Ádám Török – Ágnes Győrffy – Ilona Hernádi*

Public procurement, competition and protection of the state's financial interests

PUBLIC PROCUREMENT AND ECONOMIC TRANSPARENCY

The purpose of the research and the concept of public procurement

What would *Michelangelo's* Pieta or David be like if they had been procured under the rules relevant for government contracts in the early 2000s in Hungary? What would have happened if Michelangelo *Buonarotti* had been excluded from the procedure, because he had failed to submit the copy of the certificate to prove his qualifications when corrections were requested? What would the London Saint Paul's Cathedral, the Chartres Cathedral, the Redoute of Budapest and the House of Parliament look like if a public procurement procedure had been launched for their construction? Why so many allegations, rumours and accusations and often unverified, but unceasing suspicion of corruption in connection with the Hungarian public procurement procedures? Would it really be the necessary, but costly (and according to some, not really effective) tool to reduce corruption?

In our paper we are seeking answers to these questions. It makes the study of the subject area of public procurement more difficult that researches conducted in this field are not detailed and comprehensive enough, thus offering very few fixed points for the further analysis of the topic. The majority of Hungarian researches approach this issue from a legal point of view. On the other hand, we have embarked on elaborating the subject (i.e. the system of procurements conducted from public finance resources) expressly as an economic question. After reviewing the theoretical background, and by outlining the state of affairs of the Hungarian public procurement market, the research wishes to present alternatives for the possible development paths.

Hungarian legal definition

The principal legal regulation relevant for public procurement in Hungary, i.e. the Act on Public Procurement (PP Act), originally adopted in 1995 and last amended in 2005, was made by the legislator "…in order to ensure the transparency of public spending and to improve control of the appropriation of public funds, and to ensure fair competition in the course of public purchases".

The possible objectives of public procurement

The Hungarian Act in force is clearly aimed at transparency, the "clean" use of public funds,

* The authors express their thanks to *Szilvia Nádor* for her assistance in preparing the study.

and the economic consideration, namely the regulation of competition, only appears as a secondary objective. This is apparent in practice, when looking for an employee involved in public procurement at a public procurement actor – whether a contracting entity or a tenderer – we will be referred to the legal department, or in the case of a smaller firm, to the company lawyer, or perhaps to an independent company preparing applications. Apart from very rare occurrences, public procurement is not handled by the financial, commercial or purchase department, although from the material aspect of the process, they would be concerned in it.

These presumptions support the view of economic operators that the main aim of the PP Act is to reduce corruption. Yet, back in the early 1990s, there was still an economic policy objective behind the development of the Hungarian public procurement system and regulation, but it was later lost. For the total liberalisation of imports performed in three years was not coupled with the introduction of a regulation that would have allowed for the supply-side of the Hungarian economy to adapt to the sudden change in the conditions of competition. That is why many suggested, on the basis of Far-Eastern examples and World Bank recommendations made that time, the introduction of the public procurement system in such a manner that domestic producers and service providers could compete in public procurement, at least for a transitional period, under a certain smaller level of positive price discrimination (Török, 1996, pp 163–165). Consequently, the bid price of a domestic supplier exceeding by maximum 5 per cent that of a foreign supplier would have been considered identical with the latter, but naturally all other parameters would have been judged under identical conditions.

In the Guidelines[1] concerning the use of World Bank loans for public procurement purposes, out of the four major requirements set out for sovereign borrowers, the ones mentioned first are economy and efficiency, equal opportunities of the actors participating in the procedure from any country, the development of construction and manufacturing industries of the borrower, and the requirement of transparency is only listed after them. Similar components were to be found for some time in the public procurement interpretation and practice in the European Union (El-Agraa, 1994).

Some theoretical questions of public procurement

From the perspective of economic theory, public procurement represents a special form of the market structures. There is monopsony in public procurement, but with varied forms within it. It means a different market structure when public procurement tenders are announced for a central mammoth investment and again different when bids are invites for the annual copy paper purchase of a local government. The more homogenous a tenderer (i.e. the more similar actors there are on the market) and the smaller the value of a public procurement, the more closer the procedure is to a fair competitive situation. The more differentiated the tenderer is, or perhaps the more political power it has and the higher the value of the good to be purchased, the more closer the situation is to monopsony.

