VAT, with the VAT rate many times erroneously specified) and type of funding (national or European). Furthermore, the following processed data was added: market shares, number of contracts won (total, EU and nationally funded), whether firms are party donors/accused of being politically connected or not for each year.

In order to document and investigate the relationships between award givers and shareholders of winning companies, contracts with a value above 1 million euros pertaining to national and county-level road infrastructure projects²⁵ were selected and examined in greater detail. The

²³ In an attempt to gain systematic access to contract-level data, neither the ANRMAP, nor the Agency for Romania's Digital Agenda (AADR) could provide immediate assistance. Answers to any questions regarding specific data came with delay because these public authorities had to contact the private firm UTI, SEAP's system operator and the entity that had access to the actual database behind the online interface. SEAP's public online interface could not be used to investigate broader sectors because it provides search functions based only on one specific CPV code. Moreover, SEAP does not provide the possibility to compile statistics, comparisons or rankings. In addition, using a web crawler to gather the data directly from the website was impeded by the need to fill in a new CAPTCHA code for every single query (searches, switching from one page to another or viewing notices).

²⁴ For each type of notice, the information for which data mining was used to collect from SEAP had a different structure. Also, additional fields for the same category of notices, such as whether or not the contract was financed via EU funds, were not always filled in. One of the biggest challenges in building the database was applying the corrections made to a large amount of contracts via their respective errata which are also present in SEAP. The main problems were that the errata have different structures from one record to another and their content does not comply with any standardization, punctuation or formatting. Consequently, a considerable number of additional steps were needed to detect all possible cases and correct the errors.

²⁵ The projects pertaining to this particular sector refer to both construction work (building, repair, expansion, consolidation, maintenance) and services (consultancy, technical designs, site coordination) pertaining to road infrastructure.

information was gathered by sending a FOIA request to public entities which are also contracting authorities²⁶ in the field of road infrastructure so as to gain access to data that are not present in SEAP. In this sense, in addition to the contracts and their (potential) addenda, the request also asked for two specific types of data. First, the annual public procurement plan of the contract authority in question which lists all the signed contracts, the winners and the contract value. Second, the evaluation committee's report which contains the offers made by all the economic operators, the number and content of clarification requests made by the contenders vis-à-vis the project specifications drawn up by the contracting authority, reasons for disqualifying some contenders, the number and reasons invoked in potential contestations coming from the losing contenders, the justification for awarding the contract to the winner and the names of each committee member. Partially complete responses were received from a total of 31 County Councils²⁷.

The resulting database²⁸ was manually constructed and contains 3787 entries (each row represents a contract) and 796 winning companies. Out of each 5-member procurement award committee, a total of 215 committee presidents, considered as the main award givers, were further scrutinized by examining their statements of interests and assets from 2008 to 2013 – the years for which the documents are publicly available on the Romanian National Integrity Agency's web portal.

The purpose of this investigation was to identify the disclosed private companies which are fully or partially owned by those particular committee presidents and/or their first degree relatives and examine whether these companies were also awarded procurement projects within the same or other counties. Also, their presence in the administrative council and/or the supervisory boards of public, local-level companies (especially those active in the road infrastructure sector), as well as the existence of contracts between themselves and/or their first degree relatives with public bodies were also highlighted. The same operation was repeated regarding the statements of interests and assets of 59 County Council Presidents who were in office from 2008 to 2013. A total of 177 private and public companies were identified as being associated with these local public officials. The resulting list of companies was compared to those contract winners present in the manually constructed database in order to see if there are any matches.

²⁶ The selected entities are all the 41 Romanian County Councils, the Bucharest City Hall, the Romanian National Company of Motorways and National Roads (CNADNR), the Ministry of Transport (MT) and the Ministry for Regional Development and Public Administration (MDRAP).

²⁷ Some county councils charged prohibitively high taxes for copies to official documents, others, such as the Bucharest City Hall and the MDRAP, did not answer the FOIA request or delayed access to PP files indefinitely.

²⁸ For each contract, the following variables were taken into consideration: type of contract object (goods, works, services), type of procedure, type of contract (framework contract or not), signature date, the name, tax ID and county in which the contracting authority is located, whether the contract was awarded to a consortium of firms, name, tax ID and county in which the winning company is located, contract title, value (Romanian Lei or Euro excluding VAT) and duration, type of funding (national or European), the existence of contract addendums and the new contract value or duration inscribed in the addendums, the name of the president of the evaluating committee and of the other four members, existence of the participation notice in SEAP, names of each contender, number of offers submitted, offers' value (Romanian Lei excluding VAT), award criterion, winning price offer, contract duration, number of clarification requests.

From the list of Top 100 businesspeople and from official documents requested from the Romanian Trade Register, the names and tax IDs of 391 companies fully or partially owned by the first 10 who are mostly active in the road infrastructure sector were extracted. Additionally, from the Official Gazette of Romania the names and tax IDs of 1726 private companies which were registered as having donated money to all parliamentary political parties from 2007 to 2013 were extracted. The resulting list of companies was compared to those contract winners present in the two abovementioned databases to see if there are any matches.

2. Overview of the data

2.1 *Public procurement contracts - observations*

Around 440,000 award notices were extracted from SEAP resulting in a database consisting of 6064²⁹ contracts above the 1 million euros³⁰ threshold won by 1484 companies in the period 2007-2013. Contracts with missing data were excluded. We focused on all public procurement under 44, 45 and 71 CPV divisions, 557 framework contracts included. Most of the contracts (94.7%) imply works, while 5.3% are public procurement contracts for supply of goods or services. The final database comprises 53% of the overall value of public procurement in the construction sector and over 68% of overall value of EU funded public procurement in the construction sector³¹.

Almost a third of all contracts won in the public construction sector also received external EU financing (1905 out of 6064 contracts, see **Table 12**). It must be noted that the award notices contain unstructured (heterogeneously filled in) information regarding types of EU funding which has not been processed. Still, one could observe that besides the Structural Funds and the Cohesion Fund, other sources of financing included the European Bank for Reconstruction and Development, the European Investment Bank, the Schengen Facility or the pre-accession instruments (PHARE, ISPA and SAPARD)³².

The practice of single bidding was found in around 21.4% of the cases, meaning one out of every five contracts was won by single bidders. Also, one out of every 7 contracts was awarded to official donors of political parties (**Table 12**). Although international firms have not won many contracts over the years (under 8%), as mentioned before in section II.3, on average they were awarded a third of the total value of EU funded contracts during the researched period, reaching a share of 42.6% in 2013 (see **Figure 9**).

²⁹ The discrepancy between the high number of award notices and the contracts included in the database resides in the fact that most of the awarded contracts do not exceed 1 million euros.

³⁰ The contract values have been exchanged into EUR using an average monthly exchange rate. Inflation was not taken into account.

³¹ The percentages are probably even greater, as we operated downwards corrections on the value of contracts.

³² Details on PHARE, ISPA and SAPARD can be found at <<http://ue.mae.ro/en/node/456>>.

Table 12. Aggregated data on the number of contracts

	Total no. of contracts	EU contracts	Single bidding contracts	Won by donors to political parties	Won by international companies
Public procurement contracts	6064	1905	1297	890	446
From this number: framework contracts	557	3	63	62	3

Source: own calculations

EU funded contracts recorded a much smaller number of single bids, although the year 2011 is a notable exception. Almost half of the contracts in this category received European funding in the respective year. Thus, **one out seven EU funded contracts was awarded non-competitively through single bidding, as compared to one out of 4 in the case of nationally funded contracts**. Also, the combined value of awarded contracts that received EU funding is quite large, exceeding one third of the total value of all contracts in the database (Table 13).

Table 13. Database description

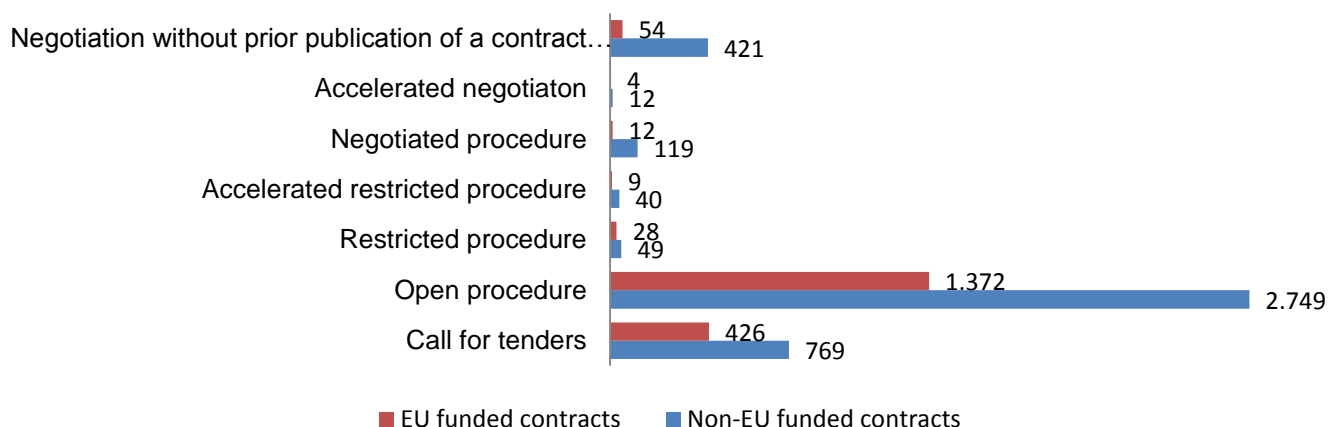
	2007	2008	2009	2010	2011	2012	2013	All years
Total no. of contracts	823	847	765	773	1124	881	851	6064
Total no. of EU funded contracts	45	76	195	298	548	414	329	1905
Total no. of contracts with single bidder	230	224	152	175	267	156	93	1297
Total no. of EU funded contracts with single bidder	13	16	21	52	105	34	18	259
Combined value of awarded contracts (million EUR)	2998	4374	4094	3744	7644	5044	4518	32 417
Combined value of awarded contracts that received EU funding (million EUR)	282.8	523.6	951.5	1321.2	3699	2653	2598	12 029.6

Source: own calculations

The award criterion for all procedures was in 46.3% of the cases “the lowest price”. Instead, contracts receiving European funding were awarded at “the lowest price” in 37.4% of the cases, the rest being awarded based on “the most economically advantageous” criterion. Also, 1 out of every 31 contracts was awarded at a price exceeding the estimated value of the contract and 1 out of every 19 contracts were awarded exactly at the estimated price³³.

Most of the contracts have been awarded through the open procedure – any company fulfilling the criteria stated in the SEAP notice could submit an offer. This is the case for EU funded contracts as well. However, non-competitive procedures such as types of negotiation or restricted accelerated procedure are less frequent in the awarding of contracts that receive European financing, as opposed to nationally funded contracts (**Figure 10**).

Figure 10. Procedures used in awarding PP contracts



Source: own calculations

2.2 Contracting Authorities

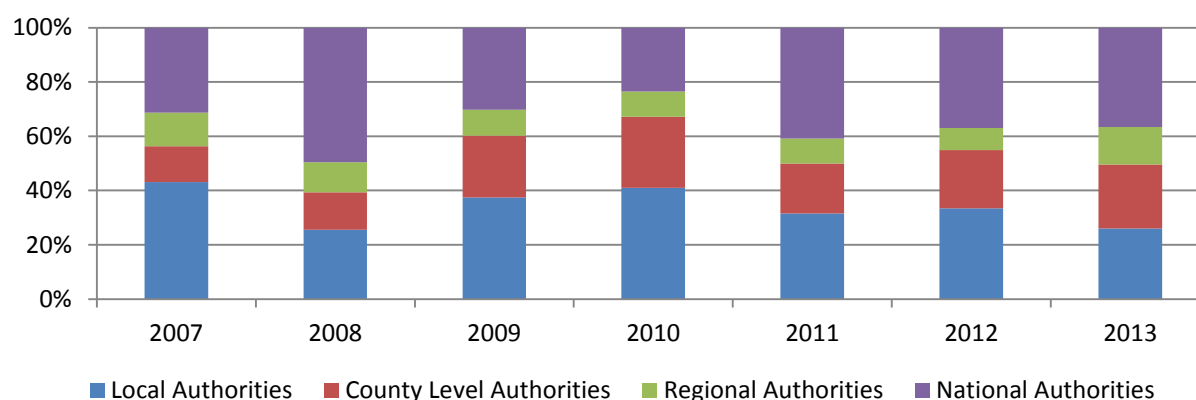
Romania has several layers of public administration, which cannot be easily assigned to local or central government. At the same time, several state entities, such as autonomous entities (*autonomous regies*), state companies or partially owned state companies, may operate at different geographical levels. Therefore, we assessed who the contracting authorities are first by

³³ There were 4883 contracts and framework contracts for which the estimated value was filled in.

territorial division³⁴ (and territorial effect of public contracts), then by major types of contracting authority³⁵.

Out of a total of 1509 contracting authorities, almost 74% are local authorities - 1115 city or town halls, local councils, schools, hospitals and state companies that operate in towns. Over 15% of these contracting authorities are present at county level while regional and national authorities represent each around 5-6% (88 regional contracting authorities and 76 national contracting authorities). Naturally, local and county level authorities combined account for most of the contracts (between 50% and 70%). Therefore, most of the awarding procedures are being completed at sub-regional level. However, by taking into account the value of contracts, one can observe that national authorities seem to be the main awarding entities, especially in pre-electoral years such as 2008, 2011 and 2013 (**Figures 11 and 12**).

Figure 11. Contracting Authorities by contract value

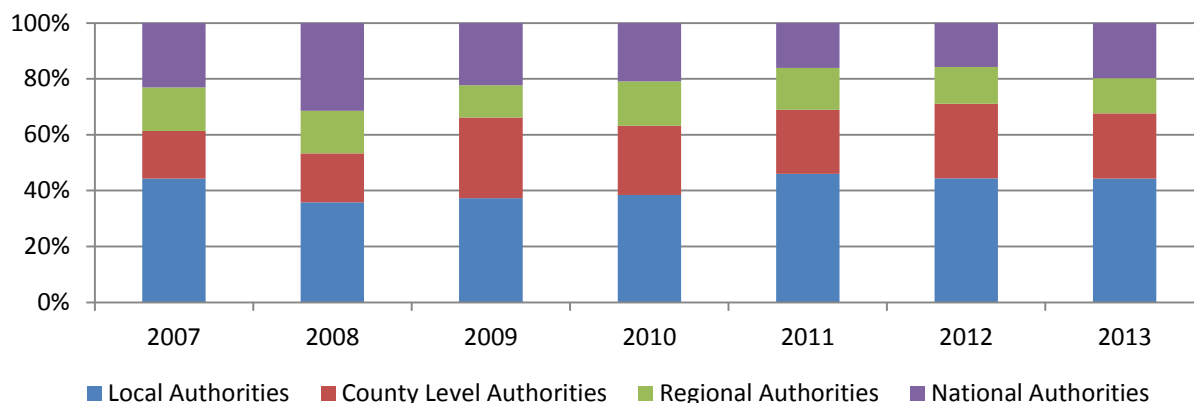


Source: own calculations

³⁴ The first classification takes into account different administrative structures by their activity identified geographically. The local level includes municipalities, towns and villages, each with their own elected mayors and local councils that award public contracts separately. The next layer refers to county level entities such as elected county councils, de-concentrated public services of ministries and government appointed prefects, as well as to the Romanian capital, Bucharest. Schools and hospitals and other public entities that are not local or central government were assigned to the two abovementioned levels. Most of the regional contracting authorities are state companies or partially owned state companies and universities. Finally, the national authorities category covers central government and state companies or partially owned state companies that operate at national level.

³⁵ The second classification refers to different types of state entities: after the fall of communism state-owned companies were reorganized in so-called autonomous regies (AR) and state companies or partially state-owned companies (Comp.) supplying public services. Other types of local government taken into account are the city and town halls and local councils (CH&LC), and county councils (County C.). Plus, we considered as being important categories of contracting authorities the following: de-concentrated services of the central government present at county level (Deconc.), central government (Central G.) and special entities active in the public road infrastructure sector – CNADNR (who is also a state company) and the so-called road and bridge departments that are active at county level (Road D.).

Figure 12. Contracting Authorities by number of contracts



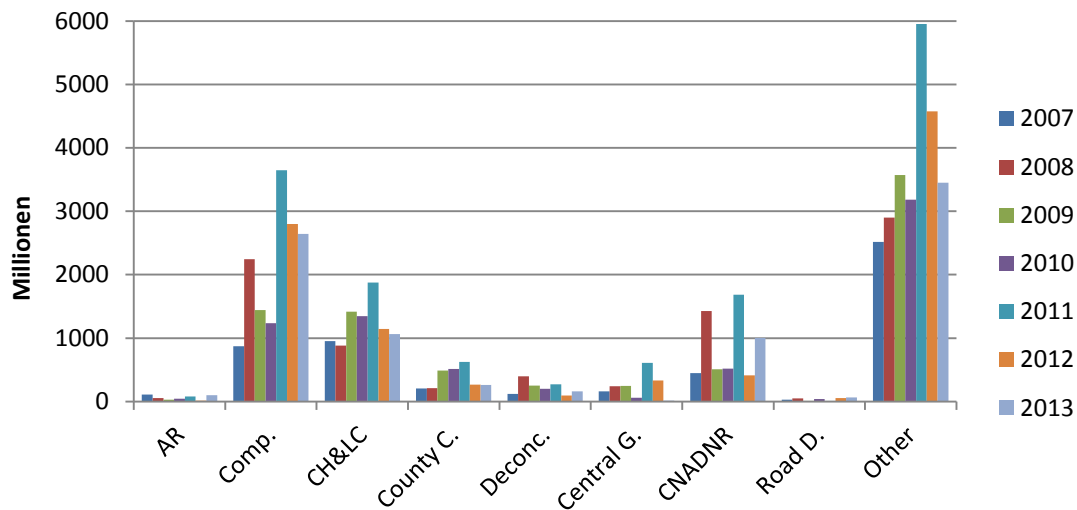
Source: own calculations

Among the most frequent public authorities awarding public procurement contracts there were five entities that signed over 100 contracts in the researched period: the Romanian National Company of Motorways and National Roads (CNADNR, 444 contracts), the Bucharest City Hall³⁶ (118 contracts), the National Housing Agency (110 contracts) and two gas national companies (over 100 contracts). Bucharest road and public domain administrations followed closely (under 100 contracts). Although, on average, there were 3 contracts per public entity, in absolute numbers 941 contracting authorities have signed only one contract surpassing the 1 million euro threshold in the researched period, while 433 entities awarded between 2 and 9 contracts. The database recorded a number of 118 contracting authorities awarding 10 to 39 contracts and 12 public entities awarding between 40 and 81 contracts. Besides national authorities, large city halls such as Brasov, Timisoara, Cluj Napoca or Iasi awarded over 30 contracts.

The main public entities in charge of road infrastructure at the county level, the road and bridges departments, are not very active actors in awarding over 1 million euro procurement projects in the construction sector (**Figures 13 and 14**). Also, the autonomous regions and central government are not important players. Instead, public companies, CNADNR, city halls and local councils awarded many contracts amounting to hundreds of millions of euros from 2007 to 2013. The pre-electoral year 2011 stands out in terms of the number and value of awarded contracts at local level (city/town halls and local councils).