Therefore, in public procurements we can hardly speak about the operation of market forces and the blessed activity of *Smith's* invisible hands, in general, among others for the following reasons:

- in the majority of cases, the procedure – save the recently instituted competitive dialogue – does not allow the iterative "approximation" of the supply and demand sides";
- products can rarely be treated as homogenous, services even more rarely;
- entry to the market cannot be considered

smooth, since the regulation of public procurement procedures has become so complicated that it makes generally necessary to involve a lawyer, and above Community thresholds, it makes mandatory to involve a public procurement expert both at the tenderer and the contracting entity sides.[2]

The exhaustive regulation aims to correct these deficiencies. As a result of what has been described above, public procurement in itself has limited ability to move the economy towards the optimal state of perfect competition.[3] What can be achieved is diminishing the market-distorting effects of corruption by guaranteeing the transparency of procedures.[4]

Laffont and *Tirole* point out that it difficult or rather expensive for the practice of shaping public procurement procedures to reflect all the requirements that can theoretically be set out. Such requirements include, for instance, quality, compliance with delivery dates, the financial stability of the winning candidate and the observance of all adjacent – e.g. environmental – regulations (Laffont – Tirole, 1993, page 560). In the authors' view, there are two main reasons why it may pose a problem. One is that the tender requirements, also expressed in money, must be adequately weighted by the tender announcer in the invitation to tender, but the weighting – even if the possibility of corruption or unlawful influence is totally excluded – may only reflect its own level of information (the problem of asymmetric information).

The other reason can be traced back to the classical problem of principal-agent[5], which is also regularly present in public procurement procedures. It occurs often that certain important tender parameters are set by the tender announcer instead of the principal, because it did not receive a sufficiently detailed list of requirements either due to principal's negligence or absence of information. According to Laffont and Tirole, both reasons may contribute to collusion between the tender announcer/evaluator (agent) and tenderers, which in the two authors' logic practically means that no fair public procurement tender is conceivable (Laffont – Tirole, 1993, page 560).

In a properly functioning democratic political system, however, this still does not mean that the public procurement procedure may inevitably cause permanent damages to the state or to taxpayers even in the long run. In principle, rational voters will withdraw their confidence from political decision-makers who manage budget resources in a wasteful or inapt manner (make inefficient transfers) (Laffont, 2000, page 9). It is, of course, doubtful that in any society rational voters can be found in sufficiently large masses to deter decision-makers from such wasteful activities. It is also doubtful whether it is worth withdrawing confidence from mismanaging politicians when there is no other group of politicians who can be expected and undoubtedly be able to handle public spending affairs efficiently.

A further theoretical problem within the operation of the public procurement system is the set of interests of the agent, i.e. the entity announcing and evaluating tenders, which not only fails to exclude collusion, but, in a more general sense, makes it more difficult for the entity to adopt a uniform strategic behaviour. For state regulatory organisations consist of three kinds of employees whose unity of interests and co-operation cannot always and necessarily be guaranteed (Viscusi, Harrington, Vernon, 2005, page 373).[6]

The public procurement procedure can also be interpreted as a situation (Eső, 1997), in which the purchase of a good (good or service) is conducted through an auction or another, centralised market co-ordination mechanism in such a way that there is a state organisation on the demand-side. The task is, as a matter of course, to determine the optimal form of purchase from the perspective of enhancing social

welfare, but in order to do so, it is indispensable to identify the type of the good.

In macro-economics, the following categories of economic goods are distinguished:

- *ordinary good:* it is homogenous, its quality is constant, independently from the producer, or information on its quality can be obtained by the buyer at no cost (for example, stock exchange commodities);
- *search good:* its quality is known before purchase, but it is expensive for the buyer to obtain information on it, or the quality is only ascertainable subsequently, after consumption, but it is verifiable before court (for example, lunch in a restaurant, fruits bought at the market);
- *experience good:* its quality or some of its components are not observable in advance, and no previous experience is available about it and it cannot be set out in a contract (unique goods, new technologies of which little experience is available).

In the case of ordinary goods, the most favourable result is attainable by the reverse auction, whose real practical implementation will be the electronic (e-) public procurement. In the case of experience goods[7], it can be demonstrated that price competition is definitely not the optimal mechanism, since the lack of experience about the quality soon leads to the appearance of counter-selection and to lower quality (Eső, 1997). Econometric models indicate that the so-called restricted auction is the best option, more precisely, the Vickrey-tender restricted by individual price floors.[8]

As regards search goods, it is hard to recommend an optimum auction mechanism, and such recommendation is not to be found in the specialist literature. This is probably the type of good where the best solution is to seek a tailor-made mechanism for the individual, specific good – the latest amendment to the Hungarian law more or less provides for that by widening the types of procedures.

The exclusion of competition does not yield the desired result even in respect of unique goods. It may be justified to apply individual treatment for experience goods, but only within a tailor-made competition mechanism for the good in question and within the framework of the law. The electronic auction, most comparable to perfect competition, is only practicable for ordinary goods.

About the history of public procurement

General history

Ever since the state as such existed there has always been public procurement, although the content of the term and the manner of regulation often changed in the meantime.

Even the ancient Greeks grasped the opportunities offered by public procurement, and it persisted all throughout the history, but right until the late 1800s the verbal form was general. This so-called auction (licitatio) procedure was an extremely effective institution. It was, however, difficult to control and was poorly documented, and publicity as a requirement of modern times was presumably ignored several times.[9] (The change in the meaning of the original Hungarian word – i.e. "kótyavetye" (squander) – for public procurement is telling.)

It was an important milestone in the history of public procurement when in the second half of the 17th century written records were ordered for public works and public supplies regarding the French royal estates. *Jean-Baptiste Colbert* (1619–1683), statesman under the rules of King Louis XIV, was the first to introduce the form of competition where bidders had to submit their bids in writing. Tendering was, however, not regular at that time. Those who became purveyor by appointment to the King could lose the orders of the court only by falling from grace and not

because of other offers of lower price or higher quality.

The first written public procurement regulations – naturally under different names in those days – date back to the 19th century, the time of the establishment of nation states and the fast-pace advancement of industrialisation. Their common feature is the advocation of protectionist economic objectives. The first laws concerning public procurement were passed between the two World Wars both in the United States and Western Europe. It was the time which saw an increase in the state's economic role and the concentration of a higher ratio of income in public finances.

It was in the 1960s that procurement acquired increased significance when its service functions related to public administration, education and health-care came to the fore. Public procurements attained an increased role and the taxpayer could feel that through publicity and controllability he had a say in the decisions taken on the use of his tax payments. Government purchases were not always conducted through tendering: the so-called system of "royal purveyors" was wide-spread. In addition to the competitive environment now becoming more general and to the requirement of efficient controllability over public spending, the growing power of more and more supply-side actors to exert legal pressure made tendering necessary for government contracts.

This trend was reinforced by the liberalisation of world trade, mainly because of the requirement of international transparency. Owing to not only an even stricter compliance with the transparency requirement but also to the opportunity to enhance legitimisation and obtain votes by the frequent reference to transparency, the attention of political elite groups was directed to the advantages to be expected from introducing the public procurement regime. The frequent reference to the protection of public funds, as well as its justification by citing legal facts are at least as essential for the future of certain elite groups as the actual protection of public funds.

The general evolution of public procurement can be summarised as follows. In the first stage, the key consideration is economy and the aim is the lowest price possible. In the second stage, the use of written records appears and documentability becomes an objective. In the third, the range of objectives is further widened, and economic policy objectives (protectionism, support of certain local groups) are added to the previous ones. Finally, in the fourth stage, the range of objectives narrows: the protectionist goals are rejected by economic liberalism. It is here that transparency and controllability gain priority.

Development of the Hungarian public procurement regulation

The first regulation, aimed at public procurement, was adopted in Hungary on 5 December 1887 governing public supply contracts in railway construction. It was enacted by *Gábor Baross,* who – as Minister of Commerce – considered the development of the domestic industry utterly important. However, this regulation can still be looked upon as a publication only intended for guidance with no real legal effect. In terms of its economic goal, it was clearly designed to be a tool of industrialisation in Hungary.

The first general regulation was published in 1893 under the title 'Rules regulating the authorities' acquisition of the needs of industrial and agricultural products and the contracting out of industrial works'. The first binding legal regulation dates back to 1907. The Industrial Development Act of 1931 and later the Public Supply Regulation concerning public procurements were conceived as a part of the new economic policy after the Treaty of Trianon. The latter[10] was drafted in a completely new structure, which to date has a significant influence

on Hungarian public procurement codification. For unlike the foreign systems, the Hungarian one provides a single regulation, in a code-like form, for governing the domain of the public procurement law with special regard to the subjects and objects of procurement. These are separately regulated in other legal systems.[11]

The goal of the regulation also changed. While earlier Hungarian regulations placed the emphasis on the development of the manufacturing industry, the new provisions envisaged the protection of craftsmen and the small industries they represented. The Public Supply Regulation governed the details of the tendering procedure, the terms of delivery, the rules of taking decisions on bids, the quantitative and qualitative acceptance, and introduced the most favourable bid as a method of evaluation.[12] The fundamental function of the Public Supply Regulation continued to be strict market protection. As with other European countries, the market of public procurements was extremely closed at that time. From today's perspective, the Hungarian purchase obligations were regulated with almost astonishing stringency.