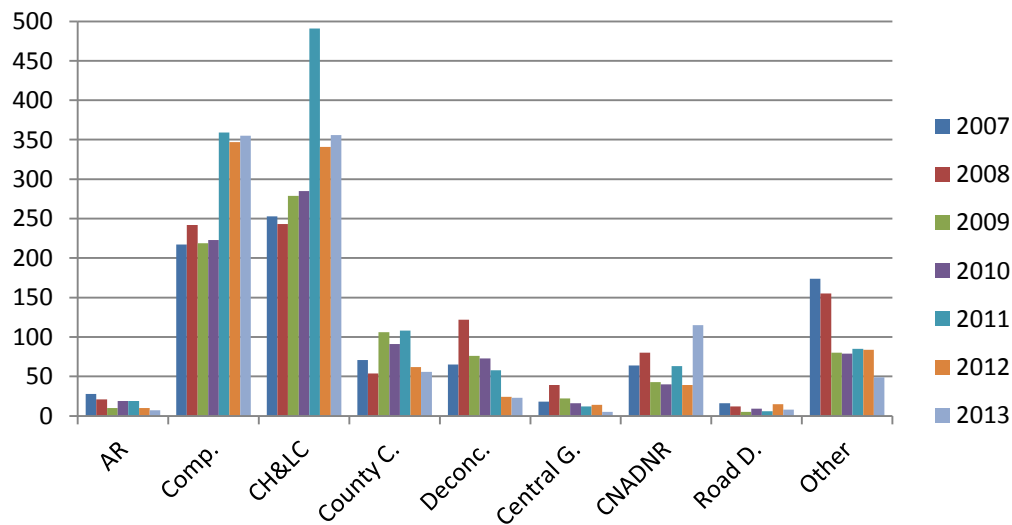
³⁶ The Bucharest City Hall was among the least transparent institutions to which SAR sent FOIA requests. It persistently refused to give any access to the annual public procurement plans or public procurement contracts.

Figure 13. Contracting Authorities by contract value (EUR)



Source: own calculations

Figure 14. Contracting Authorities by number of contracts



Source: own calculations

Legend:

- **AR** : autonomous regies
- **Comp.** : fully or partially state-owned companies
- **CH&LC**: city/town halls and local councils
- **County C.** : county councils
- **Deconc.** : deconcentratred public service departments
- **Central G.** : central government
- **CNADNR**: Romanian National Company of Motorways and National Roads
- **Road D.** : road and bridges departments awarding contracts in the road infrastructure sector at local and county level

2.3 Winner Companies³⁷

The construction sector is one of the main recipients of large public procurement contracts, as infrastructure works are highly expensive. As mentioned in section II.3, a great number of companies are active in this sector. Plus, several EU operational programmes involve financing infrastructure development. Thus, 46.5% of total winning companies in the construction sector were awarded EU funded contracts. **Table 14** shows also that most of the international companies operating in Romania win EU funded projects (107 out of 145).

Table 14. Aggregated data on the number of winner companies in PP (construction sector)

	Total PP winners	EU project winners	Single bidders	Donors to political parties
Total no. of companies	1484	691	580	156
From this number: International companies	145	107	61	2

Source: own calculations

It should be noted that among all 1484 winners, **17 firms are owned by individuals who are constantly present in Forbes top 100 richest businessmen**. Their private fortunes are known to have been built out of public infrastructure contracts.³⁸

The top 55³⁹ construction companies includes 46 nationally owned firms and nine firms with foreign capital. Four of them have shareholders or owners among the top 100 businesspeople (Besciu Dan, Umbrărescu Dorinel, the Butuza family and Istrate Corneliu). Most of the companies were founded in the 1990s (41 firms out of 55). Instead, six Romanian subsidiaries of international companies began their activity in 2000 or in later years. In conclusion, the date of foundation indicates that mostly experienced companies tend to perform well in the construction sector. Also, international entities were present on the domestic market before EU accession.

The average share of public procurement in the turnover of each Top 55 company (when data was available) amounts to over a fifth of their total revenues. A small number of firms out of the 55 depend to a large extent on public funds (**Table 15**). This might indicate that politically connected companies are not necessarily among the top performers of the construction sector, in terms of turnover. Still, out of the investigated fifty-five firms, eight have donated funds to political parties.

³⁷ Unique companies were identified as the winner company or as the leader of a winning consortium of a public procurement contract. Out of the 6064 contracts, 1022 were awarded to consortia. Also, well known leaders in the construction sector that operate both through international firms and national subsidiaries were given the same ID.

³⁸ The most well-known businessmen in the construction sector are Tecar Ioan, the Tender family, Costan Calin, Istrate Corneliu, Cornu Georgica, Casuneanu Costel, Iordache Nelu, the Butuza family, Umbrărescu Dorinel and Besciu Dan.

³⁹ The 55 construction companies under scrutiny are taken from the top 100 construction companies in 2013 depending on their turnover. Only companies operating in the public procurement market above the 1 million Euros threshold for awarded contracts and for which we managed to find information were taken into consideration. Thus, we selected 55 firms. Also, when computing the share of public procurement contracts in the companies' turnover, we excluded the contracts won in consortia (as there is no information on each partners' work load and price).

Table 15. Share of public procurement contracts in Top 55 companies' turnover

	2008	2009	2010	2011	2012	2013
Mean	17.7%	20.1%	22.7%	23.3%	23.3%	20.9%
Median	5.9%	8.6%	17.3%	16.9%	9.8%	6.0%
Share of >=60% (no. of firms)	4	3	6	4	8	5

Source: own calculations

Last but not least, the top 55 recorded high profit rates in 2008 – nine Romanian firms registered over 20% profit rate. International firms, instead, operated at a loss. The years 2009 and 2010 followed the same trend at a smaller scale, yet international companies started to show profit rates of over 10% (2 cases in 2010, 3 cases in 2013). A contraction was recorded in 2011, as five international firms registered losses and the highest profit rate did not reach 7% (as opposed to national companies who continued to record return rates of over 10% in thirteen of the forty-six cases). Only in 2013 do three international firms find themselves among the top performers, with a profit rate of over 10% (see **Appendix 1**).

3. Research Results

3.1 Market shares, single bidding and politically connected private firms

Firstly, we investigated if there is market concentration indicating non-competitive contract awarding. In computing yearly market shares for each of the unique winners we excluded the framework contracts as they are signed for long periods of time, they involve large sums and they do not imply that the whole amount be used up by the end of the period. We did not have access to subsequent contracts with full information, therefore the SEAP database was reduced to 5507 contracts above 1 million euros.

For each year of the researched period, the four-firm concentration index was under 25%, while the Herfindahl-Hirschman Index⁴⁰ registered extremely small values – under 227 out of a maximum of 10,000. Therefore, we conclude that there is no market concentration in the public procurement construction sector.

Secondly, we needed to establish how widespread single bidding is and under what circumstances it occurs. The data gathered points to the fact that single bidding is widespread at the local level and in the case of state companies (**Tables 16** and **17**). The practice has been declining for the past few years (see **Table 13**). Consequently, the number of single bidders has decreased, from 153 in 2007 to 69 in 2013. An exception is the year 2011 when the highest number of single bidders was recorded – 183.

⁴⁰ The Herfindahl-Hirschman Index is used in assessing the level of concentration on a certain market. It aggregates the squared market shares expressed as a percentage (not in absolute value). Thus zero means perfect competition while 10 000 indicates a monopoly.

In 283 of the cases stretching from 2007 to 2013, single bidder contracts were awarded to politically connected companies (political donors and firms known to have political ties), accounting for 21.8% of the total number of single bidding contracts. In contrast, party donors and politically connected firms won on average 167 contracts per year. The year 2011 is yet again an exception since 221 such contracts were awarded.

Table 16. Single bidding contracts awarded by authorities

	Local Level	County Level	Regional Level	National Level
Single bidders	521	259	113	341

Source: own calculations

Table 17. Single bidding contracts awarded by different types of contracting authorities

	RA	Comp.	CH&LC	County C.	Deconc.	Central G.	CNADNR	Road D.
Single bidders	33	395	460	110	72	28	94	16

Source: own calculations

In order to explain the occurrence of single bidding, we run some simple logistic regressions. Model (1) and (2) in the regression table below (Table 18) draw upon the database containing information on over 1 million euro contracts extracted from SEAP. Model (3) draws upon the manually constructed road infrastructure database that includes contracts which have different values, above and below 1 million euros. Statistical analysis indicates that single bidding is negatively significantly associated with EU funded projects in both model (1) and (3). In the first case, winning a contract with European funding is associated with a decrease of 52.7% in the probability of having won by single bidding. Therefore, the results point to the fact that single bids are more common in winning state budget contracts. EU funded contracts, in contrast, are awarded on a more competitive basis. Moreover, being a politically connected firm leads to a 21.2% higher probability that the firm in question won via single bidding – there is a significant association between having a political connection and winning through a single bid.

Table 18. Logistic analysis for Single bidding with different constraints as explaining variables

Dependent variable: Single bidding						
Independent variables	(1)		(2)		(3)	
	Coeff.	Exponentiated coeff.	Coeff.	Exponentiated coeff.	Coeff.	Exponentiated coeff.
EU Funding	-0.748*** (-9.87)	0.473*** (-9.87)			-0.480* (-2.20)	0.618* (-2.20)
Political Connection			0.192* (2.51)	1.212* (2.51)		
Constant	-1.100*** (-30.72)		-1.340*** (-38.01)		-0.0487*** (-11.44)	
Observations	6064		6064		2448	
pseudo R-sq.	0.0170		0.0010		0.0016	

Logit estimations; z statistics in parentheses; * p<0.05, ** p<0.01, *** p<0.001;

Note: Exponentiated coefficients give the odds ratio (the ratio by which the dependent variable changes for a unit change in an independent variable).

The data on construction sector contracts over 1 million euros points to the fact that there are privileged private firms who win far too many contracts compared to the average. Such companies are also political party donors or known to have political connections (Delta ACM 93, Hidroconstructia, Tel Drum, Cast, Selina, Tehnodomus, Tmucb, Tehnic Asist, Victor Construct, Deltacons, Pa&CO or Romstrade). Other frequent winners include Top 55 companies, such as Confort, Vega'93, Tehnologica Radion, Tancrad, Spedition Umb, Strabag, Straco Grup, Inspet, Condmag, Dafora, Technocer, Constructii Erbasu, Iasicon etc.

Privileged firms are awarded mainly nationally funded contracts (two out of three contracts are non-EU funded, from a total of 1175 contracts from 2007 to 2013). Nevertheless, the number of awarded contracts is significantly associated with the existence of political connections in the cases of both only nationally funded contracts and EU funded contracts. Even more interesting, international companies are negatively significantly associated with the number of non-EU funded contracts, while being significantly associated with the number of EU funded contracts. International companies are more active on the EU funded public procurement market and seem to be either discriminated against or not competing on the nationally funded procurement market. Finally, the number of contracts won can be explained by political connections and the frequency of single bidding in pre-electoral years in almost 45% of the cases (Table 19).

Table 19. OLS analysis for number of awarded contracts

	Only Non-EU funded			Only EU funded			All contracts
	Dependent variable:			number of awarded contracts			
Independent variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Political connection	0.359*** (3.75)			0.281*** (3.68)			0.282* (2.10)
International company			-0.602*** (-10.02)			0.415*** (6.19)	
Single bidding frequency							1.286*** (13.89)
Constant	1.112*** (47.16)	0.801*** (24.49)	1.217*** (46.56)	0.573*** (30.16)	0.518*** (24.67)	0.581*** (28.22)	1.169*** (24.82)
Observations	3090	3090	3090	3090	3090	3090	1377
R-sq.	0.0089	0.297	0.015	0.0084	0.0331	0.0111	0.4486

Robust OLS regression estimations; t statistics in parentheses; * p<0.05, ** p<0.01, *** p<0.001;

Note: the OLS regression for all contracts takes into account the pre-electoral years 2007,2008 and 2011

3.2 Evidence of agency capture

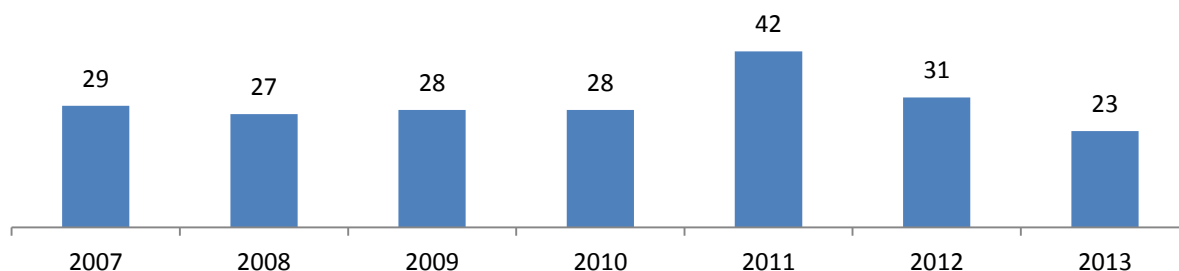
Corruption is abuse of authority for private interest. In order to trace the abusers, we investigated whether or not one private contractor obtained a disproportionate share of contracts from a public agency. Framework contracts were again omitted. As in the case of market shares, they would have distorted the information regarding yearly total volumes.

We aggregated the yearly total value of contracts awarded by contracting authorities and computed the share of each winner in relationship with the respective contracting authority per year. We defined agency capture as being the case when the share of the total sum awarded by one contracting authority during a year to only one company surpasses 50%, if the contracting authority awarded at least three contracts in the respective year.

In accordance with this definition, the resulting database recorded a number of 208 capture situations from 2007 to 2013. The pre-electoral year 2011 was again the exception in the average annual capture instances (see Figure 15). Both national firms and international firms were among the companies that won large portions of public procurement contracts (12% of

captures were made by 22 international companies). Party donors and other politically connected firms (a total of 23 different companies) accounted for 25% of the capturers.

Figure 15. Number of agency captures by year

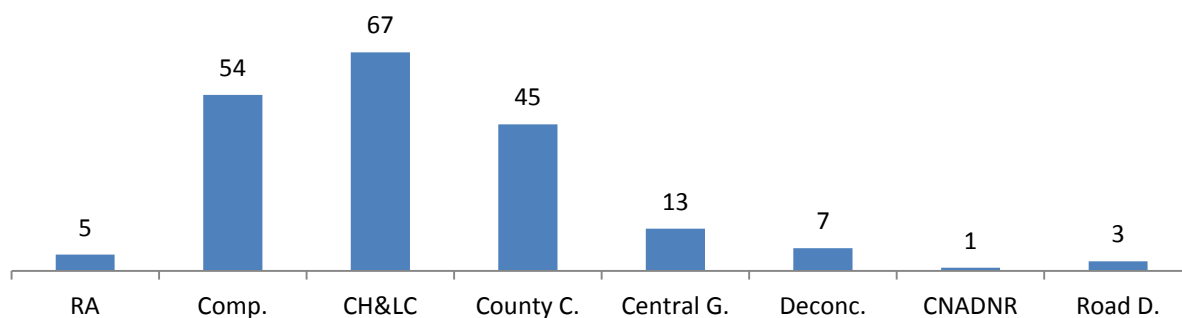


Source: own calculations

Most of the captured agencies are contracting authorities at sub-regional level: a total of 77 captures were registered at local level and 67 at county level, amounting to almost 70% of all captures. At least one fifth of the capturing involved restrictive awarding procedures.

An interesting result of the agency capture analysis is illustrated in Figure 16. Although county councils accounted, on average, for only a tenth of the awarded contracts (9.1%), they are very visible in the case of captured agencies. County councils represent 21.6% of captures, after city and town halls and local councils and state companies.

Figure 16. Agency captures by type of contracting authority



Source: own calculations. **Legend:** **AR:** autonomous regions **Comp.:** fully or partially state-owned companies **CH&LC:** city/town halls and local councils **County C.:** county councils **Deconc.:** deconcentrated public service departments **Central G.:** central government **CNADNR:** Romanian National Company of Motorways and National Roads **Road D.:** road and bridges departments awarding contracts in the road infrastructure sector at local and county level

Logistic analysis indicates that agency capture is significantly associated with both single bidding and with politically connected firms. Instead, the same association is not significant in the case of agency capture involving only contracts funded by the European Union (Table 20).

Table 20. Logistic analysis for Agency capture with different constraints as explaining variables

	Full sample of unique captures/non-captures		Only EU funds	
	Dependent variable:		agency capture	
Independent variables	(1)	(2)	(3)	(4)
Single bidding	0.666*** (4.16)		0.1325 (0.47)	
Political connections		0.344* (1.98)		0.336 (1.31)
Constant	-3.245*** (-32.57)	-3.127*** (-32.48)	-2.936*** (-24.61)	-2.993*** (-23.72)
Observations	4679	4679	1713	1713
pseudo R-sq.	0.011	0.0024	0.0003	0.0025

Logit estimations; z statistics in parentheses * p<0.05, ** p<0.01, *** p<0.001; std. errors are clustered by agency

3.3 Other indicators of corruption risks: contract addenda and number of requests for clarifications

The manually constructed database with contracts pertaining to local road infrastructure sector revealed some interesting results. First of all, we gained access to correct information regarding contract addenda. Only 1 out of 13 contracts for which an addendum was signed was funded by the EU (from a total of 233 such contracts). The practice of modifying contract value or other, technical specifications has been thoroughly investigated by the DNA as it is one of the main methods through which public resources are wasted. Subsection 3.5 of this chapter provides an illustration of this practice.

Secondly, the number of requests for clarifications is an important aspect to consider and may be viewed as a corruption risk indicator signalling tender specifications problems. It may be that contracting authorities do not have the administrative capacity to issue well-designed specification documentation. Alternatively, it may be that the documentation is intentionally unclear so as to allow favoured firms to win procurement awards procedures.

There is a negative significant association between the number of requests for clarification and single bidding on the one hand, and contract addendum on the other hand. In competitive procedures, with more than one bidder, there will be more requests for clarification from various

competitors. Also, many clarifications will lead to a clearer and more correct contract, for which there is no need to sign an addendum. The struggle to win European funded contracts can be translated in a higher number of requests for clarification – the variable being significantly associated with EU funding (see Table 21).

Table 21. OLS analysis on the number of requests for clarification

Dependent variable: number of requests for clarification	
Independent Variables	
Single bidding	-2.407*** (-13.26)
Contract Addendum	-0.666* (-2.24)
EU funding	2.875** (3.13)
Constant	2.696*** (19.98)
Observations	1007
R-sq.	0.102

*Robust linear regression estimations; t statistics in parentheses; * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$;*

3.4 Particularistic links at the local level in the road infrastructure sector

The investigation of the 215 procurement boards presidents' (considered as the main award givers) statements of interests and assets from 2008 to 2013 who are present in the FOIA database described in section IV.1 brought about the results presented below.

Four procurement boards' presidents in four different counties (Mures, Prahova, Neamt, Calarasi) had a first-degree family member employed in a company which won a road infrastructure contract at least once. Board presidents did not directly own/were not associates in companies that won road infrastructure contracts in the period surveyed. According to the available data, out of these four cases, two board members were presidents when companies considered having ties to them won a public procurement contract. One of these two cases pointed to the fact that the board president, also a technical director within the county council,

was for a short period of time also the director of the county council-owned local company that won public procurement contracts⁴¹.