For a period of fifty years after the war there had been no regulation in Hungarian law which provided a comprehensive coverage of the area of public procurements. There was, of course, control over the purchases conducted by the heads of state and local government institutions, but the potential direction and other main characteristics of purchases were determined principally through informal channels.[13]

Ministerial Decree 14/1982 (IV. 22.) already contained the declared aim of guaranteeing the fairness of competition, yet compared to former regulations of similar purport, this legal regulation treated the field of purchases generously. The regulations, in effect for less than five years, were replaced in 1987 by Law-Decree 19 of 1987, which failed to clearly define even its own scope. The law-decree set especially high thresholds, and included no prescriptions for the conclusion and fulfilment of contracts, nor did it impose sanctions for their infringement.

This situation was to end by the birth of Act XL of 1995, the former Public Procurement Act, as amended from time to time, which breaking with the socialist traditions went back to the Code of 1934.[14]

The Europe Agreement, signed on 16 December 1991, was an important document preceding the formulation of the 1995 PP Act[15]. Article 67 of the Agreement set out the general requirements of legal harmonisation for Hungary, which naturally also applies to the area of public procurements. Based on all the above, the PP Act, coming into force on 1 November 1995, incorporated the fundamental rules of Community Directives, but also taking account of the rules of the GATT/WTO government procurement codes and the rules of the model laws of INCITRAL (the United Nations Commission on International Trade Law) and even some components of the Hungarian Public Supply Regulation in force before the Second World War. The old PP Act required lesser or greater changes, which were basically justified by the general experience gained in the operation of the law but the amendments also kept in mind the requirements of legal approximation, especially as regards the voluminious Act LX of 1999. The 2003 revision of the Act was necessitated by Hungary's accession to the European Union and by the legal harmonisation with EU legal principles. A new public procurement law was created, i.e. Act CXXIX of 2003, followed by further amendments in 2005.

By examining the process of how the Public Procurement Act, adopted in 1995, was created and the parliamentary debate over it, we can see that one of the key objectives was local industry protection, which signifies the appearaence of an expressly protectionist intention. By

recalling the developments of the political-economic transition, it is understandable and even justified that the legislators of a country struggling with high inflation, unemployment, the rapid decline in production and with the indebtedness and insolvency of Hungarian producers who are very often unable to compete with the foreign capital entertain protectionist thoughts.

As *Pál Vastagh*, then-Minister of Justice, has put it the essence of the 1995 Public Procurement Act is the following: organisations constituting part of the public finances or receiving financial aid or allowance from central or local budget resources may conclude contracts for the purchase of goods, construction projects and services in excess of the set threshold exclusively with the winning tenderer in the public procurement procedure. Based on the parliamentary debate of the darft-law, the objectives of the PP Act are: "By establishing the rules for purchases form public funds, the draft law identies three principal considerations:

- *ensuring the effective use of public funds;*
- *giving an opportunity for the protection of the Hungarian market: in a transparent way, but only granting temporary preference to goods, services and construction projects which are of Hungarian origin and have Hungarian labour behind them;*
- *guaranteeing enforcement of the directives set out in the Europe Agreement and their incorporation into the Hungarian legal system; guaranteeing national treatment."*

The 2003 amendment makes changes to the objectives: the protection of the Hungarian market is excluded, whereas controllability is added to the objectives specified in the 1995 Act. The largest group within the fields of procurement constituting exceptions is the national defence expenditures. This was an exception during all periods of the regulation and, as a matter of course, it is not likely to change[16]. The purchase of almost HUF 60 billion made by the Ministry of Defence in 2005 represented 4 per cent of the total Hungarian government purchases.

Public procurement regulation of the European Union[17]

The Treaty of Rome, i.e. the Treaty establishing the European Economic Community,[18] set the goal of developing a common – later single – internal market which ensures the free movement of goods, services, persons and capital. No express provision for government contracts is includeed in the EEC Treaty contains with even the term "public procurement" missing from its articles. So for long, the area of government contracts had not been looked upon by the Member States as a component of the internal market and as one that falls under the scope of the four freedoms. The individual Member States considered government contracts practically as the last tool of national market protection (since the prohibition of subsidies is expressly stated in the Treaty establishing the European Economic Community). However, in the mid-1980s, Community institutions were to realise that there was hardly any liberalisation in the public procurement market. Thus, only two per cent of public contracts – although publicly announced – were awarded to contracting tenderers from other Member States. So the Community institutions set the aim of creating new public procurement directives. In the 1990s, a number of directives providing more stringent regulation for public procurement were launched, but they continued to strive for only establishing a so-called regulatory minimum. In 2002, the Common Procurement Vocabulary (CPV) was created.

In the interest of implementing liberalisation, Community legislators found it indispensable that certain questions of public procurements should be regulated at Community level

(including, in particular, the announcement of public procurement tenders, evaluation of the submitted tenders). Consequently, the Community-level regulation of public procurement is not focused on ensuring the transparent and controllable use of public funds, the fight against corruption and the rationalisation of national expenditures.[19] Rather, the key objective of this Community regulation is to create the single market and to ensure its operation, and to prevent the situation in which government contracts are exclusively won by local bidders. This is designed to guarantee that tenderers residing in different Member States could compete under equal conditions in the award procedures of "public contracts" within the huge European market of public procurements.

The broadening of the Community public procurement market in such an extent may easily lead to the fast increase of market concentration which may result in the exclusion of small and medium-sized enterprises from the market and in the establishment of an oligopolistic market. Community regulation should thus help the realisation of effective government purchases, as well as the prevalance of the multi-faceted supply-side.[20] A further argument behind opening up the market of public procurements is that, as generally thought in the EU, the earlier protection of state markets significantly contributed to certain high tech sector' lagging behind the world market (typical examples: information technology, telecommunication industry). Due to discrepancies in the national standards, European companies manufactured, on average, three times as many types of the same product as their American competitors, and this proportion was fourfold in relation to the Japanese.[21]

The price-lowering effect of public procurement procedures was really well measurable in the case of certain types of goods and services. The purchase prices of telecommunication equipment were down by 20–30 per cent and those of electrical installations by 30–40 per cent[22]. At the same time, it is usually difficult to demonstrate the beneficial effect of the creation of the Single Internal Market in the field of public procurements. According to a Eurostat-survey cited by *McDonald* and *Dearden* (1999), merely 9 per cent of the enterprises operating in the industry felt that the opening up of public procurement among the Member States had a positive impact on their business activity, 71 per cent experienced no changes, while 4 per cent reported a negative impact.

The expansion of the Community market was also facilitated by international agreements, in particular, the Government Procurement Agreement (GPA) formulated under the auspices of the World Trade Organisation (WTO). The application of the most-favoured-nation treatment is already stipulated in the second – modified – public procurement agreement, which came into force in 1996. The GPA covers central government institutions, as well as a considerable part of regional and local institutions and a rather large proportion of public utility companies. Apart from the acquisition of goods, it regulates public procurements aimed at services and construction projects.

The changes incorporated in the Community Directive, adopted in February 2004, also impose obligations on Hungary to modify its legislation. This was provided for in the 2005 amendments. The major changes include:

- EU thresholds have been simplified;
- new methods of procedure have been launched: the competitive dialogue and the framework agreement;
- changes furthering the spread of electronic procurement techniques have been introduced: deadline allowances, the launch of a dynamic procurement regime and the so-called electronic auction;

- out of public utilities, the postal services sector has been included in and telecommunications excluded from the scope of the regulation.

As regards national treatment, the new Directive sets out the obligation for tender announcers to ensure the equal treatment of tenderers established in EU Member States. The possibility of granting national treatment to non-Community tenderers and non-Community goods is regulated by the effective international agreements of the Republic of Hungary and the European Union. The Directive is a legal regulation applicable above the EU thresholds, which are relatively high from Hungarian point of view[23]. Below EU thresholds, only the opportunity is granted to apply a regulation conforming to the Directive in respect of procedures whose values reach or fall below national thresholds.

Electronic public procurement

The advance of information technology makes it possible to use new methods for public procurement, and thereby establishing and applying new purchase mechanisms. The concept of electronic public procurement may, however, represent several forms. The successive development stages of e-procurement are as follows: (World Bank, 2001).

1. Public procurement publication system (in all countries of the European Union)
2. Tender documents (for example Canada)
3. Electronic tender parallel with submitting the document (in a few countries of the European Union, Australia, Mexico)
4. Fully electronic publication, tender, processing of tenders, contract signing (to our knowledge, this form is not yet operational in any country).

The European Union's SIMAP internet-based system is the closest and compulsory example to follow by Hungary. SIMAP represents the lowest level of the four stages, and provides a practicable model for countries along the path of electronisation. This information system operates reliably so far, handling altogether 100 000 announcements annually in the approximate value of EUR 10 000 000 000 000. SIMAP is planned to be further improved to serve the fourth, i.e. the electronic, stage as well.