Eight board presidents were also members or presidents or the shareholders' general assembly of the so-called Roads and Bridges Companies – local construction companies which are fully or partially owned by the county councils. According to the available local data, these companies won, by themselves, 13% of the total number of contracts from 2007 to 2013. One should not automatically consider the presence of board members in these companies' general assemblies as an indication of corrupt procurement procedures. Awarding contracts to such companies can also have a social underpinning since local jobs and economies depend on their existence. Five board presidents from four counties (Mures, Prahova, Braila, Brasov) have been questioned/indicted by the DNA or sentenced to prison⁴² under the accusation of having favoured certain companies in winning public procurement contracts. One was released and two cases do not refer to the road infrastructure sector. In Prahova County, one of the board presidents is accused of having favoured three construction companies that won 15 contracts exactly when he was presiding over the procurement board. The FOIA database constructed for this report does not contain an important number of procurement contracts awarded by the Brasov County Council because these were seized by the DNA in an ongoing investigation. In December 2014, the Brasov County Council President, together with a member of the Parliament, five local public servants and two businessmen, were indicted for not only having favoured two construction companies, but also for increasing the initial contracts' values even by 1000% (DNA press statement no. 1822/VIII/3, 17 December 2014). Five board presidents from five counties (Tulcea, Olt, Neamt, Sibiu, Teleorman) deservedly received negative press pertaining to their connections with road infrastructure companies. In Tulcea County, the companies accused of having been favoured won 17 contracts when the person mentioned by the local press presided over the procurement board. Regarding the investigation into the companies of County Council Presidents and the frequency with which they won procurement contracts, we found that only three companies belonging to them or to their first degree relatives were in such a situation. The three companies in question won 16 contracts in six different counties. In conclusion, from the data we gathered, direct links between companies and award givers present in procurement boards are not pervasive and apparent. It is more common that the owners or administrators of favoured companies enjoy personal ties with either one of the procurement board members, the County Council (vice)president or the prefect. The latter two could exert their influence over the board and steer its decision in the preferred direction and, as a result, receive kickbacks from the winning companies. This picture points to the importance of local independent media outlets which monitor the activity of state entities in the whole public procurement sector, not just in construction.

⁴¹ The case of this particular company was also in the local media spotlight because of the tense situation within the company's shareholders' general assembly that resulted in a complaint filed at a local DNA office. More specifically, the shareholders' general assembly refused to approve payments ordered by the County Council for performing road construction works which had been already finalized (Nechita, 2014).

⁴² Former director of the County Roads and Bridges Department within the Mures County Council was sentenced to three years in prison (suspended sentence) for bribe taking (DNA press statement, penal decision 3811, 20 November 2012).

4.5 Particularistic links – case studies

While single bidding and agency capture can be red flags for corruption risks, the situations discussed in the case studies below indicate that politically connected companies will find their way in winning large public procurement contracts. Making friends with the right people, sponsoring political parties and supporting the right politically connected persons who are given important public offices are some of the methods through which businessmen attempt to ensure their companies thrive in the construction market.

CASE STUDY I

When referring to the issue of defrauding EU funds in the construction sector through public procurement, a case in point is that of Nelu Iordache – owner of the firm ROMSTRADE and one of the wealthiest Top 300 businessmen with an estimated fortune of 70-75 million euro in 2012 – and the contract he won for the construction of the 22 kilometre segment of the Arad-Nadlac highway.

Nelu Iordache built his wealth in the 1990s by winning snow removal contracts financed by the Ministry of Transport. In the early 2000s he moved into the road infrastructure business and through his connections in the ministry and the National Air Transport Company, he started his own air company, Blue Air. Iordache entrusted the management of his company to Gheorghe Racaru, a former public official, head of the management board of the national airline company, TAROM. Ruxandra Brutaru, Blue Air's former marketing director and daughter of a former TAROM director, was named in 2007 by the Minister of Transport at the time, Ludovic Orban (Liberal Party), as TAROM's deputy director. Brutaru was accused in 2008 of purposefully refusing to participate in a public tender organized by the Romanian Post for airmail services (Befu, 2012). The 44.8 million Euros contract was won by the single bidder, Blue Air, that, as was later pointed out by the Court of Accounts, caused a damage of almost 10 million Euros because payments were made for non-existent planes and flights (Court of Accounts Annual Report, 2010). Despite being accused of faulty management, when Radu Berceanu (Democratic Liberal Party) came at the helm of the Ministry of Transport, he kept Brutaru as TAROM's CEO (Florescu, 2012). She quit in 2011 leaving behind an estimated 100 million Euro financial damage (Tiron, 2011). Nelu Iordache's close ties with the Liberal Party were evident in 2008 when then Prime-Minister Calin Popescu Tariceanu visited, together with Transport Minister, Ludovic Orban, Iordache's hometown in a county close to Bucharest in order to assess the possibility of building a new airport. Although plans to carry out a feasibility study were announced, no action was taken because the ministry did not actually dispose of the necessary money for a project which had no technical, economic or social justification (Wall-Street, 2009).

In 2011, Iordache built a consortium with two other companies, MonteAdriano Engenharia e Construção SA – which had experience in highway construction – and SC DONREP

CONSTRUCT SRL – a company with dubious ownership⁴³ and won the Arad-Nadlac 115 million euro contract from the CNADNR⁴⁴. Although the deadline was in late 2012, in early June 2012 the construction work was only at about 4%, but the payments to ROMSTRATE reached approximately 16.9 million euros (around 20% of the contract) because of the alleged complicity of some CNADNR employees. Criminal charges were brought against lordache in early December 2012 by the DNA. After lordache's arrest and following the mass termination of its CNADNR contracts, ROMSTRATE filed for bankruptcy. In March 2014, the value of claims coming from the company's creditors, the majority of which are public entities, was established at 622 million euros⁴⁵.

The prosecutors' indictment pointed out that the advanced payments earmarked for highway construction were used not only to pay off outstanding debts incurred by ROMSTRATE and other companies controlled by lordache, but also for personal use. Ironically, European funds for the Arad-Nadlac project helped finance work done by several companies in other construction projects also funded with European money⁴⁶. This scandal was among the reasons for which, in October 2012, the EC decided to pre-suspend three operational programmes, including the one on transport infrastructure. The audit missions found that – at the management authority level – public procurement procedures were faulty, financial management was defective and the prevention and detection practice with regard to fraud and conflict of interest was inadequate (Pop, 2012).

Nelu lordache's company was accused by the press and, following his arrest, by Prime-Minister Victor Ponta, as having been offered sweetheart deals by Liberal and Democrat-Liberal ministers of Transport, the Minister of Regional Development and Tourism, Elena Udrea (Democrat-Liberal Party), and the CNADNR in exchange for his contributions to the Liberal Democrats' electoral campaigns (Mediafax, 2012). According to the information available on SEAP, from 2011 to 2012 – a time period roughly coinciding with Elena Udrea's mandate (23 December 2009-9 February 2012) at the Ministry of Development and Tourism (MDRT) –, ROMSTRATE won three contracts worth 428 million Euros. Consequently, he was one of the main beneficiaries of the National Infrastructure Development Program (PNDI) which sought to complement the European operational programmes aimed at modernizing county and local roads, building water and sewerage networks, waste water treatment facilities, renovating

⁴³ DONERP had just 4 employees in 2010 and 0 employees in 2011, the year the Arad-Nadlac highway construction started (Romanian Trade Register). The shadow administrator of DONREP was not an official associate, but one of lordache's acquaintances, named Marinescu Bogdan Olteanu.

⁴⁴ During the contract award phase, ROMSTRATE's offer was 24% higher than the cheapest counter-offer, but the price criterion represented 30% of the overall score.

⁴⁵ The largest creditors are BCR (68,1 million Euro), Astra Asigurări (52,9 million Euro) and EximBank (37,2 million Euro), but also the Municipal Town Hall of Bucharest and CNADNR (Ionascu, 2014).

⁴⁶ Among the various payments made, some examples include 50.000 lei to SC Turbomet SRL, for work on the Caracal Belt; 100.000 lei to SC Euromontaj SRL, for DN 67 C modernization; 100.000 lei to SC Record SRL in Bistrița Năsăud for cement on a rehabilitation site in Bistrița; 506.306 lei to SC Lafarge Agregate Betoane SRL for delivery of fillers for Arad-Nădlac, when in fact they were for delivering materials to the Sieu-Odorhei project, DJ 151 Bistrița and Baru –Hațeg; 50.000 lei to SC Construcții Ramis SRL, for civil construction work at School number 16 in Bucharest.

schools and kindergartens and multiannual environmental and disaster management programmes.

During Ludovic Orban's (National Liberal Party) tenure in the Ministry of Transport (5 April 2007-22 December 2008), ROMSTRADÉ's turnover took off⁴⁷ thanks to the 400 million euro contracts he and his company managed to win. Iordache's success continued under the following three ministers of Transport, all belonging to the Democrat-Liberal Party. Under Radu Berceanu's tenure (22 December 2008-3 September 2010), ROMSTRADÉ registered its highest turnover, over 260 million euro. The company benefitted from 2009 to 2012 from the most lucrative contracts with the Romanian state since their value exceeded 1 billion euro under Anca Boagiu's mandate (3 September 2010 - February 9 2012) and of her successor, Alexandru Nazare (February 9-May 9 2012) at the Ministry of Transport and under Elena Udrea's mandate at the MDRT.

According to the data available in SEAP, from 2007 to 2012, ROMSTRADÉ won from the CNADNR 25 contracts, the most valuable (343 million euros) being the Transalpina highway⁴⁸, which remains unfinished due to ROMSTRADÉ's insolvency claim, filed in December 2012. Consequently, the construction work for this highway was abandoned and traffic halted until March 2015, resulting in state damages estimated at 100 million euros (Digi24, 2015).

During his arrest, he made statements which led to the investigation of two political figures: Dragos Benea (Social Democratic Party), Bacau County Council President⁴⁹ and Ovidiu Silaghi (National Liberal Party), former Minister of Transport for a brief period in 2012. Silaghi has managed to elude to this day being criminally prosecuted by taking advantage of his national and even European parliamentary immunity⁵⁰. The charges brought against him are of influence peddling while in office at the Ministry of Transport whereby Silaghi offered to convince high ranking CNADNR employees not to annul Iordache's on-going contracts and to continue delivering payments although some construction works were in delay in exchange of introducing

⁴⁷ In the year prior to Orban's investiture, ROMSTRADÉ's turnover was around 14,5 million Euro. The company registered its highest turnovers in 2007 (195,6 million Euro), 2008 (218 million Euro) and 2009 (267,3 million Euro).

⁴⁸ In May 2014, the Transalpina investigation, which resulted from splitting the Arad-Nadlac case, led to new criminal charges against Iordache. In this case, public servants working for a local CNADNR branch accepted to reimburse ROMSTRADÉ costs incurred from fictitious construction works and materials which had not been actually bought. The damage estimated at 5 million Euro was recovered during the prosecution (DNA press statement no. 606/VIII/3, 16 May 2014).

⁴⁹ In July 2009 the Bacau Airport was sub-licensed for 35 years to Nelu Iordache's air company, Blue Air (ROMSTRADÉ being its mother company), on the promise that the latter would invest in the airport's modernization. Suspensions arose because the company had rented two commercial spaces from Benea's close relatives and because Benea himself was a staunch supporter of Blue Air winning the concession contract. Following the EU funds defrauding scandal and ROMSTRADÉ's insolvency, the concession contract was annulled, Iordache's air company was sued by the county council for unpaid debts and breach of contract since modernization works were minimal (Bogdanel, 2013).

⁵⁰ The evolution of Ovidiu Silaghi's indictment was a very sinuous one. In August 2013, Silaghi was accused by the DNA of influence peddling during his ministerial tenure and a request to lift his parliamentary immunity was sent to the Parliament. Silaghi used the common tactic of resigning from the Parliament so as to make the request null and void. Consequently, the DNA obtained the President's approval for starting a criminal prosecution, but from September 2013 to May 2014, the Liberal Party named Silaghi as a replacement to one of his party colleagues in the European Parliament. The latter failed to address the DNA's new immunity-related request and Silaghi was elected for another parliamentary mandate on behalf of the Social Democratic Party after having migrated from the Liberals (Attila, 2014).

new air routes via Iordache's air company to a local airport⁵¹. In addition, Silaghi also received 200,000 euro from Iordache in exchange of favouring the approval and continuation of his company's contacts within the CNADNR (DNA press statement no. 781/VIII/3, 12 September 2013).

CASE STUDY II

Costel Casuneanu is a steady presence in the Top 300 wealthiest businessmen with a net worth of 130 million euros in 2013, considerably less than in 2012 when his fortune amounted to 250 million euros⁵². By researching the Romanian Trade Register, one finds that Casuneanu moved closer to the political sphere not only by winning public contracts in road infrastructure and maintenance, but also through two of his business associates who later entered public service, one occupying a seat in Parliament and one in local administration. The businessman was a public supporter of the Social Democratic Party (PSD) by being a member of "Club 75"⁵³, a non-profit that aims to support social-democratic causes in Romania. He even entered into a dubious land transaction with then Bacau County Prefect and later PSD leader Viorel Hrebenciuc⁵⁴. However, Casuneanu has also been known to enjoy strengthening ties with other political figures. During the early 2000s, there was a series of transactions that took place between then Minister of Transport and later President Traian Basescu and Casuneanu⁵⁵, with the press speculating that this was a bribe from the PA&CO owner, who required several transport licenses (Gotiu, Popescu, 2014).

Casuneanu's interactions with politicians took a criminal turn in 2013 when he was sentenced to four years in prison (suspended sentence) for influence peddling in a case involving former PSD Senator Catalin Voicu, who was sent to prison for seven years on corruption charges. According to the DNA, in 2009 Casuneanu gave bribe money to Voicu for him to exert his influence over the chief of the Civil and Fiscal department of the High Court of Cassation and Justice (ICCJ), Florin Costiniu, such that he may convince his colleagues in the Administrative Court to favour PA&CO in a lawsuit against CNADNR (DNA press statement no. 183/VIII/3, May 2010). Moreover, in July 2014, he was indicted by the DNA on charges of giving a bribe to Bacau

⁵¹ Silaghi's request was allegedly aimed at supporting the electoral campaign of a person close to the minister and it resulted in a half a million Euro loss for the air company.

⁵² Casuneanu's business flourished between 1999 and 2004, when it reached an annual business turnover of 48,5 million Euro. His companies reached a peak between 2008-2009 and 2011-2012, when his businesses produced somewhere between 52 to 80,87 million Euro.

⁵³ "Club 75" was founded by 69 businessmen who contributed 75 million lei (about USD 3,5 million) to support the PSD in winning the 2000 presidential election. Other notable members, who have been or are prosecuted or convicted of corruption cases – are Sorin Tesu (former chief-of-staff in Prime-Minister Adrian Nastase's cabinet), former PSD member Șerban Mihăilescu (nicknamed Micky Bribe), and Aristide Roibu, former PSD treasurer.

⁵⁴ In 1992, Casuneanu was given property rights to a well-placed piece of forest (2,500 m²) in a sky resort by then Bacau County Prefect, Viorel Hrebenciuc. In less than a month after, Casuneanu sold 20% of the land back to Hrebenciuc's family for the mere sum of 25 USD (Gotiu, Popescu, 2014).

⁵⁵ In 2000, Basescu made some very advantageous land purchases in Bucharest. Simultaneously, a similar transaction takes place with a nearby land parcel, purchased by Casuneanu who paid approximately 225,000 USD, even though Basescu paid only 68,000 USD for his similar parcel, hence only a third of the total price paid by Casuneanu. In 2001, when Basescu was Mayor of Bucharest, he sold the same parcel to Gabriela Blaj (Casuneanu's sister-in-law and business partner) for around 3 million Euros. Basescu was investigated in 2004 for money laundering, but the file was closed after he became president (Stancu, 2011).

County mayor, Romeo Stavarache (National Liberal Party), after the latter requested money in exchange for releasing a construction permit needed by a company that won an EU funded project. The Stavarache case is also a case in point as to the method through which public contracts are given discretionally to handpicked businesses. The Liberal mayor is charged with asking several local businessmen for bribes in exchange for winning public contracts or, for those who were implementing projects, kickbacks in the form of a percentage of the contracts' values (DNA press statement no. 1110/VIII/3, July 2014; Bogdanel, 2014).

The modernization and expansion project of the Ploiesti West belt represents a case of awarding a public procurement contract financed through the state budget to a politically well-connected businessman active in the construction sector.

The public tender for the expansion and modernization of the Ploiesti West belt organized by CNADNR had four final offers which were evaluated on the basis of four criteria: price, quality of the work programme, equipment and execution timeframe. Costel Casuneanu's construction company, PA&CO International, won the 23.3 million euro contract for the 13-kilometre highway in late 2007. PA&CO breached the latter three criteria during the contract's execution, but blamed the CNADNR for not updating its feasibility studies to the new conditions on the ground (Etves, 2008; Etves, 2013). Both the value and the project's completion deadline changed in the following years. Through addenda to contracts⁵⁶ awarded through the least transparent procedure (negotiation without the publication of the participation notice) which entails the suspicion of intent to favour a particular company, the value of the construction works increased by 7.9 million euros in just two years and the project was finalized with a 9 months delay, in August 2010. In total, PA&CO received from CNADNR a total sum of 31.2 million euros for four lanes of the Ploiesti West belt⁵⁷. Considering that in the original tender the most expensive offer was 30.1 million euros, Casuneanu's offer and subsequent work ended up costing more public money. Although the overall price difference is not very large, the quality of the work done by PA&CO prompted the CNADNR to issue a public statement in November 2013 – the date when the portion of road was reopened to the public after being closed for repairs – whereby it deplored “major execution defects” and accused the company of being the “preferred client of the Democrat Liberal Party” (CNADNR press statement, November 2013).

Transport Minister to be Radu Berceanu (Democrat Liberal Party) declared, after PA&CO won the Ploiesti West belt project, that “PA&CO became a prime-ministerial company” (Cotidianul, 2008) since it began receiving more contracts under Prime-Minister Calin Popescu Tariceanu

⁵⁶ In July 2008, when the project was less than 50% completed, PA&CO was allocated a supplementary 180,333 Euros for project design services through an addendum to the contract. In July 2009, PA&CO received a further 7 million Euros via a new addendum. In December 2009, the company was allocated a further 739,000 Euros for supplementary works. Source: Official SEAP database.

⁵⁷ Costel Casuneanu also benefitted from expropriation money from lands owned in the vicinity of the construction sites he was servicing. His son had bought 10,000 m² next to the Ploiesti Belt which ended up being included in the construction site perimeter. As a result, his son was expropriated and given a compensatory sum of money. Also, in June 2014, Prahova County Council gave compensatory sums of money to him, his wife and PA&CO which amounted to nearly 50,000 Euro (Mediafax, 2014; Unturica, Ilie, 2014).

and then Transport Minister, Ludovic Orban, both belonging to the Liberal Party. However, after Berceanu's return to the ministry (22 December 2008 - 3 September 2010), CNADNR approved the contract addenda and payments to PA&CO which increased the overall contract value by almost 8 million euros. Berceanu re-named Dorina Tiron – who was accused of mismanagement and removed as CNADNR director during Anca Boagiu's (Democrat Liberal Party) mandate at the Ministry of Transport (Evenimentul Zilei, 2010) – as head of CNADNR, who, in turn, in March 2010 appointed Ovidiu Barbier as Coordinating Director of Detour Bypasses. Barbier was both director and associate in of the firm Maxidesign that was the beneficiary of several design projects awarded by CNADNR. Most importantly, Maxidesign was also the company that designed the entire Ploiesti detour belt, executed by PA&CO. Therefore, from March to August 2010, when the belt's inauguration was made by Prime- Minister Emil Boc, PA&CO's activity was monitored by Casuneanu's own designer.

Unlike the Nelu Iordache case, Costel Casuneanu's company did not suffer major blows because of financial constraints or his owner's political dealings and it continues to win public contracts from national and local public entities, including CNADNR⁵⁸.

Final remarks

The case studies revealed that both owners went to great lengths to consolidate a network of relationships with high ranking officials so as to keep their doors open and contact political elites (from various political parties, from Social Democrats to Democrat Liberals or Liberals), but also various state institutions whose activity can favour or disrupt their companies' economic well-being. Both had strong contacts within the CNADNR and the Ministry of Transport. Relying on political regimes, they have had fluctuating turnovers from year to year, variations which affected their functioning. Lack of liquidity is one of the reasons why the owner of ROMSTRADE repeatedly breached the law: to keep his cluster of firms alive.

In contrast to the project financed through the state budget, where it was possible to juggle with the price of the work in favour of the constructor and to the state's detriment, the project financed through EU funds received more scrutiny from both national and European authorities and, therefore, it suffered fewer changes throughout its life cycle.

V. CONCLUSION

In Romania, the allocation of public resources shows patterns of particularism. Only 15% of transactions were found to have a particularistic character from the 6064 contracts, in terms of winning firms who had financed political parties through legal donations. If we extend the privileged firm definition and include firms known to have political connections, the particularistic distribution of public funds rises to 19.4% of all transactions. This means that one out of five contracts awarded by public authorities may have a particularistic character.

⁵⁸ From 2007 to 2012, PA&CO managed to win 22 contracts from the CNADNR. Source: Official SEAP database.

The agency-capture analysis revealed that corruption risk in public procurement occurs especially at the local level and in state-owned companies. The results on county councils are confirmed by the recent DNA investigations – more than half (22 out of 41) of county council presidents are being charged with acts of corruption (Mihalache, 2015). Most of the companies that “captured” contracting authorities are politically connected firms. Moreover, following the analysis above, one out of ten contracting authorities has been captured by a single company. However, there is no guarantee that particularism does not present itself in a situation of non-capture.

European funded contracts, compared to non-EU public contracts, are less prone to corruption, as the rules are stricter and the controls are more frequent. Only 1 out of 13 contracts for which an addendum was signed had received European financing. The EU funded public procurement market is competitive, with a strong international presence. Only 1 out of 7 EU financed contracts were awarded by single bids, as opposed to 1 out of 4 contracts financed by the state budget. The practice of single bidding and the tendency to establish political connections exist in the entire public procurement market. Nonetheless, the non-EU funded contracts present a higher corruption risk as single bidding is negatively associated with EU funding, but positively associated with political connections. Agency capture is significantly associated with both single bidding and with politically connected firms, but not in the case concerning strictly EU funded contracts. Still, 1 out of every 3 contracts won by a politically connected firm received European funding. Data analysis concluded also that the number of awarded contracts per company can be explained by single bidding and the existence of a political connection in 44% of the cases in pre-electoral years.

One of the main requirements in detecting corruption is access to data and information. The main challenges to this report consisted in accessing public information (and receiving answers to FOIA requests), but also the process of data mining and cleaning all the erroneous information. The Romanian Government’s commitment to increase transparency in the public procurement sector is currently a “shape without substance”. One cannot reproach the authorities for the lack of transparency, but the tools in place do not favour extensive analyses of corruption risk. It is impossible to comprehensively analyse the public procurement system even at your own, private expense. More troubling is the fact that not even the state has the right instruments to perform a correct statistical evaluation. The solutions are obvious and largely covered by budgetary allocations (such as those for open government), or should be in the process of being covered by European funding. Thus, our recommendations are the following:

1. The new electronic system for public procurement (SICAP) which is about to be contracted should enable information to be extracted in a functioning unitary database which would contain several verification and selection filters (the system should, first and foremost, not allow crucial information to be missing). Omitting a contract must automatically be penalized with administrative fines. Access to SICAP, unlike SEAP, needs to be liberalized given that, currently, the cost of subscribing is prohibitive. Plus, the data export module from SICAP to CSV format should allot greater attention to diacritic symbols.

2. According to the National Anticorruption Strategy 2012-2015, Specific Objective 6 titled “Increasing efficiency of corruption preventing mechanisms in the area of public procurement”, “assembling a database of companies that have carried out contracts with public funding inappropriately” is being considered. This information is extracted from what Government Decision 925/2006 calls “primary and final ascertaining documents of fulfilment or non-fulfilment of contractual obligations” which ANRMAP receives and archives from contracting authorities. It would be useful for this “black list” of companies to be instantly available to all actors involved in public procurement, at least in the future, through SICAP. For EU funded projects, a similar system is the so-called ARACHNE tool whereby public servants within contracting authorities have the possibility of accessing an extensive amount of information on companies. Contracting authorities would be most advantaged, as they would have access to the names of business operators towards which they should exercise caution when awarding both nationally funded and European funded contracts. Contracting authorities could be encouraged, in the offer evaluation stage, to seek out the names of bidding companies in this database, and ignoring potential alarming signs could be considered evidence of intended fraud. Also, ANRMAP could publish regular reports on this issue and make these available to the general public.
3. The Freedom of Information Act needs to be amended to include implementation rules, which would specify access through newer technologies (such as digital photography, which is often rejected by authorities on grounds that it is not mentioned by the law), as the FOIA predates widespread use of this technique.
4. The annual report of each public authority or company should include a chapter on the effectiveness of procurement (‘value for money’). This report should be published no later than February of the following year. The methodological rules of Law 544/2001 already specify that the report needs to contain a justification of the authority’s budget (how objectives are met through spending) and can additionally contain a template for a chapter on public procurement. Unfortunately, at this time there is no department in the Romanian Government to monitor the completion of this report, and the Court of Accounts is limited to procedures and cannot make the necessary connection between how much tax-payers pay and how much they get for their money. Also necessary is a system of administrative sanctions for omitting to fill in this report.
5. The practice of single bidding and that of the “lowest price” criterion should be legally limited.

Also, for corruption risks to be better assessed the following **necessary improvements** should be made to the Electronic Public Procurement System. They cover both technical aspects of the system and rationales for restructuring the SEAP interface and are based on the direct negative experience of the SAR researchers in collecting data:

- Any additional information to different types of announcements (Errata; Corrections) should be added in a structured manner (not typewritten text, as is the case now).
- Selecting the field to be altered should be the norm and not typing the field name by hand as currently. The main announcement would contain the latest information added and only a track record of changes.
- The system should automatically be connected to the Trade Registry or to a simple database so that those who fill in announcements could insert just the tax ID and get the name of the company automatically.
- In case the winners of a procedure are associations-consortia of firms: there should be an option to tick that it is a consortium and get extra fields to insert one tax ID for each firm (clearly specifying that the first ID belongs to the leader).
- Each announcement should have clearly delineated fields for the post code and tax ID of both the winners and the contracting authority.
- Adding a self-filling option for Country and Locality – the user should type in the first letters and see a list of automatic suggestions for these two fields.
- The sums in the contracts should be either inserted strictly without VAT (remove the VAT option) or by selecting VAT from a predefined dropdown list (not manually inserted as is the case now).
- The sums in the contracts should be automatically converted to the other currencies (EUR and USD if RON was chosen) at the rate of exchange on the day the contract was awarded.
- When adding new values or changing older ones, there should be two separate fields, for numerals and for decimals.
- In case of an announcement containing several contracts, the appropriate CPV code should be mentioned for each contract. Information regarding unsuccessful bidders to an award procedure should be available – tax ID, prices bid.
- CAPTCHA codes, which, at present, are used in an extensive manner (at each stage of the search), should be used randomly or even removed.

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Appendix 1

Top 60 companies (based on their 2013 turnover) active on the public procurement market in the construction sector

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
ACOMIN S.A.	1993	2008	78337485	1309170	0	1.67%
ACOMIN S.A.	1993	2009	92746909	2095406	0	2.26%
ACOMIN S.A.	1993	2010	146486242	2061851	0	1.41%
ACOMIN S.A.	1993	2011	188461462	4681525	0	2.48%
ACOMIN S.A.	1993	2012	132210304	2155241	0	1.63%
ACOMIN S.A.	1993	2013	116148443	-1703807	0	-1.47%
AKTOR S.A. GRECIA ROMANIA	2004	2008	94115488	-3256200	1	-3.46%
AKTOR S.A. GRECIA ROMANIA	2004	2009	N/A	N/A	1	N/A
AKTOR S.A. GRECIA ROMANIA	2004	2010	52371032	1988876	1	3.80%
AKTOR S.A. GRECIA ROMANIA	2004	2011	26322667	-1823274	1	-6.93%
AKTOR S.A. GRECIA ROMANIA	2004	2012	38049642	887394	1	2.33%
AKTOR S.A. GRECIA ROMANIA	2004	2013	277658004	38055858	1	13.71%
ALPINE S.A.	2007	2008	96325731	-8985383	1	-9.33%
ALPINE S.A.	2007	2009	N/A	N/A	1	N/A
ALPINE S.A.	2007	2010	41784701	-30705356	1	-73.48%
ALPINE S.A.	2007	2011	167624190	-7892837	1	-4.71%
ALPINE S.A.	2007	2012	316908561	-106146390	1	-33.49%
ALPINE S.A.	2007	2013	N/A	N/A	1	N/A
APOLODOR COM IMPEX SRL	1992	2009	304199447	12134120	0	3.99%
APOLODOR COM IMPEX SRL	1992	2010	184227385	-5742370	0	-3.12%
APOLODOR COM	1992	2011	208057401	2023416	0	0.97%

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
IMPEX SRL						
APOLODOR COM IMPEX SRL	1992	2012	171562186	1762304	0	1.03%
APOLODOR COM IMPEX SRL	1992	2013	140170766	-8716045	0	-6.22%
APOLODOR COM IMPEX SRL	1992	2008	351751438	27469302	0	7.81%
ARCADA COMPANY SA	1994	2008	98086749	27922489	0	28.47%
ARCADA COMPANY SA	1994	2009	151016869	66015943	0	43.71%
ARCADA COMPANY SA	1994	2010	155421994	47538675	0	30.59%
ARCADA COMPANY SA	1994	2011	89537118	27646750	0	30.88%
ARCADA COMPANY SA	1994	2012	46465253	8624718	0	18.56%
ARCADA COMPANY SA	1994	2013	192680253	62684630	0	32.53%
ASTALDI SPA ITALIA SUCURSALA BUCURESTI	1998	2008	N/A	N/A	1	N/A
ASTALDI SPA ITALIA SUCURSALA BUCURESTI	1998	2009	114027305	2393698	1	2.10%
ASTALDI SPA ITALIA SUCURSALA BUCURESTI	1998	2010	54880956	18856698	1	34.36%
ASTALDI SPA ITALIA SUCURSALA BUCURESTI	1998	2011	330052870	-739268	1	-0.22%
ASTALDI SPA ITALIA SUCURSALA BUCURESTI	1998	2012	627591603	-120487023	1	-19.20%
ASTALDI SPA ITALIA SUCURSALA BUCURESTI	1998	2013	318270100	98830448	1	31.05%
AZVI S.A. - SEDIU PERMANENT DESEM NAT	2009	2009	N/A	N/A	1	N/A
AZVI S.A. - SEDIU PERMANENT DESEM NAT	2009	2010	165414923	11731082	1	7.09%
AZVI S.A. - SEDIU PERMANENT DESEM NAT	2009	2011	193301624	12024789	1	6.22%
AZVI S.A. - SEDIU PERMANENT DESEM NAT	2009	2012	147603225	12628626	1	8.56%
AZVI S.A. - SEDIU	2009	2013	183249333	873916	1	0.48%

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PERMANENT DESEMNAT						
AZVI S.A. - SEDIU PERMANENT DESEMNAT	2009	2008	N/A	N/A	1	N/A
BOG'ART S.R.L.	1991	2008	342242635	33933659	0	9.92%
BOG'ART S.R.L.	1991	2009	381194802	41715466	0	10.94%
BOG'ART S.R.L.	1991	2010	347047123	6598320	0	1.90%
BOG'ART S.R.L.	1991	2011	325273623	3998264	0	1.23%
BOG'ART S.R.L.	1991	2012	339018944	2687114	0	0.79%
BOG'ART S.R.L.	1991	2013	403822082	3228061	0	0.80%
CON-A S.R.L.	1991	2008	190412791	20197667	0	10.61%
CON-A S.R.L.	1991	2009	123366705	10851356	0	8.80%
CON-A S.R.L.	1991	2010	196642666	8991259	0	4.57%
CON-A S.R.L.	1991	2011	232894875	8746423	0	3.76%
CON-A S.R.L.	1991	2012	199814329	14319553	0	7.17%
CON-A S.R.L.	1991	2013	229566464	12962910	0	5.65%
CONARG CONSTRUCT S.R.L.	2007	2008	225790997	33037441	0	14.63%
CONARG CONSTRUCT S.R.L.	2007	2009	141220751	21876198	0	15.49%
CONARG CONSTRUCT S.R.L.	2007	2010	154479309	2587735	0	1.68%
CONARG CONSTRUCT S.R.L.	2007	2011	135176973	412416	0	0.31%
CONARG CONSTRUCT S.R.L.	2007	2012	106317782	362607	0	0.34%
CONARG CONSTRUCT S.R.L.	2007	2013	111653080	854414	0	0.77%
CONDMAG S.A.	1999	2009	226799345	21513196	0	9.49%
CONDMAG S.A.	1999	2010	198452126	14316322	0	7.21%
CONDMAG S.A.	1999	2011	113716459	1474293	0	1.30%
CONDMAG S.A.	1999	2012	92849288	-26086405	0	-28.10%
CONDMAG S.A.	1999	2013	115676385	-24613253	0	-21.28%
CONDMAG S.A.	1999	2008	145313194	10355591	0	7.13%
CONSTRUCTII ERBASU SA	1992	2009	148045310	10061056	0	6.80%
CONSTRUCTII ERBASU SA	1992	2010	170602364	19483305	0	11.42%
CONSTRUCTII ERBASU	1992	2011	185161688	33844312	0	18.28%

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SA						
CONSTRUCTII ERBASU SA	1992	2012	459822636	35745630	0	7.77%
CONSTRUCTII ERBASU SA	1992	2013	165822208	13019108	0	7.85%
CONSTRUCTII ERBASU SA	1992	2008	84584968	4001930	0	4.73%
COPISA CONSTRUCTORA PIRENAICA S.A.	2009	2008	N/A	N/A	1	N/A
COPISA CONSTRUCTORA PIRENAICA S.A.	2009	2009	1592	-400228	1	-25139.95%
COPISA CONSTRUCTORA PIRENAICA S.A.	2009	2010	N/A	N/A	1	N/A
COPISA CONSTRUCTORA PIRENAICA S.A.	2009	2011	66955717	-8258429	1	-12.33%
COPISA CONSTRUCTORA PIRENAICA S.A.	2009	2012	45937112	7337042	1	15.97%
COPISA CONSTRUCTORA PIRENAICA S.A.	2009	2013	98011974	4237254	1	4.32%
DELTA ANTREPRIZA DE CONSTRUCTII SI MONTAJ 93 S.R.L.	1993	2008	417686429	27514936	0	6.59%
DELTA ANTREPRIZA DE CONSTRUCTII SI MONTAJ 93 S.R.L.	1993	2009	307718317	53744440	0	17.47%
DELTA ANTREPRIZA DE CONSTRUCTII SI MONTAJ 93 S.R.L.	1993	2010	391885984	126292821	0	32.23%
DELTA ANTREPRIZA DE CONSTRUCTII SI MONTAJ 93 S.R.L.	1993	2011	407736320	59637067	0	14.63%
DELTA ANTREPRIZA DE CONSTRUCTII SI MONTAJ 93 S.R.L.	1993	2012	502606342	18404556	0	3.66%
DELTA ANTREPRIZA DE CONSTRUCTII SI MONTAJ 93 S.R.L.	1993	2013	544067907	46466261	0	8.54%
DIFERIT S.R.L.	2001	2009	42543606	2092386	0	4.92%
DIFERIT S.R.L.	2001	2010	28733170	1430913	0	4.98%

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DIFERIT S.R.L.	2001	2011	90661276	5362425	0	5.91%
DIFERIT S.R.L.	2001	2012	114280040	11034298	0	9.66%
DIFERIT S.R.L.	2001	2013	132472003	6962749	0	5.26%
DIFERIT S.R.L.	2001	2008	40935309	4256428	0	10.40%
ELECTROGRUP SA	1997	2008	105540601	33714705	0	31.94%
ELECTROGRUP SA	1997	2009	85468228	22566190	0	26.40%
ELECTROGRUP SA	1997	2010	95297424	21591699	0	22.66%
ELECTROGRUP SA	1997	2011	133145637	24184388	0	18.16%
ELECTROGRUP SA	1997	2012	146998482	20814671	0	14.16%
ELECTROGRUP SA	1997	2013	185621466	28214800	0	15.20%
ELECTROMONTAJ S.A.	1991	2008	192565219	15605033	0	8.10%
ELECTROMONTAJ S.A.	1991	2009	179483043	18569567	0	10.35%
ELECTROMONTAJ S.A.	1991	2010	311328750	34035811	0	10.93%
ELECTROMONTAJ S.A.	1991	2011	218674815	18753009	0	8.58%
ELECTROMONTAJ S.A.	1991	2012	185175218	11711960	0	6.32%
ELECTROMONTAJ S.A.	1991	2013	210748195	830752	0	0.39%
ENERGOBIT S.A.	1992	2008	83677204	3491290	0	4.17%
ENERGOBIT S.A.	1992	2009	7582076	15266434	0	201.35%
ENERGOBIT S.A.	1992	2010	7350013	25811741	0	351.18%
ENERGOBIT S.A.	1992	2011	9529748	36488176	0	382.89%
ENERGOBIT S.A.	1992	2012	8126958	62152403	0	764.77%
ENERGOBIT S.A.	1992	2013	7639106	48686374	0	637.33%
ENERGOMONTAJ SA	1991	2008	389619010	9225971	0	2.37%
ENERGOMONTAJ SA	1991	2009	430111738	9759584	0	2.27%
ENERGOMONTAJ SA	1991	2010	429579610	9358008	0	2.18%
ENERGOMONTAJ SA	1991	2011	466558469	3466594	0	0.74%
ENERGOMONTAJ SA	1991	2012	406460041	5288158	0	1.30%
ENERGOMONTAJ SA	1991	2013	402313922	5967140	0	1.48%
EURO CONSTRUCT TRADING '98 SRL	1998	2008	216016260	68095189	0	31.52%
EURO CONSTRUCT TRADING '98 SRL	1998	2009	251342741	68629464	0	27.31%
EURO CONSTRUCT TRADING '98 SRL	1998	2010	270571549	98376791	0	36.36%
EURO CONSTRUCT TRADING '98 SRL	1998	2011	354497745	45637706	0	12.87%
EURO CONSTRUCT	1998	2012	458900643	40395091	0	8.80%

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TRADING '98 SRL						
EURO CONSTRUCT TRADING '98 SRL	1998	2013	462611947	31254831	0	6.76%
FCC CONSTRUCCION S.A. BARCELONA ROMANIA	2004	2008	109796563	-18477203	1	-16.83%
FCC CONSTRUCCION S.A. BARCELONA ROMANIA	2004	2009	286808889	51514996	1	17.96%
FCC CONSTRUCCION S.A. BARCELONA ROMANIA	2004	2010	N/A	N/A	1	N/A
FCC CONSTRUCCION S.A. BARCELONA ROMANIA	2004	2011	139485134	-6283814	1	-4.51%
FCC CONSTRUCCION S.A. BARCELONA ROMANIA	2004	2012	315446253	-845233	1	-0.27%
FCC CONSTRUCCION S.A. BARCELONA ROMANIA	2004	2013	246001985	-24604434	1	-10.00%
HIDROCONSTRUCTIA S.A.	1991	2008	918750904	60174751	0	6.55%
HIDROCONSTRUCTIA S.A.	1991	2009	1122399432	46652663	0	4.16%
HIDROCONSTRUCTIA S.A.	1991	2010	977141225	59632354	0	6.10%
HIDROCONSTRUCTIA S.A.	1991	2011	1002178651	60449579	0	6.03%
HIDROCONSTRUCTIA S.A.	1991	2012	623555725	23068304	0	3.70%
HIDROCONSTRUCTIA S.A.	1991	2013	599709378	11670914	0	1.95%
IASICON S.A.	1992	2009	97064297	7189334	0	7.41%
IASICON S.A.	1992	2010	94266952	8559059	0	9.08%
IASICON S.A.	1992	2011	102133225	14723753	0	14.42%
IASICON S.A.	1992	2012	93894169	2212168	0	2.36%
IASICON S.A.	1992	2013	100665151	35482	0	0.04%
IASICON S.A.	1992	2008	94644938	9116946	0	9.63%
IMSAT SA	1991	2008	391120862	13445636	1	3.44%
IMSAT SA	1991	2009	330703933	-823582	1	-0.25%
IMSAT SA	1991	2010	228555307	-20404542	1	-8.93%