Since the launch of SIMAP, the time required for processing and publishing announcements has dropped. SIMAP has also contributed to cutting costs. Based on estimates, the use of the system has resulted in a reduction of the administrative costs related to public procurements, on average, by EUR 100 per procedure, and by about 1 per cent of the average value of tenders. One per cent does not seem to be a significant sum in the case of low-value purchases, but it is not negligible when high-volume purchases are concerned.

Several lessons can be drawn by Hungary from the EU's present practice of e-public procurement.

- The efficiency of the system is rather low without highly qualified and motivated personnel who have excellent knowledge of both the public procurement and electronic systems.
- Appropriate computer and internet usage are pre-conditions for all procurement actors, therefore it is worth considering that small tenderers should be given assistance in this respect (support, full or partial reimbursement of costs, interest-subsidised credit).
- However cost-intensive it may be, it is indispensable in the initial phase to operate the electronic and the paper-based tender announcements side by side.
- It is important to involve the procurement actors of both sides in designing, building and testing the system;
- In respect of more advanced (second and higher-stage) systems, the conditions include availability of an electronic signature already

executed by the person concerned and security coding.

◗Ongoing training, further training, exchange of experience for the procurement actors of both sides, with special regard to tenderers, since e-public procurement, as the necessary information will be forwarded to the contracting entity through the government programme.

◗Finally, *Carayannis* and *Popescu* (2005) highlighted the importance of communication and information flow, which help access to the best examples.

The EU's bureaucratic, yet economically beneficial public procurement practice demonstrates considerable efficiency advantages, among others, probably due to the huge market size. In the case of major government contracts, the enterprise-size makes automatic selection among candidates, since smaller actors would not be able to fulfil the given high-volume contracts. On the other hand, such a selection is less frequent on small national markets, so there it is the task of the government contractor and/or the public procurement regulation to carry out such preselection.

About corruption

It is generally believed that in Hungary public procurement is linked to corruption. This fact could be well illustrated by data from specialised economic literature, as well as on the basis of personal questionings, if we think of some of the Hungarian public procurement scandals which hit the headlines in the 2000s. The connection between public procurement and corruption, however, deserves much more careful considerations. Mainly, because there are two important points where this connection may come into the focus in analysing public procurement.

The first is that one of the underlying reasons behind the rather complicated and costly system of public procurement is to prevent corruption, i.e. to make community-purchases more transparent. The second is that in several cases it is precisely the seemingly fully lawful application of a given public procurement practice or method that may arouse the suspicion of corruption, in other words, it may happen that the public procurement system itself gives rise to corruption. In the area of managing public property, situations that are most likely to tempt to corruption can be categorised as below[24]:

- public procurement,
- privatisation,
- party financing,
- state subsidies.

Public procurement is thus only one of the areas concerned, but in some experts' view, the one that is most likely to lead to the risk of corruption.[25] There might be a close relation among the above-listed areas also in the occurrence of corruption. For instance, if the public procurement procedure, which has not been executed in a truly transparent manner, serves basically party or other political financing purposes. Let us suppose that the contracting entity for a large infrastructure investment is selected through public procurement procedure, and it is among the hidden award criteria of the procedure that the candidate is expected to be willing to transfer a certain percentage of the contract fee to companies previously designated by the government contractor (e.g. for expert opinions or communication services), and a part of the income received by such companies goes to political parties. Such type of corruption is difficult to corroborate because, in most cases, the very public officials who committed the crime of corruption are the potential source of information, or they are authorised to declare as business secret the information needed to uncover the truth.

In the public procurement procedures accompanied with corruption the delivery of goods or services ordered does take place in every case, so it is not the matter of throwing the money out of the window without consideration. It is true, but in such cases the government purchase is obviously made under unfavourable conditions. The corrupt sale of an asset or unfair assignment of powers may cause similar or even much more severe damage. Of the above-mentioned areas, public procurement is governed by a uniform and high-level regulation which ensures the greatest transparency and fastest remedy. For this reason, it takes a relatively short time to throw a light on the violation of the regulations in public procurement events, which is then quickly and widely covered by the representatives of press who are interested in revealing the case. So corruption – or its suspicion[26] – to be found in the field of public procurements may be made public due to the very stringent regulation which helps uncovering it.

Corruption is, however, not the only illegal act that can be tied to public procurement. During the various stages of the public procurement procedures the following unlawful acts may occur:

- corruption, i.e. gaining unlawful advantage in return for a consideration;
- cartel, i.e. the price-fixing or other agreement of tenderers before submission of the tender;
- falsification, i.e. concealing or tempering with data which influence the outcome of the decision in order that a more favourable decision is taken;
- blackmail, i.e. influencing a person who can in any way affect decision-making, by posing threat on him, or on a person or asset close to him;
- "soft", yet sometimes unlawful acts which are often also part of our everyday life: flower, kind telephone call, obtaining extra information from young and apparently new colleagues by artful questions; and finally;
- involuntary violation of law arising from unprofessionality and incompetence.