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IMSAT SA	1991	2011	261414217	11179104	1	4.28%
IMSAT SA	1991	2012	210561085	1285301	1	0.61%
IMSAT SA	1991	2013	189397898	1647408	1	0.87%
INSPET S.A.	1992	2009	204187960	11777715	0	5.77%
INSPET S.A.	1992	2010	275335960	25037171	0	9.09%
INSPET S.A.	1992	2011	182405099	18047591	0	9.89%
INSPET S.A.	1992	2012	196028092	9009773	0	4.60%
INSPET S.A.	1992	2013	148323824	12262560	0	8.27%
INSPET S.A.	1992	2008	169631301	11955072	0	7.05%
LUXTEN LIGHTING COMPANY SA	1995	2008	234387573	67367389	0	28.74%
LUXTEN LIGHTING COMPANY SA	1995	2009	169119398	22467486	0	13.28%
LUXTEN LIGHTING COMPANY SA	1995	2010	176745990	25739360	0	14.56%
LUXTEN LIGHTING COMPANY SA	1995	2011	183529321	18702925	0	10.19%
LUXTEN LIGHTING COMPANY SA	1995	2012	153492498	27122941	0	17.67%
LUXTEN LIGHTING COMPANY SA	1995	2013	185986060	36125978	0	19.42%
MAX BOEGL ROMANIA S.R.L.	2003	2009	77646119	10550151	1	13.59%
MAX BOEGL ROMANIA S.R.L.	2003	2010	98851194	10664563	1	10.79%
MAX BOEGL ROMANIA S.R.L.	2003	2011	207780105	7158870	1	3.45%
MAX BOEGL ROMANIA S.R.L.	2003	2012	387873211	9578504	1	2.47%
MAX BOEGL ROMANIA S.R.L.	2003	2013	151374270	4355426	1	2.88%
MAX BOEGL ROMANIA S.R.L.	2003	2008	86859484	-2200605	1	-2.53%
PROMS CONCEPT GROUP S.R.L.	2007	2008	4315601	1788734	0	41.45%
PROMS CONCEPT GROUP S.R.L.	2007	2009	N/A	N/A	0	N/A
PROMS CONCEPT GROUP S.R.L.	2007	2010	16024162	2057188	0	12.84%
PROMS CONCEPT GROUP S.R.L.	2007	2011	20538349	1478826	0	7.20%

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PROMS CONCEPT GROUP S.R.L.	2007	2012	57875401	3441009	0	5.95%
PROMS CONCEPT GROUP S.R.L.	2007	2013	100153053	4095315	0	4.09%
ROMELECTRO SA	1991	2008	511323085	38674164	0	7.56%
ROMELECTRO SA	1991	2009	510705467	50108119	0	9.81%
ROMELECTRO SA	1991	2010	465807819	62398275	0	13.40%
ROMELECTRO SA	1991	2011	351350620	54488533	0	15.51%
ROMELECTRO SA	1991	2012	346269505	13514998	0	3.90%
ROMELECTRO SA	1991	2013	317065411	36904781	0	11.64%
ROTARY CONSTRUCTII S.R.L.	1991	2008	106636091	3954284	0	3.71%
ROTARY CONSTRUCTII S.R.L.	1991	2009	78419639	3873911	0	4.94%
ROTARY CONSTRUCTII S.R.L.	1991	2010	94868722	4526104	0	4.77%
ROTARY CONSTRUCTII S.R.L.	1991	2011	148296619	5729507	0	3.86%
ROTARY CONSTRUCTII S.R.L.	1991	2012	176071799	4304041	0	2.44%
ROTARY CONSTRUCTII S.R.L.	1991	2013	137280299	2902700	0	2.11%
SALINI IMPREGILO S.P.A MILANO-SUCURSALA SIBIU	2011	2008	N/A	N/A	0	N/A
SALINI IMPREGILO S.P.A MILANO-SUCURSALA SIBIU	2011	2009	N/A	N/A	0	N/A
SALINI IMPREGILO S.P.A MILANO-SUCURSALA SIBIU	2011	2010	N/A	N/A	0	N/A
SALINI IMPREGILO S.P.A MILANO-SUCURSALA SIBIU	2011	2011	0	-191884	0	-191 884
SALINI IMPREGILO S.P.A MILANO-SUCURSALA SIBIU	2011	2012	291404612	-16791437	0	-5.76%
SALINI IMPREGILO S.P.A MILANO-SUCURSALA SIBIU	2011	2013	199643777	-77274904	0	-38.71%
SHAPIR STRUCTURES S.R.L.	2000	2008	1710021	-1312807	1	-76.77%
SHAPIR STRUCTURES	2000	2009	21237263	1993840	1	9.39%

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S.R.L.						
SHAPIR STRUCTURES S.R.L.	2000	2010	16058256	533862	1	3.32%
SHAPIR STRUCTURES S.R.L.	2000	2011	49853876	1471506	1	2.95%
SHAPIR STRUCTURES S.R.L.	2000	2012	181200591	1635251	1	0.90%
SHAPIR STRUCTURES S.R.L.	2000	2013	232645499	-33723906	1	-14.50%
STRABAG AG AUSTRIA SUCURSALA BUCURESTI	2005	2008	147365764	7623329	0	5.17%
STRABAG AG AUSTRIA SUCURSALA BUCURESTI	2005	2009	218163356	-11667081	0	-5.35%
STRABAG AG AUSTRIA SUCURSALA BUCURESTI	2005	2010	282448673	-4952386	0	-1.75%
STRABAG AG AUSTRIA SUCURSALA BUCURESTI	2005	2011	272871504	-8191969	0	-3.00%
STRABAG AG AUSTRIA SUCURSALA BUCURESTI	2005	2012	784401062	16361303	0	2.09%
STRABAG AG AUSTRIA SUCURSALA BUCURESTI	2005	2013	400689829	556476880	0	138.88%
STRABAG S.R.L.	1994	2008	489221703	28180644	0	5.76%
STRABAG S.R.L.	1994	2009	512393401	28340640	0	5.53%
STRABAG S.R.L.	1994	2010	556577129	28965062	0	5.20%
STRABAG S.R.L.	1994	2011	585828064	15340387	0	2.62%
STRABAG S.R.L.	1994	2012	1403884345	32849687	0	2.34%
STRABAG S.R.L.	1994	2013	1028034647	116097478	0	11.29%
STRACO GRUP S.R.L.	2003	2008	133577052	28287092	0	21.18%
STRACO GRUP S.R.L.	2003	2009	163945104	1804476	0	1.10%
STRACO GRUP S.R.L.	2003	2010	213413851	3041585	0	1.43%
STRACO GRUP S.R.L.	2003	2011	372590194	5856956	0	1.57%
STRACO GRUP S.R.L.	2003	2012	872556755	3244469	0	0.37%
STRACO GRUP S.R.L.	2003	2013	616549831	1619187	0	0.26%
SWIETELSKY BAUGESELLSCHAFT M.B.H. LINZ	2011	2008	N/A	N/A	0	N/A

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
SUCURSALA BUCURESTI						
SWIETELSKY BAUGESELLSCHAFT M.B.H. LINZ SUCURSALA BUCURESTI	2011	2009	N/A	N/A	0	N/A
SWIETELSKY BAUGESELLSCHAFT M.B.H. LINZ SUCURSALA BUCURESTI	2011	2010	N/A	N/A	0	N/A
SWIETELSKY BAUGESELLSCHAFT M.B.H. LINZ SUCURSALA BUCURESTI	2011	2011	8459361	163031	0	1.93%
SWIETELSKY BAUGESELLSCHAFT M.B.H. LINZ SUCURSALA BUCURESTI	2011	2012	116892597	-9056120	0	-7.75%
SWIETELSKY BAUGESELLSCHAFT M.B.H. LINZ SUCURSALA BUCURESTI	2011	2013	199392671	-21652857	0	-10.86%
TANCRAD S.R.L.	1995	2008	117544796	24628357	0	20.95%
TANCRAD S.R.L.	1995	2009	91408862	10218679	0	11.18%
TANCRAD S.R.L.	1995	2010	105671099	10240473	0	9.69%
TANCRAD S.R.L.	1995	2011	157769876	15474304	0	9.81%
TANCRAD S.R.L.	1995	2012	194346100	13011440	0	6.69%
TANCRAD S.R.L.	1995	2013	239959729	14944212	0	6.23%
TECHNOCER SRL	1997	2008	43408319	4679606	0	10.78%
TECHNOCER SRL	1997	2009	41974065	5307555	0	12.64%
TECHNOCER SRL	1997	2010	73985358	9600252	0	12.98%
TECHNOCER SRL	1997	2011	129537856	22628909	0	17.47%
TECHNOCER SRL	1997	2012	164591579	37335938	0	22.68%
TECHNOCER SRL	1997	2013	108417322	16550910	0	15.27%
TEHNOLOGICA RADION S.R.L.	1993	2008	665869469	146364299	0	21.98%
TEHNOLOGICA RADION S.R.L.	1993	2009	459070700	19702155	0	4.29%
TEHNOLOGICA RADION S.R.L.	1993	2010	599568293	49953020	0	8.33%

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TEHNOLOGICA RADION S.R.L.	1993	2011	584307327	27734629	0	4.75%
TEHNOLOGICA RADION S.R.L.	1993	2012	560013055	6498576	0	1.16%
TEHNOLOGICA RADION S.R.L.	1993	2013	356891562	4818173	0	1.35%
TEHNOSTRADE SRL	2004	2008	441828063	204865361	0	46.37%
TEHNOSTRADE SRL	2004	2009	645164746	188361914	0	29.20%
TEHNOSTRADE SRL	2004	2010	419721027	115581346	0	27.54%
TEHNOSTRADE SRL	2004	2011	572444536	147569485	0	25.78%
TEHNOSTRADE SRL	2004	2012	549761129	87125842	0	15.85%
TEHNOSTRADE SRL	2004	2013	338804149	51750680	0	15.27%
TEL DRUM S.A.	1993	2008	192302364	25364564	0	13.19%
TEL DRUM S.A.	1993	2009	N/A	N/A	0	N/A
TEL DRUM S.A.	1993	2010	165414923	11731082	0	7.09%
TEL DRUM S.A.	1993	2011	193301624	12024789	0	6.22%
TEL DRUM S.A.	1993	2012	147603225	12628626	0	8.56%
TEL DRUM S.A.	1993	2013	183249333	873916	0	0.48%
TIAB SA	1991	2008	130974303	1276365	1	0.97%
TIAB SA	1991	2009	132919380	1600093	1	1.20%
TIAB SA	1991	2010	121280413	1312232	1	1.08%
TIAB SA	1991	2011	157727641	2685344	1	1.70%
TIAB SA	1991	2012	144671204	5951966	1	4.11%
TIAB SA	1991	2013	190674277	4106515	1	2.15%
VECTRA SERVICE S.R.L.	1994	2009	182114722	7267684	0	3.99%
VECTRA SERVICE S.R.L.	1994	2010	212591028	7230104	0	3.40%
VECTRA SERVICE S.R.L.	1994	2011	280969243	7780361	0	2.77%
VECTRA SERVICE S.R.L.	1994	2012	188575923	1214905	0	0.64%
VECTRA SERVICE S.R.L.	1994	2013	153690521	-9707711	0	-6.32%
VECTRA SERVICE S.R.L.	1994	2008	213417014	5252704	0	2.46%
VEGA 93 S.R.L.	1993	2008	266110768	38841558	0	14.60%
VEGA 93 S.R.L.	1993	2009	373709795	34273414	0	9.17%
VEGA 93 S.R.L.	1993	2010	356099029	39237878	0	11.02%

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
VEGA 93 S.R.L.	1993	2011	361214554	33994027	0	9.41%
VEGA 93 S.R.L.	1993	2012	352784284	1323444	0	0.38%
VEGA 93 S.R.L.	1993	2013	258770876	4633980	0	1.79%
VIAROM CONSTRUCT S.A.	2001	2008	83325375	9229	1	0.01%
VIAROM CONSTRUCT S.A.	2001	2009	209765423	3361855	1	1.60%
VIAROM CONSTRUCT S.A.	2001	2010	106422618	1198505	1	1.13%
VIAROM CONSTRUCT S.A.	2001	2011	139925805	1493241	1	1.07%
VIAROM CONSTRUCT S.A.	2001	2012	139925805	5827220	1	4.16%
VIAROM CONSTRUCT S.A.	2001	2013	185151440	2282473	1	1.23%
GENERAL CONSTRUCT SRL	1994	2008	45914320	1114799	0	2.43%
GENERAL CONSTRUCT SRL	1994	2009	79716355	1476460	0	1.85%
GENERAL CONSTRUCT SRL	1994	2010	53082335	1357781	0	2.56%
GENERAL CONSTRUCT SRL	1994	2011	80673410	3056090	0	3.79%
GENERAL CONSTRUCT SRL	1994	2012	83453301	2891948	0	3.47%
GENERAL CONSTRUCT SRL	1994	2013	95234615	4607644	0	4.84%
DRUPO S.R.L.	2001	2008	47261646	2261857	0	4.79%
DRUPO S.R.L.	2001	2009	37104844	956598	0	2.58%
DRUPO S.R.L.	2001	2010	56023362	4850859	0	8.66%
DRUPO S.R.L.	2001	2011	87142920	5354924	0	6.14%
DRUPO S.R.L.	2001	2012	93165922	3351637	0	3.60%
DRUPO S.R.L.	2001	2013	94105223	8121484	0	8.63%
ACI CLUJ S.A.	1991	2008	137858980	9973119	0	7.23%
ACI CLUJ S.A.	1991	2009	131681391	12853291	0	9.76%
ACI CLUJ S.A.	1991	2010	122365880	8776630	0	7.17%
ACI CLUJ S.A.	1991	2011	188662832	10377948	0	5.50%
ACI CLUJ S.A.	1991	2012	93801598	5072543	0	5.41%
ACI CLUJ S.A.	1991	2013	93298899	1214352	0	1.30%
CONEST S.A.	1991	2008	72661219	6643391	0	9.14%

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
CONEST S.A.	1991	2009	N/A	N/A	0	N/A
CONEST S.A.	1991	2010	48117233	379379	0	0.79%
CONEST S.A.	1991	2011	46230155	587334	0	1.27%
CONEST S.A.	1991	2012	67290635	288889	0	0.43%
CONEST S.A.	1991	2013	90208664	414660	0	0.46%
SOCIETATEA DE CONSTRUCTII IN TRANSPORTURI BUCURESTI S.A.	1991	2008	79251772	5136552	0	6.48%
SOCIETATEA DE CONSTRUCTII IN TRANSPORTURI BUCURESTI S.A.	1991	2009	105692130	2198528	0	2.08%
SOCIETATEA DE CONSTRUCTII IN TRANSPORTURI BUCURESTI S.A.	1991	2010	91844290	1576221	0	1.72%
SOCIETATEA DE CONSTRUCTII IN TRANSPORTURI BUCURESTI S.A.	1991	2011	105082473	2614935	0	2.49%
SOCIETATEA DE CONSTRUCTII IN TRANSPORTURI BUCURESTI S.A.	1991	2012	202176315	904790	0	0.45%
SOCIETATEA DE CONSTRUCTII IN TRANSPORTURI BUCURESTI S.A.	1991	2013	88371167	700093	0	0.79%
LOIAL IMPEX S.R.L.	1993	2008	66086447	3727854	0	5.64%
LOIAL IMPEX S.R.L.	1993	2009	N/A	N/A	0	N/A
LOIAL IMPEX S.R.L.	1993	2010	48117233	379379	0	0.79%
LOIAL IMPEX S.R.L.	1993	2011	46230155	587334	0	1.27%
LOIAL IMPEX S.R.L.	1993	2012	67290635	288889	0	0.43%
LOIAL IMPEX S.R.L.	1993	2013	90208664	414660	0	0.46%
GEIGER TRANSILVANIA S.R.L.	2004	2008	84357824	2859661	0	3.39%
GEIGER TRANSILVANIA S.R.L.	2004	2009	58432032	420069	0	0.72%
GEIGER TRANSILVANIA S.R.L.	2004	2010	60031176	812853	0	1.35%
GEIGER TRANSILVANIA S.R.L.	2004	2011	89963407	316386	0	0.35%

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
GEIGER TRANSILVANIA S.R.L.	2004	2012	78302102	2745854	0	3.51%
GEIGER TRANSILVANIA S.R.L.	2004	2013	87238695	4561346	0	5.23%
TEHNODOMUS S.A.	1994	2008	97762322	12415625	0	12.70%
TEHNODOMUS S.A.	1994	2009	145712567	29124955	0	19.99%
TEHNODOMUS S.A.	1994	2010	152624069	23709926	0	15.53%
TEHNODOMUS S.A.	1994	2011	175549055	12929757	0	7.37%
TEHNODOMUS S.A.	1994	2012	40803255	1740845	0	4.27%
TEHNODOMUS S.A.	1994	2013	81961723	2488900	0	3.04%
AGETAPS S.R.L.	1994	2008	69971552	2511766	0	3.59%
AGETAPS S.R.L.	1994	2009	56473658	691693	0	1.22%
AGETAPS S.R.L.	1994	2010	56436335	248046	0	0.44%
AGETAPS S.R.L.	1994	2011	68044669	1321665	0	1.94%
AGETAPS S.R.L.	1994	2012	87219181	442861	0	0.51%
AGETAPS S.R.L.	1994	2013	81009466	451505	0	0.56%
TERRA GAZ CONSTRUCT S.R.L.	1998	2008	27163058	705279	0	2.60%
TERRA GAZ CONSTRUCT S.R.L.	1998	2009	56902683	2176216	0	3.82%
TERRA GAZ CONSTRUCT S.R.L.	1998	2010	48388396	1644660	0	3.40%
TERRA GAZ CONSTRUCT S.R.L.	1998	2011	57338760	1988093	0	3.47%
TERRA GAZ CONSTRUCT S.R.L.	1998	2012	55521386	1486129	0	2.68%
TERRA GAZ CONSTRUCT S.R.L.	1998	2013	79023999	3373980	0	4.27%
DRUM CONSTRUCT S.R.L.	1995	2008	58837223	2280758	0	3.88%
DRUM CONSTRUCT S.R.L.	1995	2009	44110491	1185476	0	2.69%
DRUM CONSTRUCT S.R.L.	1995	2010	56543494	662342	0	1.17%
DRUM CONSTRUCT S.R.L.	1995	2011	70063620	948878	0	1.35%
DRUM CONSTRUCT S.R.L.	1995	2012	79885457	846745	0	1.06%
DRUM CONSTRUCT S.R.L.	1995	2013	77845648	847180	0	1.09%
PORR CONSTRUCT	2006	2008	35009166	-29561410	0	-84.44%

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
S.R.L.						
PORR CONSTRUCT S.R.L.	2006	2009	235086476	29828401	0	12.69%
PORR CONSTRUCT S.R.L.	2006	2010	252858105	-38073432	0	-15.06%
PORR CONSTRUCT S.R.L.	2006	2011	299672016	-29364539	0	-9.80%
PORR CONSTRUCT S.R.L.	2006	2012	83310445	-12927536	0	-15.52%
PORR CONSTRUCT S.R.L.	2006	2013	51315808	975204	0	1.90%
VICTOR CONSTRUCT S.R.L.	1993	2008	89413230	15354561	0	17.17%
VICTOR CONSTRUCT S.R.L.	1993	2009	71195187	7433190	0	10.44%
VICTOR CONSTRUCT S.R.L.	1993	2010	76641116	10638472	0	13.88%
VICTOR CONSTRUCT S.R.L.	1993	2011	74349604	10831385	0	14.57%
VICTOR CONSTRUCT S.R.L.	1993	2012	85693389	8239650	0	9.62%
VICTOR CONSTRUCT S.R.L.	1993	2013	77174019	5574218	0	7.22%
NEWAMPORT COMPANI S.R.L.	2004	2008	11850525	64195	0	0.54%
NEWAMPORT COMPANI S.R.L.	2004	2009	19742856	158236	0	0.80%
NEWAMPORT COMPANI S.R.L.	2004	2010	31654670	272851	0	0.86%
NEWAMPORT COMPANI S.R.L.	2004	2011	39656018	367344	0	0.93%
NEWAMPORT COMPANI S.R.L.	2004	2012	49736806	482575	0	0.97%
NEWAMPORT COMPANI S.R.L.	2004	2013	76395345	682513	0	0.89%
CAST S.R.L.	1994	2008	120987729	16815172	0	13.90%
CAST S.R.L.	1994	2009	69506141	6681215	0	9.61%
CAST S.R.L.	1994	2010	116562857	13822783	0	11.86%
CAST S.R.L.	1994	2011	148165257	13309510	0	8.98%
CAST S.R.L.	1994	2012	124191029	10165983	0	8.19%
CAST S.R.L.	1994	2013	75090967	5351112	0	7.13%
SELINA	1994	2008	104335410	9394291	0	9.00%

Company name	Creation date	YEAR	Turnover (RON)	Gross profit (RON)	International firm	Profit Rate
SELINA	1994	2009	104451320	10769718	0	10.31%
SELINA	1994	2010	133030941	12964559	0	9.75%
SELINA	1994	2011	149637017	24793883	0	16.57%
SELINA	1994	2012	136753552	17602329	0	12.87%
SELINA	1994	2013	70836636	-60911806	0	-85.99%
STRABAG	1994/2005	2008	636587467	35803973	1	5.62%
STRABAG	1994/2005	2009	730556757	16673559	1	2.28%
STRABAG	1994/2005	2010	839025802	24012676	1	2.86%
STRABAG	1994/2005	2011	858699568	7148418	1	0.83%
STRABAG	1994/2005	2012	2188285407	49210990	1	2.25%
STRABAG	1994/2005	2013	1428724476	672574358	1	47.08%



ABSTRACT

The Turkey Country Report was prepared as part of the requirements for the ANTICORRP project, WP8. The report employs national data to analyse recent developments in the construction sector. However, the contract-level procurement data have not been compiled as requests for the data were unanswered by the Turkish Public Procurement Agency. Therefore, aggregate data on public procurement have been used to trace developments in law and implementation. The post-2002 incumbent AKP government has to a large extent considered construction investments as an engine of economic growth which resulted in a substantial expansion of this sector. The Turkish Public Procurement Law (PPL) came into force in 2003 to bring Turkey into compliance with EU procurement standards. Although certain improvements have been achieved, frequently introduced exemptions distorted the rules and procedures for transparency, competition and non-discrimination. A considerable number of amendments have aimed at removing major public contracts from the scope of PPL. Recently, Public-Private Partnerships (PPPs) have been used principally to build up large-scale infrastructure projects. Due to the large capital requirements and the fact that the legal structure of PPPs is largely incompatible with the PPL and the EU regulations, only a smaller group of companies which have allegedly close connections with top level politicians win PPP projects worth billions of Euros. Thus, under the current framework, PPPs in the Turkish construction sector are significantly prone to corruption risks.

ACRONYMS

AKP	Adalet ve Kalkınma Partisi (Justice and Development Party, the ruling party in Turkey since its founding in 2001)
ALB	Abnormally Low Bids
BDP	Barış ve Demokrasi Partisi (Peace and Democracy Party)
BOT	Build, operate, and transfer
CHP	Cumhuriyet Halk Partisi (Republican People's Party)
EC	European Commission
EPPP	Electronic Public Procurement Platform
EU	European Union
GDP	Gross Domestic Product
IPA	Instrument for Pre-Accession Assistance
İBB	İstanbul Büyükşehir Belediyesi (İstanbul Metropolitan Municipality)
İSKİ	İstanbul Su ve Kanalizasyon İdaresi (İstanbul Water and Sewerage Administration)
MHP	Milliyetçi Hareket Partisi (National Movement Party)
PPA	Public Procurement Agency
PPB	Public Procurement Board
PPL	Public Procurement Law
PPP	Public-Private Partnership
REB	Report Evaluation Board
SEE	State Economic Enterprise
TCA	Turkish Court of Accounts
TGNA	Turkish Grand National Assembly
TPC	Turkish Penal Code Law
TRY	Turkish Lira

TABLES

Table 1. Construction and Public Procurement Markets (%)

Table 2. Turkish Public Procurement Reform in 2002

Table 3. Potential Size of Exemptions in GDP (%)

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I. INTRODUCTION

The perception of corruption or corruption risk is a serious concern for much of Turkish society, which is clearly observable in public opinion surveys. For instance, according to a 2013 Corruption Survey prepared by Ernst & Young (2013) Turkey performed relatively better than certain European countries in terms of public perception of bribery and irregularity, but failed in the area of public procurement. Some 39% of respondents think that bribery is a must in order to qualify for a public procurement contract. Transparency International (2013) identified public procurement as one of the sectors most susceptible to corruption, with many cases involving high-level figures. Similarly, the 2013 Enterprise Survey study by the World Bank and IFC (2013) singled out public procurement as the greatest source of corruption along with other activities such as getting a construction permit, and import and operating licenses. Not only international studies underlined corruption risks in public procurement but domestic studies also put emphasis on the issue. A nationwide survey conducted amongst firms (Adaman et al. 2009) pointed out the perceived favouritism in large scale public contracts such as highway and dam procurement increased between the years 2004 and 2008.

The existing AKP government, in power since 2002, has to a large extent considered construction investments an engine of economic growth, and has therefore paid special attention to expanding this sector. The share of construction expenditures as a percentage of GDP is about 9% of which approximately 5-6% comes from the private sector. The total amount of public procurement constitutes almost 6% of GDP the majority of which comes from central government agency projects, not local government projects. Public Procurement Law (PPL) also regulates certain expenditures of state economic enterprises (SEEs) whose share of procurement in GDP is 1%. Finally, the share of public works contracts in total has considerably increased from 38% in 2008 to 60% in 2013, a result of the construction-led growth strategy pursued in Turkey.

The PPL came into force in 2003 to bring Turkey in alignment with EU Public Procurement Directives. The PPL was largely in conformity with the EU *acquis* at the beginning although not fully. Consecutive AKP governments have repeatedly changed regulations by claiming to improve competition and transparency and ensure further alignment with the EU legislative framework. Although certain improvements have been achieved, the large part of amendments distorted the rules and procedures for transparency, competition and non-discrimination. A considerable number of amendments have aimed at removing major public contracts from the scope of the PPL. Therefore the official share of public procurement as a percentage of GDP (6%) is much lower than in the EU overall (15-16%). Potential share of exemptions in GDP has consistently continued to increase from 1.8 % in 2008 to 4% in 2013.

Unfortunately, PPL amendments have also enabled contracting agencies to make non-competitive procurement procedures easier. As a result, the use of open procedures has decreased from 81% in 2008 to 73% at the end of 2013. Furthermore, a large part of public works procurement has been closed to foreign competition contrary to EU procurement philosophy and policy. The share of procurement open to foreign competition in total has only

remained between 50-60%. Moreover, a price advantage up to 15% has been applied to domestic bidders in almost half of all international tenders.

Concerning the appeal of contracting agencies' tender decisions, the Public Procurement Board (PPB), financially and administratively independent and responsible for overseeing public tenders has been completely reshuffled in recent years. Along with new appointments, the Board decisions have apparently changed in favour of contracting agencies. In this respect, the cancelation rate of contested tender decisions has sharply decreased from 11.9% in 2008 to 2.2% in 2013, indicating that the Board has begun to significantly disregard complaints. Second, the capacity of the Turkish Court of Accounts that reports criminal acts in the area of public procurement was limited for effective external audit in 2012. Finally, with unprecedented solidarity, all political parties represented in the Turkish parliament reached an agreement to reduce sanctions for those involved in mischief during the public tenders in 2013. All of these developments may undermine the oversight structure and implementation of public procurement policies.

Regarding EU-funded projects, the tender results of 66 works contracts with a value of €867 million have been analysed for this report. Mean and median values of market shares are about 1-2% and do not suggest a systemic risk of collusion or corruption. However, when market shares are split according to the nationality of winning companies, the dominant position of Turkish companies in EU funded tenders is quite observable.

The government has frequently appealed to public-private partnerships (PPPs) in recent years for the delivery of large-scale infrastructure investments (e.g. airports, bridges, roads, electricity generation and distribution facilities etc.). PPPs are exempted from public procurement law. They are instead subject to their own procurement procedures which vary across different sectors and PPP methods (e.g. build-operate-transfer, long term lease, and transfer of operation rights). Due to the large capital requirements as well the necessity of significant experience in construction, there have only been a few players in the PPP projects, which makes the formation and maintenance of collusion easier. Seventy-two PPP contracts with an investment value of €53 billion have been put to tender in sectors such as airport and highway construction, and electricity distribution and generation since 2008. These contracts have been awarded to 62 companies, which submitted a bid individually or collectively. Eight companies control 82% of the market. The unique characteristic of these business groups is that they allegedly put capital into the so-called "pool media" which was established by the request of top-level government representatives of in order to secure control of a media giant, Sabah-ATV. Mega projects requiring billions of Euros failed to gain adequate funding; therefore, crucial elements of PPP contracts were renegotiated and revised in order to boost the project value after they had been signed. For instance, loan guarantees were introduced in order to increase the bankability of previously signed projects. In a similar manner, previously signed contracts benefited from tax exemptions introduced after they had been signed, and the cost savings arising due to the contract revision. If the winning companies had strategically underbid (or overbid depending on the award specifications of the tender in question) with the advantage of being informed about the aforementioned changes before the tender, this would be a cause for concern.

Concerning contract-level data, a big challenge emerged. The Turkish Public Procurement Agency (PPA) publishes tender results in a non-standardised manner. As such, it does not allow us to properly evaluate the procurement sector according to the guidelines in WP8 (i.e., mean/median market share of the companies that participate in all (relevant) public mean/median share of public procurement income in total income of these companies). To this end, Hacettepe University officially demanded the standard data from the PPA in July 2014, but this request was not fulfilled. Furthermore, we have personally contacted representatives of the PPA for the same purpose; nevertheless they have been unwilling to share the requested data with us.

As far as the reporting data on all procurement winners in the construction sector and descriptive data analysis are concerned, there was still a big challenge to compile firm level procurement data. Furthermore, due to the constraints/restrictions stemming from business confidentiality, we were also unable to compile financial and institutional statistics of companies. We also cannot observe donations to electoral campaigns, or financial contributions to political parties, because there is almost no serious regulation and institution to track these donations and contributions, not to mention the lacklustre implementation and enforcement of the existing rules and regulations.

Recently, Public-Private Partnerships (PPPs) have been used principally to build up large- scale infrastructure projects (e.g. airports, bridges, roads, electricity generation and distribution facilities etc.). PPPs are exempted from public procurement law. They are instead subject to their own procurement procedures which vary across different sectors and PPP methods (e.g. build-operate-transfer, long term lease, and transfer of operation rights).

II. CONSTRUCTION AND PROCUREMENT MARKET DEVELOPMENTS

The share of public construction expenditures constituted around 17-20% of total public expenditures over the 2008-13 period. The sum of public and private construction expenditures accounts for roughly 8-9% of GDP in the same period. The private sector's share in the total construction expenditures (e.g. 5-6 % of GDP) is twice as much as corresponding public expenditures (e.g. 3 % of GDP). It is thus reasonable to suggest that the construction industry in the country offers considerable business opportunities to both domestic and foreign contractors (Column I in Table 1).

Table 1 Construction and Public Procurement Markets (%)

Years	Construction (I)			Share of public procurement in GDP (II)					
	Share of public construction in total expenditures	Public construction/ GDP	Private construction/ GDP	Central government (1)	Local government (2)	Sub-total of (1) and (2)	SEEs (3)	Total	Share of works contracts in total procurement
2008	19.0	3.2	6.3	3.3	2.7	6.0	1.1	7.2	38.2
2009	16.6	3.1	4.7	3.1	1.6	4.7	0.9	5.6	37.1
2010	18.3	3.3	5.1	2.6	1.7	4.2	0.7	4.9	34.5
2011	18.2	3.2	5.9	2.7	1.5	4.2	1.4	5.5	52.5
2012	16.9	3.2	5.8	2.6	1.9	4.5	1.3	5.8	57.2
2013	19.8	3.9	5.2	2.8	2.0	4.8	1.3	6.1	60.0

(1) general and special budgetary agencies and social security institutions

(2) municipalities, special provincial administration, local administrative unions and municipality-owned companies

(3) State Economic Enterprises

Source: Ministry of Finance, Ministry of Development, and Public Procurement Agency

The share of public procurement as a percentage of GDP remained within a range of 6-7 % in the investigation period with a declining tendency. Although its proportion of GDP is lower than the EU (which is about 15-16 %), it still makes up significant part of the Turkish economy. The share of central government procurement in GDP (about 3%) is higher than that of local governments (on average 2%), indicating that public expenditures are rather centralized in the country. Procurement of SEEs accounts for about 1% of GDP. Public works contracts constitute a larger part of total procurement with a growing tendency, and its share in total was 60 % in 2013 (Column II in Table 1).

III. LEGAL AND INSTITUTIONAL FRAMEWORK

1. Public procurement regulation

Public procurement in Turkey is regulated by Public Procurement Law N. 4734 enacted in 2002 and put into force in 2003. The stated objective of the PPL was to achieve alignment with EU procurement directives. Table 2 summarizes key features of the PPL. It is important to note here that the scope of public procurement was initially expanded in a substantive way compared with the repealed procurement law through removing/repealing dozens of regulations involving exemptions for a number of public contracts. In line with the basic principles of public procurement, the PPL requires procuring agencies to ensure transparency, competition, reliability, confidentiality, public supervision, and efficient use of public resources. Furthermore, a number of provisions were inserted into the new law setting and/or clarifying the rules determining technical specifications, tender call notices, tender commissions and selection criteria. Besides, competitive tender procedures were introduced and identified as a basic procurement procedure. The PPL also involves certain provisions regarding building integrity in public procurement. Last but not the least, as an administratively and financially autonomous oversight body the Public Procurement Agency was established and empowered to regulate and monitor procurement rules and procedures. The decision-making body of the PPA is the Public Procurement Board. Its nine members are required to have no past or present connection or affiliation which could conflict with their task, including relations with any political parties to ensure their impartiality and fairness.

Table 2 Turkish Public Procurement Reform in 2002

Reducing margin of discretion of procurement officials	Increasing integrity
Standards/Transparency <ul style="list-style-type: none"> scope of law was expanded basic principles involved transparency, competition, equal treatment, confidentiality, public supervision and efficient use of resources minimum elements of technical specifications, qualifications, procurement notices, standard tender documents and contracts were specified mandatory publications of procurement notices selection and evaluation criteria were objectively determined and pre-announced 	<ul style="list-style-type: none"> all kind of corrupt practices were prohibited corrupt bidders were prohibited from participation in coming tenders and subject to criminal investigation corrupt officers were subject to a disciplinary punishment and criminal prosecution disclosure of confidential information was not allowed conflict of interest was prohibited Oversight <ul style="list-style-type: none"> an independent regulatory agency was established

<ul style="list-style-type: none"> ▪ unsuccessful bidders to be informed about finalized tender results ▪ procurement proceeding should be recorded and kept for all procurements ▪ tenders commissions consisted of at least five members <p>Competition</p> <ul style="list-style-type: none"> ▪ open tender and restricted procedures were prioritized ▪ restrictions were introduced to limit non-competitive bidding procedures (e.g. direct and negotiated procedures) 	<ul style="list-style-type: none"> ▪ agency was an administratively and financially independent entity at the central government level to monitor and supervise public procurement rules and procedures
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Source: Authors' compilation

2. The differences between Turkish and EU procurement rules

Although the PPL has attempted to adopt main principles and procedures in line with EU procurement directives, certain contradictions still persist. For example, there are important variations between PPL and EU Directives concerning the exact scope and content of such concepts as concessions, public contracts, contracting agencies, and exemptions. The PPL includes a domestic price advantage up to 15% to support domestic bidders against foreign competitors. Additionally, tenders below certain thresholds may be closed to foreign involvement. Perhaps more importantly, the PPL has been amended mostly for the purpose of introducing new exemptions which are not allowed by the EU procurement directives. Therefore, not all public contracts are covered by the PPL. Especially, the political big-ticket projects or the procurement of public agencies in charge of mega projects have been excluded from the scope of PPL. Last but not least, Turkey has not yet taken the required steps for the alignment of the EU utilities directive, as well as the legislation for concession/PPP contracts.

3. Impartiality of tender commissions

The contracting officers authorized for spending and carrying out public procurement in the contracting agencies are in charge of appointing members of tender commissions which consist of at least five commissioners and in odd numbers. A tender commission shall include two specialists on the subject matter of tender, and one expert responsible for accounting and finance. For instance, when a tender involves a works procurement contract, the tender commission must include at least two civil engineers and one financial officer. At least four of the commissioners are supposed to work as full-time employees for the contracting agency. A tender commission should convene with the participation of all members and make its decisions by majority voting. The PPL does not allow members to remain noncommittal. Dissenting members are required to submit written statements.

Although the PPL contains explicit provisions for the establishment and working conditions of tender commissions, it remains silent on how to ensure commissioners' autonomy against improper influences which can manipulate and distort tender outcomes. For a start, commissioners who disobey improper requests may be unseated for any reason (e.g. she/he can be assigned/re-assigned to different positions) before the procurement process concerned is completed. There appears to be no mechanism to block such potential improper actions related to the commissioners' tenures. Second, the tender commissions may consist of members who have a superior-subordinate relationship in the workplace independently of responsibilities in the tender commissions. Thus, the former might force the later to meet improper demands in order to support a favoured bidder by exercising their superiority over subordinate(s) through threats to block promotion in their careers¹. Furthermore, asymmetric information and transaction cost problems may arise, because tender commissions are required to be separately composed/appointed for every single tender. On the positive side, the replacement of members of previous commissions by new ones may make it difficult for interest groups to capture commissioners, because the time and monetary cost of engaging in corrupt activities would increase as long as the rate of commissioners' substitution is high, engendering information asymmetry between new commissioners and interest groups. On the other hand, frequently unseating commissioners may impose transaction cost on public contracts, because each new commissioner needs to spend extra time and effort to ascertain how to efficiently carry out procurement procedures².