Due to its nature, measuring the prevalence of corruption is rather difficult, usually only estimates can be made. Two professionally accepted methods are available for the measurement: expert opinions and questioning the interested parties and the public opinion in the course of researches.

György Várday believes that almost 10 per cent of Hungarian public procurement procedures can be considered completely fair. i.e. corruption- and cartel-free.[27] Others hold the view that bribery and collusion can be revealed in about half of the procedures, with 40 per cent originating from violation of law due to incompetence[28], and only the remaining 10 per cent being entirely lawful[29].

One of the most recognised efforts to measure corruption was made by Transparency International. The method is not only aimed at public procurement, but it endeavours to measure the perceived levels of corruption in the public sectors of the countries under review.[30] Hungary received five of the ten CPI (corruption perceptions index) scores in 2005. Although it indicates a slight improvement against the figures of last year, its absolute value shows the corruptibility of the public sector and reinforces the sceptical expert opinions in connection with public procurements.

A study prepared by the Foundation for Market Economy in 2003[31] points out that the following few factors may be instrumental in decreasing public procurement corruption:

- amendment of the Act on Public Procurement in order to have an opportunity to evaluate long-tem and well-functioning purchase relations;
- adoption of the Lobbying Act[32], which would create a clear situation, at legislative

level at least, and help separate lobbying activity from corruption.

The cited study also reinforces that the current legal regulation is of a sufficient level to suppress corruption, and its further reduction would be difficult by administrative means. The State Audit Office is also of the opinion that there is no need to render the Public Procurement Act more rigorous as a whole and to narrow down the legislators' scope for action.[33]

In foreign specialised literature, *Celentani* and *Ganuza* (Celentani – Ganuza, 2002) have analysed the relation of corruption and optimal public procurement mechanisms with econometric tools. They have concluded that the increase in competition could lead to an increase in corruption.[34] Results of other research fields demonstrate that from a more general point of view, corruption should not necessarily be looked upon as the wrong that is to be wiped out completely. From the aspect of behaviour biology, an important role is attributable to corruption in evolution (Tóth, 2003).

ABOUT THE PRACTICE OF PUBLIC PROCUREMENT (EMPIRICAL RESULTS)

Numerical facts concerning Hungarian public procurement

The volume of Hungarian public procurements has shown a continuous growth since 1996. There are estimates for the preceding years, because there had been no accurate data gathering before such type of activity was regulated by the Public Procurement Act.

During the parliamentary debate of the first Public Procurement Act the aggregate value of economic activities relating to public procurement in 1994 was estimated at HUF 270 billion by *László Keller.*[35] In 1996, the aggregate value of public procurement procedures conducted on the basis of the new Act was stated at HUF 150 billion by the Public Procurement Council. On the other hand, the total value amounted to HUF 1291.3 billion in 2005. The so-called simple procedure, applicable below national thresholds, is likely to further augment this value by approximately HUF 200 billion, i.e. by 2005 the overall value can be estimated at HUF 1500 billion, about 10 per cent of GDP in the year under review.[36]

In EU-comparison, this ratio can be regarded as average. According to the figures presented on the official homepage of the European Union dealing with public procurements, which is not updated too frequently, in 2002 the aggregate value of EU public procurement activities was EUR 1500 million, 16 per cent of the union's total outlet. Data relating to Member States vary from 11 to 20 per cent.

In the majority of the Member States there are no separate Community and national thresholds, whereas in Hungary there is a significant difference between the two levels. The share of the public procurement procedures exceeding the Community threshold was 26 per cent within all Hungarian procedures in 2005, but in terms of their value they represented about 75 per cent of that of all public procurements, i.e. 7.5 per cent of the annual GDP.

Construction projects came to 40.5 per cent of the 2005 value of public procurements, services to 34.3 per cent, and the remaining 25.2 per cent represented the purchase of goods. Within the entrepreneurial sector, micro-, small- and medium-sized enterprises won nearly 70 per cent of all procedures, and 41 per cent based on their value. Their proportion will presumably be higher within simple procedures, but there are no precise data available on them yet. In 2005, 95 procedures were awarded to non-resident tenderers representing 2.5 per cent of all procedures and 15.4 per cent of their total value.[37]

Methodology of interviewing

We have conducted in-depth interviews to reveal and evaluate the state of affairs in this special market. The in-depth interview does not give an opportunity to obtain standardised answers and to process them statistically (as a questionnaire), at the same time, the fact that the subject matter of the examination with hardly any history of research justified our focusing on unique cases and unusual problems.