4. Evolution of procurement law

This PPL has been in force since 2003, being initiated by and implemented over the years during the ruling of consecutive Justice and Development Party governments (*Adalet ve Kalkınma Partisi*, AKP, post-2002 incumbent), with much help from the bureaucrats mostly appointed by the same party. In other words, the PPL and its implementation have not passed the test of being audited and managed by another government party. The AKP government has made amendments in the PPL over time, claiming to increase competition and transparency, and to achieve further alignment with the EU procurement rules and procedures. The PPL has been repeatedly amended over the same party rule to the point that it has significantly deviated from its original structure over the years³. Some amendments might have really improved competitive conditions and increased value for money in public procurement. However, it seems that a large part of the changes enacted to date has imposed much higher costs to the public by actually restricting competition and transparency.

¹ In the workshop held by Hacettepe University on the subject matter of WP4 and WP8 in September 2014, one participant stated that the president of one of state universities entrusted himself in the tender commission so as to allegedly manipulate the outcome of tender.

² Note that it is still possible to assign the same officials for different commissions.

³ The 35 amendments having been made for 11 years have changed 135 sub(provisions) of the PPL. In this context, ex-president of Turkish Contractors Association Eren (2010) declared by going a further step that the PPL would be needed to be comprehensively revised to get a well-structured legislation in order to improve value for money in public procurement.

5. Eliminating Corruption Risks

5.1 *Electronic Public Procurement Platform*

Amendments of 2008 introduced provisions in order to enable the PPA to establish an electronic platform with the hope of increasing transparency and competition so as to ensure integrity in public procurement. The E-procurement platform (Electronic Public Procurement Platform-EPPP hereafter) officially started operation on 10 September 2010 and has successfully evolved up until now. All tender documents from contract notices towards tender results are required to be published in the EPPP⁴. It has eventually engendered two crucial outcomes. First, the preparation and publication of tender documents have been standardized so that procurement officials are no longer allowed to misinterpret them. Second, although the EPPP hardly allows online bidding except for the framework agreements in the health sector, tender call notices above the threshold value of €67,600 are required to be published through its electronic bulletin. Therefore, it is possible to say that transparency and competitive conditions have been improved in public tenders, although to a limited extent, because more candidates have been enabled to get electronic information about tender calls across the country, perhaps resulting in more participation in public procurement.

5.2 *Abnormally low tenders*

The PPL initially introduced a new concept, the rejection of abnormally low bids (ALB) in line with EU directives. Within this concept, tender commissions are required to identify the ALBs compared with other bids and estimated cost calculated by the contracting agency which is also required to keep it confidential. The owners of ALBs submitted are required to explain the economic and technical nature of bids in writing, and to verify how they would fulfil their offers. As a result of this evaluation process, the bids whose written explanations are found insufficient or the bidders who fail to make a written explanation are rejected. Remaining bids are accepted as valid.

Tender commissions enjoyed broad discretion to evaluate and reject ALBs, likely resulting in the rejection of lower bids and the selection of a favoured-bidder with a relatively higher bid. The trick to discriminate between bidders, and to support a favoured one was working as follows: in suspected cases, the contracting agencies were artificially calculating estimated cost much higher than real market conditions that bidders should normally take into account while preparing bids. Therefore, a high number of bids were likely becoming abnormally low except for risk averse bidder(s) with higher bids. A contracting agency with broad discretionary power was able to accept only the expression of the single (favoured) bidder whose bid's status would then move up from the ALB towards the lowest bid enough to win the tender concerned⁵. In other

⁴ Transactions that can be performed in EPPP involve publication of contract notices, preparation of the contract document, downloading the contract document, verification of tax liability, balance sheet and income statement information, social security premium debt information of the economic operators.

⁵ For instance, Istanbul Water and Sewerage Administration (İstanbul Su ve Kanalizasyon İdaresi, İSKİ) a subsidiary of Istanbul Metropolitan Municipality (İstanbul Büyükşehir Belediyesi, İBB) called tenders for the construction of a water distribution network with an estimated cost of TRY 21.2 million in the past. 43 out of 57 bids were considered as abnormally low. İSKİ

cases, a contracting agency was able to directly identify all bids as abnormally low only lower than the bid of a favoured bidder who would become the winner of the tender⁶.

Eventually, an amendment in 2008 improved evaluation process and considerably limited the discretionary power of tender commissions by introducing an objective criteria set for the evaluation of tenders. The PPA has been also authorized to prepare detailed guidelines regarding how to deal with ALBs, it has also published a larger set of rules and procedures.

6. Emerging Risks

6.1 Exemptions

A growing number of public contracts seem over the years to have been left out of the PPL. We have estimated the size of exemptions by calculating the difference between the actual volume of expenditures of central and local governments on goods, services and works contracts and total public procurement of said procurement agencies on the same areas. The difference between two figures indicates the potential amount of public procurement exempted from the PPL which is about 4% of GDP in 2013. In monetary terms, representative amount of exemptions have jumped from €9.1 billion in 2008 up to €24.8 billion in 2013, indicating a growing tendency (Table 3).

Table 1 Potential Size of Exemptions in GDP (%)

Years	Total expenditures of central and local government/GDP	Total procurement of central and local governments/GDP	Exemptions/GDP	Amount of Potential Exceptions (Billion €)
2008	7.9	6.0	1.8	9.1
2009	8.5	4.7	3.7	16.6
2010	8.2	4.2	3.9	21.6
2011	8.1	4.2	4.0	22.2
2012	8.2	4.5	3.7	23.0
2013	8.8	4.8	4.0	24.8

Source: Ministry of Finance, Ministry of Development, Public Procurement Agency, and authors' calculations

approved the viability of only single bid among the rejected bids with an amount of TRY12.2 million the owners of which have allegedly maintained close connections with top level politicians for years. Note that, the bid envelopes submitted were opened in front of all bidders participated in the tender in order to secure transparency. Most probably with an advantage of being informed about the value of other failed bids, the winning company authorized one of failed companies with a bid value of TRY9.6 million as a sub-contractor. Interestingly, before the award, the contracting agency had not been convinced with the explanation of sub-contractor which then successfully completed the awarded network construction. Thus, winning company presumably gained an easy-profit not less than the difference between its own bid and the sub-contractor's bid submitted earlier -i.e. TRY2.6-(Gürek, 2011; pp. 56-7). We are unaware of whether the winning bidder incurred any other cost paid covertly. Winning bidders of such tenders are called as 'bag-man', because they transfer works contracts to a sub-constructor shortly after winning tenders without engaging in the construction work.

⁶ In another tender carried out again by the İSKİ for the construction of wastewater network and collector, the threshold value for the identification of ALB was calculated as TRY10 522 350.00. The difference between the threshold value and winning bid (TRY10 522 350.01) was only TRY1 cent. Allegedly the winning bidder was a close friend of top managers of İSKİ (the PPA Decision Date Jan. 11, 2006 and N.2006/UY.Z-3143).

Exclusions seem to have been introduced on an ad hoc basis. Many public officials seem willing to avoid PPL procedures and the review mechanism of the PPA. Therefore, individual ministries have frequently introduced new exemptions on an ad hoc basis. In that sense, they have attempted to convince parliamentarians keen to please the constituents to get support by promising that the large part of society would get easier and quicker access to the public services such as coal aid, the supply of electricity and railway services, and provision of certain health services, when the exceptions are enacted. Thus the public contracts in such areas have been removed from the PPL. Besides, big-ticket projects⁷ and/or agencies responsible for these kinds of projects are also excluded from the scope of the PPL. The procurement procedures of exempted contracts are quite flexible compared with the PPL⁸ making them more susceptible to corruption. Although the expenditures of public institutions are finally audited by Turkish Court of Accounts, flexible procurement rules may still reduce the efficiency and effectiveness of audit. Accordingly, one should need to be aware of those flexible and uncontrolled procurement principles and procedures are usually prone to the abuse⁹.

6.2 *The use of non-competitive procurement procedures*

The scope of special conditions enabling the use of non-competitive tender procedures (direct and negotiated procedures) has been enlarged. Therefore their use has significantly increased overtime. Table 3 corroborates this suggestion. For instance, the use of restricted procedure has grown from 2% in 2008 to 10 % in 2013. Moreover, the share of direct procurement¹⁰ in total has increased from 7% in 2008 to 21% and 12% respectively in 2011 and 2012, and backed to its initial value of 7% in 2013. Conversely, the proportion of competitive open procedure in total has sharply dropped by 8%, from 81% in 2008 to 73% in 2013 (Row I in Table 4).

One of main goals of the EU procurement directives is to improve competitive conditions in the single market. Conversely, Turkey appears not keen to benefit from international competition in procurement markets. The PPL involves a specific provision which enables contracting agencies

⁷ For instance, 2011 Winter Universiade Olympics with a cost of €225 million; IMF-World Bank İstanbul Summit with a cost of €107 million (Ironically, IMF-World Bank along with the EU as external anchor forced Turkey to undertake the EU procurement directives with an objective to remove exemptions among others in public procurement in the wake of 2000-01 financial crisis); Fatih project aiming at putting a tablet computer on the table of every student in elementary schools with a cost of € 2.8 billion in total; organization of G-20 meeting to be held in 2015 with a cost of €365 million.

⁸ While defending the exemption of G20 meeting from the PPL, an AKP's deputy said that "we would need to become flexible against unexpected developments, because it is a huge organization. For instance, if we rented 50 luxury automobiles and used just 10, we would be held accountable for the unused 40 cars under the PPL provisions" (Kuvel, 2014).

⁹ Regarding outcomes of tenders of exempted public contracts, the narrative of 2011 Winter Universiade is really noteworthy. Three of five ski-jump towers, built in for the 2011 Winter Olympics collapsed in July 2014 and two other towers became almost useless. The tender of ski-jump tower was awarded to a Turkish construction company. The winning company was required to sink between 25-50-meter-long steel piles into the ground to support the towers of ski-jump. Instead, it first poured concrete into the tower foundation then sank only a one-meter-long pile in it, according to experts (Alagöz, 2014). The company had long been a sub-contractor before the AKP governments, and then has allegedly become one of the fast growing companies in the country over the AKP era, undertaking 40 tenders with an average value of € 3.5 billion due to close connections with high level decision-makers according to Özay (2014).

¹⁰ Direct procurement enables the contracting agencies to purchase their needs directly from the sole supplier through negotiating about technical terms and price under certain conditions.

to apply a price advantage up to 15% for domestic bidders¹¹ in works procurement. Furthermore, the procuring administrations may¹² enable only domestic bidders to participate in public tenders in cases when the estimated costs fall below the threshold values¹³.

Row II in Table 4 again provides information with respect to international participation in total public procurement. The share of internationally competitive procurement in total has dropped from 68% in 2008 to 63% in 2013. In other words, 37% of total procurement is closed to international competition in 2013. Furthermore, the domestic price advantage has been extensively used. The proportion of public procurement with domestic price advantage in international tenders has significantly risen from 15% in 2008 to about 40% in recent years. On the other hand, the international competition for works contracts has traditionally been far lower, and its share in total works procurement has remained within a range of 55-58%, except 39% in 2010 (Row III in Table 4). Domestic price advantage in international tenders has been more extensively used in works contracts as well. Some 50-60 % of works contracts open to foreign participation have recently used domestic preference. Turkey's growing interest to protect domestic bidders against international players may however backfire in the common market while helping consolidation of some domestic actors¹⁴. Moreover, the lack of foreign competition may mitigate efficiency in public procurement, facilitating opportunistic behaviours between domestic bidders and procurement officials¹⁵.

6.3 Reducing sanctions

Corruption in public procurement requires collusion among politicians, bureaucrats and businessmen. In 2013, the country witnessed unprecedented solidarity between ruling AKP on the centre-right and the main opposition Republican People's Party (*Cumhuriyet Halk Partisi*, CHP) on the centre-left. Under this solidarity initiative, two parties along with the support of other smaller parties, National Movement Party, (*Milliyetçi Hareket Partisi*, MHP) and Peace and Democracy Party (*Barış ve Demokrasi Partisi*, BDP) unanimously amended Turkish Penal Code Law N. 5237 (TPC) in the Turkish Grand National Assembly (TGNA) in order to reduce the term

¹¹ Domestic bidder means Turkish citizens and legal persons established in accordance with the Laws of Republic of Turkey.

¹² The threshold value of works procurement was about €11 million in 2014.

¹³ The law amendment of 2013 made optional domestic price advantage of up to 15 % compulsory for medium and high-technology industrial goods. The amendment introduced offsets which allow the contracting agencies to request compensating measures if goods are not produced domestically. The change contradicts the EU *acquis* (European Commission, 2014).

¹⁴ In this respect, in its Country Assessment Report of 2012, SIGMA (2012: pp. 30) informs that "[i]n the absence of any agreement, the use of domestic preference by Turkey is mirrored by the exclusion of Turkish economic operators from some of EU procurement markets". If so, restricting international competition to support domestic bidders in Turkish procurement markets may apparently harm the wealth of domestic constructors who qualify for participation in the European procurement markets.

¹⁵ For instance, in the third lot of tender of tablet computers within the scope of Fatih project cited in footnote 7, Apple Inc. failed to qualify for financial requirements of specifications which require candidates to have certain level of revenue realised within borders of the country. Apple's Turkey operations were not enough to produce the annual turnover required by the tender specification. According to the authorities, Turkey aims at becoming a major producer and exporter of tablets and other devices in the region in coming years, due to technology and know-how transfers as a result of the Project. Therefore, they applied such a domestic preference provision to restrict participation of international giants in the tender. Eventually, a Turkish Company, Telpa Telekom won the tender with a contract value of €142 million for 675,000 tablets. Interestingly, its production centre is based in the Far East. The company imports parts such as motherboards, displays and electronic circuits and then only assemble them in Turkey.

of imprisonments imposed on the those engaging in bid-riggings in public tenders. Interestingly, the two major political parties have seldom reached such an important agreement in the past¹⁶.

In fact, the statement of the Interior Minister made at the beginning of the year 2014 provides a good insight to help us better understand the very *raison d'être* of this amendment. Between the year 2009 and the year 2013 the ministry authorized 3,861 investigations for mayors across the country (Cihan News Agency, 2014). The breakdown of this figure according to the political parties is as follows: AKP (1,682), CHP (1,181), MHP (481), BDP (199), and others (318). Allegations against mayors basically involve bid-rigging in public tenders as well as forgery of official documents and membership in a terrorist organization. Apparently, all of the political parties represented in the TGNA were not sure whether their mayors would remain clean. The relief introduced by the amendment would also be exploited by the procurement officers of central government as well as that of local administrations. On the other hand, the data provided by the Ministry of Justice upon request of a parliamentary inquiry submitted by a deputy of the MHP (Topçu, 2014) show that the number of bid-rigging convictions has increased by 75% from 1,115 in 2009 to 1,947 at the end of 2012. When taking into account the message signalled by the solidarity of political parties represented in the TGNA in the amendment process, it is reasonable to suggest that launching an investigation for the bid-rigging allegations would hereupon be hampered, while mischief in public tenders would be implicitly tolerated.

6.4 Appeal mechanism

An important particularity of the PPL was the establishment of the Public Procurement Agency and the introduction of appeal mechanism for bidders who claim that they have suffered from a loss of a right or damage. The PPL requires unsatisfied bidders should first submit a complaint to the contracting agency concerned. If they are still disappointed from the agency's decision, they are thereafter able to appeal to the PPA.

The first members of the PPB were appointed before the AKP had taken office in 2002. The AKP governments completely reshuffled formerly appointed board members in 2007. The appointment criteria of board members are allegedly the relations to the AKP's cadres rather than merit. As a result of such political appointments, the PPB has allegedly begun not to consider some award decisions as a violation of law in recent years, which were regarded as infringement by ex-members of the Board. The policy shift of the PPB regarding appeal decisions are explained as an attempt to ignore or tolerate irregular procurement decisions of the central government and the AKP municipalities¹⁷. Row IV in Table 4 depicts cancellation rates of tender decisions complained in works procurement. While the PPB was cancelling 11.9% of tenders appealed in 2008, it invalidated just 2.8% in 2013. Note that the cancellation

¹⁶ Interestingly, the title of the law enacting the amendment is "Law Regarding Changes to Some Laws with Respect to Human Rights and Freedom of Expression". A journalist characterized the expression of this change as follows: "[p]ut another way, politicians are saying that the right to rig tenders and squander the taxpayer's money should be listed as a fundamental human right" (Bozkurt, 2013).

¹⁷ After reviewing tender decisions of the AKP's metropolitan municipalities and corresponding decisions of PPA on them, Gürek (2011: p. 90) suggests that the decisions of the PPB have begun to markedly change along with appointment of new board members. After the Board was completely reshuffled, in certain cases the PPB has moved away from its previous decisions which would, if applicable, have invalidated certain tender decisions of the AKP's mayors.

rate was 22.9% in 2006 which was the very last year of tenure of board members appointed before the AKP. These figures apparently translate how the decisions of PPB have shifted from protecting complainants towards safeguarding accused contracting agencies.

6.5 The role of the Turkish Court of Accounts

Concerning the external audit of public procurement, the Turkish Court of Accounts (TCA) was authorized to check, among others, regularity¹⁸ and performance audits¹⁹ in accordance with international audit standards. The Law N. 6085 which initiated to modernize the structure and functions of the TCA according to international audit standards was enacted in 2010 and amended in 2012. The amending law changed the audit remit and particularly operating process of the TCA. As suggested by SIGMA (2013), the amendment (i) limits the authority of the TCA to conduct performance audits²⁰, (ii) re-affirms the priority of regularity audit, (iii) most importantly institutes a mediation committee for the finalization of audit reports in cases where the TCA and relative public agency disagree on the matter. The mediation committee is composed of three members from the TCA and two representatives from the audited agency.

Following the amendment of 2012, the presidency of the TCA decided not to submit regular reports of auditors to the TGNA. Instead, it has begun to present its own reports which are basically prepared by the Report Evaluation Board (REB)²¹ for the Turkish parliament. As an auditor, Arslan (2013) affirms that the content of short REB reports are not clear and easily understandable, furthermore they may manipulate the findings of audit reports so as to conceal potential accusations. Therefore, the author suggests that the detailed audit reports should be presented to the TGNA along with the reports of REB²².

Upon complaint of the main opposition party CHP, the Constitutional Court has overturned the aforementioned amendment²³, and then a crucial uncertainty regarding the TCA's audit function has emerged for the time being, because a new arrangement has not been promulgated to substitute for the rescinded provision yet. This uncertainty being occurred by the decision the Court as well as the TCA's approach not to send auditor reports to the TGNA would limit the capacity of TCA to carry out regularity and performance audit. Therefore, it is plausible to offer the approach to avoid the TCA's audit authority may represent a cause of concern.

¹⁸ The regularity audit intends to ensure the reliability and accuracy of financial reports in accordance with financial management and control systems, and the compliance of administrative transactions and spending with the relative legislations.

¹⁹ Performance audit aims at ensuring that public agencies function effectively, economically, efficiently.

²⁰ The president of Association of Auditors of Turkish Court of Accounts (Özsemerci, 2011) argued that, without performance audit, it would be difficult to check inefficiencies occurred because of corrupt transactions.

²¹ The audit reports are prepared by headships of audit groups as a result of regularity and performance audit of public administrations, while the REB is composed of the members of TCA and two chairmen of chambers and evaluates the audit reports with a critical perspective and prepare its own -shorter- reports.

²² Criminal acts which are reported by the TCA to the public mostly involve the procurement issues among others (SIGMA, 2013).

²³ The Court's decision: 27/12/2012 date and 2012/102 E., 2012/207K.

Table 4 Selected Procurement Statistics (%)

Years		2008	2009	2010	2011	2012	2013
I. Use of procurement procedures (as share in total)	open procedure	81.0	79.0	78.0	66.0	71.0	73.0
	restricted procedure	2.0	2.0	4.0	7.0	9.0	9.0
	negotiated procedure	10.0	11.0	9.0	6.0	8.0	11.0
	direct procurement	7.0	8.0	10.0	21.0	12.0	7.0
II. Foreign participation in total procurement	share of procurement open to foreign participation	68.0	66.0	67.0	61.0	64.0	63.0
	share of procurements with domestic preference in procurement open to foreign participation	15.0	21.0	21.0	34.0	42.0	38.0
III. Foreign participation in works procurement	share of procurement open to foreign participation	58.0	53.0	39.0	50.0	57.0	55.0
	share of procurements with domestic preference in procurement open to foreign participation	26.0	46.0	50.0	58.0	63.0	55.0
IV. Cancellation rate of tenders complained	cancellation rate of tenders complained	11.9	6.2	4.1	3.5	3.7	2.2

Source: Public Procurement Agency

IV. EU FUNDS

For the 2007-2013 period, the amount of EU funds provided to Turkey under the Instrument for Pre-Accession Assistance (IPA) is about €4.8 billion of which almost €3 billion has been spent for the time being. The EC and the Turkish agencies work together to evaluate the needs and select the projects which are included in the annual national programme. Procurement procedures are regulated by the “European Commission's Practical Guide to Contract Procedures for EC External Actions.”

In order to evaluate the EU funded tenders, we compiled the results of works tenders from the websites of the contracting agencies²⁴. 66 works contracts with a contract value of €867.1 million have been put out to tender over the 2005-2014 period. The average number of bids submitted in tenders is about 6.4, while the mean value of market shares of bidders is about 2%. When the two largest tenders are excluded, the average market share falls to 1%, because the market share of the top two contracts with a value of €366.8 million constitutes 42% of total. Both are railway projects, and the biggest one with a contract value of 220 million Euros was

²⁴ Central Finance & Contracts Unit of Turkey: <http://www.cfcu.gov.tr/tender.php?lng=en&action=tender_search>;
Ministry of Environment and Urbanization: <<http://www.ipa.gov.tr/TenderSearch/?Page=2>>;
Ministry of Science, Industry and Technology: <<http://ipa.sanayi.gov.tr/en/default>>

awarded to a Turkish consortium, while the smaller one which is worth about €146.8 million was allocated to a joint venture involving one Turkish and two European companies. Two European companies and two consortiums including European and Turkish companies have been involved in the top ten contracts. Six European companies individually won tenders with contract values of €77.7 million Euros and with a market share of 9%, while three joint ventures including European and Turkish companies won tenders worth about €187.3 million with a market share of 22%. The distribution of market shares do not necessarily represent a cause of concern however, it is plausible to say that Turkish companies apparently dominate in works tenders financed by the EU funds.

V. Detecting Risks in Public-Private Partnerships

Public-private partnerships/concessions have been extensively used in Turkey as well as European countries for the delivery of infrastructure investments over the last two decades. As already mentioned, unlike EU procurement directives, the PPL does not involve rules and procedures for the procurement of PPPs/concessions. Almost every contracting agency and/or every PPP model has different procurement legislations (Table 5) which are in conformity neither with the provisions of PPL nor with the EU procurement directives. Furthermore, they may create confusion and uncertainty especially for foreign bidders in PPP markets due to their different rules and procedures. On the other hand, the PPA is not in charge of exercising *ex post* control mechanism on PPP procurement, implying that the decisions taken in bidding process by the contracting agencies are appealed only to the courts where the time period of final decisions may last for years which may again reduce the effectiveness of the appeal.

Table 5 Regulations for Delivery of Public Services in Turkey

Conventional Public Procurement	Means of Private Participation	Outright Privatization Private Market Activities
<ul style="list-style-type: none"> Procurement of works, services and goods of public institutions, using public resources (2002/4734) 	<p>A) Concessions</p> <ul style="list-style-type: none"> The law dated 1910 regulates general characteristics of concessions Public services provided by local governments (2005/5302 for special provincial administrations and 2005/5393 for municipalities) Telecommunication services (2000/4502)* Privatization Act (1994/ 4046) <p>B) PPPs</p> <ul style="list-style-type: none"> Built-Operate-Transfer (1994/3996 for sectors in need of high capital resources or advanced technology; 1984/3096 for electricity generation and integrated facilities; 	<ul style="list-style-type: none"> Privatization Act (1994/ 4046) Turkish Commercial Code for corporate governance of companies (2011/6762) Protection of competition (1995/4054) Capital markets law (2012/6312) Sectoral regulations (e.g. regulations for electricity, natural gas, transport, telecommunications, and banking)

	<p>1993/3465 for highways; for public services provided by local governments 2005/5302 for special provincial administrations and 2005/5393 for municipalities)</p> <ul style="list-style-type: none"> ▪ Built-Own-Operate (1988/4283 for thermal power plants; for public services provided by local governments 2005/5302 for special provincial administrations and 2005/5393 for municipalities) ▪ Transfer of Operation Rights (1994/ 4046 for public monopolies; 1984/3096 for electricity; 2005/5335for airports) ▪ Built-Lease-Transfer (2005/ 3359 and 2013/6428 for health care facilities; 2010/ 351 for university dormitories; decree by Cabinet 2001/ 652 for schools) 	
<p>Note: The numbers in parentheses demonstrate the enactment years and numbers of laws concerned respectively</p> <p>BOT: Build, operate, and transfer; TOOR: Transfer of operation rights; BOO: build, own, and operate; BLT: built-lease-transfer</p> <p>*The name and characteristic of licensing regime in the telecom sector was changed from the concession to the authorised operator in 2008 through the Law N.5809</p> <p>Source: Authors' compilation</p>		

Concerning implementation, 72 contracts with a project value of €52.8 billion have been signed since the beginning of 2008 to the end of 2013. These contracts constitute 41% of those PPP contracts which had been delivered between early 1990s and 2013, while the value of 2008-13 period contracts accounts for 67% of the total, indicating that the government has tended to deliver larger-scale investment projects through PPPs in recent years. The project value includes two components: (i) investment value and (ii) payment commitments to the government to get an authorisation to exploit PPP/concession assets and collect usage fees that the government would have otherwise collected. Within this taxonomy, investment value and payment commitments to the government involve respectively €18 billion and €34.8 billion over the 2008-2013 period.

1. Relations between government and businessmen

Having presented aggregate data regarding PPP contracts in Turkey, we focus on PPP contracts tendered since 2008. In this context, 17 out of 72 PPP contracts were awarded to eight companies which won contracts individually in some tenders or jointly in others. The value of contracts awarded to these companies is worth about €43.2 billion and accounts for 82% of total projects²⁵. The main characteristic of these companies among others is that they are key participants of the so called 'pool media' which was allegedly formed by the request from top

²⁵ We concentrated on 17 contracts and 8 companies, because these contracts account for more than four-fifths of the total and thus can explain a very large part of game even not at all.

level government officials according to the corruption prosecution reports which targeted ministers' relatives and a group of businessmen and voice recordings leaked on 17 and 25 December 2013. According to Bloomberg (Srivastava et al. 2014) and many other sources²⁶, an attempt was made by business allies of government to secure control of Sabah-ATV media group in order to serve as the government's mouthpiece. The eight aforementioned companies were allegedly required to put US\$630 million in the pool in return for the promises to award them major government tenders including a multibillion-euro third airport in Istanbul and some other major transport and energy projects²⁷. Furthermore, it was allegedly promised by some members of government to provide loans from public banks for those who claim lack of cash money to contribute to the pool. Accordingly, the Sabah-ATV media group was purchased by one of members of the pool allegedly with the pooled funds.

All of those alleged to have participated in the pool denied any wrongdoing (Dombey, 2014). The Turkish government has described the bribery and corruption accusations as "a judicial coup attempt", launching a strong fight against investigators at police and judiciary through sacking and relocating hundreds of officials who had initiated the graft probe. The government got strong support from voters in municipal and presidential elections held respectively in March and in August 2014 as proof of renewed legitimacy, but concerns remain. In September 2014, the newly-appointed chief prosecutor dropped the corruption prosecution against all suspects including ministers, their relatives and businessmen. The reasoning behind the decision was that previous prosecutors in the probe breached judicial procedures, and conducted unlawful wiretaps and physical surveillance in order to attempt to overthrow the government (Gürsel, 2014)²⁸. Last of all, although the government has survived, the four cabinet ministers whose sons and relatives were linked to the investigation were forced to resign (Arango, 2014). Furthermore, the then Minister for Environment and Urban Planning, one of ministers alleged to have been involved in the scheme, announced his resignation from Cabinet and Parliament, further calling on the then Prime Minister Erdoğan to resign because most of the amendments on construction plans mentioned in the investigation had been made with the then Prime Minister's knowledge (Hürriyet Daily News, 2013)²⁹. Finally, a parliamentary investigation commission established to examine the graft allegations decided not to commit for trial four former ministers accused in a corruption investigation on January 5, 2015, and TGNA subsequently approved the Commission's decision.³⁰

²⁶ See among others, Cengiz (2013), Freedom House (2014), Rethink Institute (2014) and sources cited therein.

²⁷ Besides, the members of 'the pool media' also allegedly made donations, upon request of top level decision-makers, in the form of both cash and real estate to the Turkey Youth and Education Services Foundation (Türkiye Gençlik ve Eğitim Hizmet Vakfı) whose executive board is composed of relatives and close friends of the then Prime Minister (Gürsel, 2014).

²⁸ Incidentally, the then Prime Minister Mr. Erdoğan publicly confirmed at least one of wiretaps in which he was asking the manager of a broadcasting firm to remove an opposition politician's speech on TV (Freedom House, 2014). Note that, the relations between top level politicians and top level managers of private companies as long as revealed by the leaked recordings represent a clear conflict of interest and a cause of concern.

²⁹ Soon after, the Minister took back his resignation and apologized to the then Prime Minister.

³⁰ In the meantime, a deputy of the main opposition party, CHP, directed a parliamentary inquiry (Oran, 2013) to the then Prime Minister in order to ask whether a minister on behalf of him had asked millions of US dollars in bribes from a group of businessmen known to be close to the government for the acquisition of the Sabah-ATV Media Group. As of this writing, the inquiry has been yet unanswered.

Indeed, in the end, the companies alleged to have participated in the scheme won the new airport tender of Istanbul as well as some other major tenders in the transport and energy sectors. Furthermore, they stand out as the winners of large-scale public tenders over the last decade. Although the establishment of these companies goes back years, their growth has gained great momentum in recent years. As stated by Buğra and Savaşkan (2014: p. 89), privatization, public tenders and PPPs have been important means of business development for certain companies including those involved in the alleged media pool. Furthermore, the authors generalize their argument by claiming that the government's role in shaping the areas of lucrative business has become more significant in recent years.

VI. RISKS IN PPP CONTRACTS

Having surveyed more than 1,000 PPP/concession contracts granted in Latin America and Caribbean Region, Guasch (2004) offers that the extent of corruption matters in designing and implementing PPP contracts. If the bidders believe that the government counterpart is subject to influence, and then the renegotiation and capture of additional rents are possible, they will be more likely to strategically overbid (or underbid depending on the award criteria). If the expected renegotiations and revisions emerge, they would undermine the integrity of a PPP contract, reduce efficiency and distort social welfare. The study demonstrates that the contract renegotiations in the surveyed countries are common and mostly profitable for private companies rather than for the government partner. This is to certain extent true in Turkish experience as well.

PPP contracts give the private operator the right only to collect revenues. Since PPP assets are still owned by the government, they cannot be pledged against loans which are expected to finance the project concerned. The only asset to be used as collateral is the revenue stream of the project³¹. Besides, the governments generally retain a right to early termination of the contracts under certain conditions. If the government terminates a PPP contract before it expires, the creditors have no right to the revenue generated in the remaining period of the original contract. These limitations inherent in part of the PPP/concession contracts increase re-payment risks, raise capital costs and affect overall financing conditions. Therefore, the private partners are keen to maintain a friendly relationship with the government during the contract design and implementation, implying that both parties may be prone to engage in an opportunistic behaviour.

In this context, some large scale PPP projects had been long unable to qualify for the needed project finance. Therefore, the Law on Regulating Public Finance and Debt Management N. 4749 and the Law on Build Operate and Transfer N.3996 were amended with an objective to provide loan guarantees for PPP projects in 2013. Within the framework of the new guarantee scheme, the government will undertake the relative debt in the events in which PPP contracts are terminated before their expiration date, and then take over PPP assets in question. The maximum percentage of guarantee is 85% of remaining debts, if the contract is terminated for

³¹ Indeed, the net present value of a PPP project cannot truly be estimated at the beginning in certain cases, because demand and corresponding revenue may largely fluctuate overtime.

the reasons arising from the failure of the operator, 100% otherwise. Furthermore, the newly introduced guarantee scheme has been also granted to previously signed contracts which had been still unable to put altogether the needed private finance. In this context, a consortium including companies involved in the pool media alleged entered a BOT (Build, operate, and transfer) contract with the government for Gebze-Izmir Motorway & Izmit Bay Crossing Project with an investment value of €4.9 billion in 2010. It had been long unable to attain the level of funding needed in international markets to fund the road construction. Therefore, the council of ministers granted to it a debt assumption guarantee backed by the Turkish Treasury in 2013 years after the contract signed.

This is not the only legal change which affects financial conditions of PPP contracts after they signed in favour of the private operators. For instance, the Law N. 3065 was amended in 2012 to introduce value-added tax exemptions for PPP projects. The stated reasoning of amendments was to improve the bankability of PPP contracts, accelerate their realization, and deliver public services in question on time. Even if these arguments are valid, it is still plausible to claim that the expected benefit of competitive tender being executed long before the amendments took place would have been significantly reduced if the winning bidder had strategically overbid or underbid to enter a PPP contract with an expectation or assurance of revising it at a later stage³².

It is a well-known fact that PPP/concession contracts have frequently been revised in Turkey, but their nature of confidentiality seldom enables the third parties to evaluate financial consequences of the amendments. Fortunately, we still have open sources which may signal risks regarding the contract revisions. In this respect, the new multi-billion Euro airport tender of İstanbul, which was won by a consortium including companies involved in the “pool media” in 2013, represents an interesting case. The tendered airport's estimated cost is about €28.9 billion of which €6.7 billion is investment value and the rest €22.2 billion will be paid to government by the consortium as annual rents over 25 years starting when the airport is set to open. The airport project has long suffered from lack of funding like many other PPP projects, and will likely benefit from debt assumption guarantee as well. Most strikingly, the BOT contract of the airport was allegedly revised to reduce investment cost. According to the news reported by Boyacıoğlu (2014) reaching the desired elevation level for the airport, which is planned to be built on an area with many old open-pit coal mines that must be filled, requires around 2.5 billion cubic meters of filling material. After the contract was signed, the elevation level of the airport has been allegedly reduced to lower the amount of filling material needed³³. A deputy of the main opposition party CHP submitted a parliamentary inquiry (Acar, 2014) to the Minister of Transport, Maritime Affairs, and Communications in order to request (i) whether the elevation level was reduced by 30 meters which may carry out cost savings amounted to 2 to 3 billion Euros, (ii) why the

³² Şimşek (2012) informed that some of failing bidders had claimed that they would have submitted higher bid, had they been told that technical and financial specifications would be changed in this manner.

³³ In fact, in a newspaper interview, one of the members of the consortium said, “we would build up the airport much cheaper than its estimated cost, that's why we did not get nervous in the tender. If we had had a foreign partner, we would seldom have submitted a bid at such a high level” (Güngör, 2013). This member's tax debt of €151.6 million was allegedly cleared through reconciliation in 2010 as well (Today's Zaman, 2014).

revision of elevation was made shortly after the tender, and (iii) what else changed other than identification of winners after the tender³⁴.

Last but not the least, the Turkish Court of Accounts (2012: pp. 22-4) reported that while transferring operation rights of electricity distribution companies, millions of Euros were left in the bank accounts of the companies on the transfer day. During transfer of operation rights of distribution networks, the cash accounts of distribution companies were underreported, and non-reported accounts were not taken into account in the valuations, and eventually transferred to acquiring firms. On the other hand, the report stated that compared with previous months, electricity usage was also significantly underreported in the bills a month before the contract date, then the non-reported usage was then billed by new private-operators, causing a wealth transfer from public to private party.

VII. Concluding remarks

In this report, we have first quantitatively explored construction and procurement markets of the country through nationwide data. We have then moved on to investigate and document legal and institutional structure of public procurement and its evolvement. Although the PPL was initially to some extent in line with the EU *acquis*, its structure has been significantly altered from the original due to frequent amendments. The EU-funded tenders have also been generally reviewed. According to the tender results of 66 EU-funded works contracts reviewed, it is not possible to suggest that there are systemic irregularities to rig bids. Despite this, it is still observable that Turkish companies maintain a dominant position in the EU-funded tenders. Lastly, we have dealt with public-private partnership (PPP)/concession contracts which have been used with an objective to deliver large scale infrastructure investments, and are significantly prone to corruption risks.

The Public Procurement Law was put in force in 2003 with an objective to improve competition, transparency and integrity. Although it had some limitations compared with the EU directives, its enactment was really a positive step in a country where irregularities in public tenders were frequently encountered. It has been implemented under single party -the AKP- rule for years, and been repeatedly changed so that its shape has significantly deviated from the original structure.

The most striking feature of amendments is the frequently introduced exemptions. Dozens of public contracts have been taken outside the scope of it over time. Therefore the share of Turkish public procurement in GDP (e.g. % 5-6) is much lower than the EU equivalent (% 15-16). The exemptions are frequently introduced in order to avoid tight regulations of the PPL and oversight authority of the Public Procurement Agency. The exempted public contracts have been procured through relatively flexible rules and procedures. Note that even though the flexible

³⁴As of this writing, the inquiry has been still unanswered within required period of time. However, the Minister of Transport, Maritime Affairs, and Communications informally asserted in the press that all bidders before the tender were informed about that a change can be made in the elevation level of airport project through an addendum, if needed at further stages of investment. Moreover, he noted if a cost saving emerges from a change in the elevation level, it will certainly enter into the state's finance (Hürriyet Daily News, 2014).

procurement rules and procedures may expedite procurement process, they are still prone to opportunistic behaviour. Furthermore the use of non-competitive tender procedures such as direct procurement and restricted procedure has been on rise while the use of competitive open procedure is declining. In the meantime, the foreign participation in public tenders has decreased and the price advantage to domestic bidders in international tenders has been extensively and increasingly used in recent years.

Unlike the EU regulations, the PPL does not include procedures and provisions for the delivery of PPP contracts/concessions. However, one of the crucial policy objectives of the government is to deliver especially large scale infrastructure investments through PPPs. The legal structure of PPPs is very fragmented, implying that almost every sector and model has its own procurement law which is largely incompatible with the PPL and the EU regulations. Not surprisingly, smaller group of companies which have allegedly close connections with top level politicians win PPP projects worth billions of Euros. In other words, the public procurement and PPPs have likely become significant means of business development for particular enterprises developing close relations and affiliations with high level representatives of the government.

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Project profile

ANTICORRP is a large-scale research project funded by the European Commission's Seventh Framework Programme. The full name of the project is "Anti-corruption Policies Revisited: Global Trends and European Responses to the Challenge of Corruption". The project started in March 2012 and will last for five years. The research is conducted by 20 research groups in fifteen countries.

The fundamental purpose of ANTICORRP is to investigate and explain the factors that promote or hinder the development of effective anti-corruption policies and impartial government institutions. A central issue is how policy responses can be tailored to deal effectively with various forms of corruption. Through this approach ANTICORRP seeks to advance the knowledge on how corruption can be curbed in Europe and elsewhere. Special emphasis is laid on the agency of different state and non-state actors to contribute to building good governance.

Project acronym: ANTICORRP

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