◗We have tried to describe the characteristics of this market with the help of analysing the in-depth interviews. The data survey was conducted between September 2005 and December 2005. During the survey 35 persons were asked from the same number of economic entities.

◗We have conducted in-depth interviews with the actors of the Hungarian public procurement market whom we consider important. We have collected direct information concerning the opinion of market actors. We have analysed the statements, experience and attitudes of the interviewees in connection with the research theme, taking into account their special way of thinking.

◗Methodologically, we have endeavoured to survey market actors in the widest circle possible, at the same time aiming at gathering forward-looking opinions and proposals. In the interviews we have attempted to reveal the similarities that may signify malfunctions of the public procurement system, but we have also summed up the differences which have structured even this small sample.

◗We have collected responses as to what market actors deem as problematic areas and the weaknesses of the system, what they think about the regulatory and institutional system, the operational mechanism and future development potentials of public procurement. We have asked what the responders think about the PP Act, whether they find it suitable for implementing the specified objectives, namely whether the law ensures transparency, encourages efficiency and generates competition in the market, and which are the areas where it fails to be effective. The responders have expressed their view about the information level of market actors, about the official databases, the willingness to apply remedies, the electronic public procurement solutions and tecniques and to what extent they are aware of them.

The results of interviewing

When analysing the interviews, we grouped the answers and problems according to the basic principles laid down in the Preamble of the Act on Public Procurement. Although these are difficult to discuss separate from one another, we have set up four major groups.

◗Transparency and publicity

◗Rationality, efficiency, equal opportunities and competitiveness

◗Controllability and the institutional system

◗Electronic public procurement

The latter has been treated separately being one of the most essential direction of development.

Transparency and publicity

The first questions of the interviews related to the definition of public procurement. Looking at it as a definition question, we could see that the interviewees (except one) interpreted public procurements basically as an economic question, as a special question of procurement. They believed, however, that in practice it was mainly approached from legal point of view. One of the possible explanations to this general, legal approach is – in their view – that in Hungary the subject matter of public procurement falls under the Ministry of Justice, and therefore *"the area is in the hands of lawyers"*.

The principal aim of the public procurement procedure is to ensure the transparency, comtrollability and efficiency of public spending, as well as the fairness of competition in such a way that none of the aims should be prioritised at the expense of the other. It is generally believed that Hungarian legislators have not been able to achieve this delicate equilibrium. In the responders' opinion, one of the main weaknesses of the system is that it is inflexible, too bureaucratic and not clear enough. With a view to avoiding corruption, legislators have created such a rigorous system that has an adverse effect on efficiency and, in many cases, on the professionally reasonable selection.

There was also general agreement among those questioned that an extremely strict and cogent[38] law in itself cannot ensure transparency. *"It is easier to create a prohibitive law"*, yet this principle strictly and clearly means that neither the contracting entity nor the tenderer can apply or incorporate in the particular public procurement procedure any rules contrary to the provisions of the law by citing that the law fails to prohibit them (even if both parties consent to it), and the law alone is not capable of entirely rid public procurement of corruption. In the judgement of many, it is a wrong assumption that corruption can be eliminated or significantly curtailed merely by strict laws.

Despite the fact that Hungary's public procurement law is widely regarded by representatives of the profession as one of the most stringent laws in Europe, the law alone is apparently not able to establish a transparent and fair public procurement environment without social consensus, the involvement of the public and really consistent political will. The Public Procurement Act is a good example for the birth of a set of unjustifiably strict rules for the sake of enhancing transparency that cannot put an end to corruption but makes it considerably difficult to attain efficiency in the process of public procurements. "*Very simple but creative rules should be made. Under normal circumstances, for instance, on one condition can a factory be built on the river if the site of water intake is lower than that of water discharge. Simple as that.*"

When examining the reasons for overregulation, it seems advisable to review a group of arguments of political economy. Driving back corruption in a democratic political system is not a moral issue, but rather it is the matter of economic incentives. Decision-makers, or more precisely, legislators are not only motivated by the opportunity to enhance efficiency and to use public funds more economically in declaring war against corruption (which means effective counter-corruption combat at best), but also by the pressure to gain popularity and obtain votes. It is therefore reasonable for them to adopt a behaviour that makes the political elite's commitment to counter corruption credible in the eye of a growing number of actors in the political market. So they consider it just as important that the majority of the society believes in the determination of the political leadership to eliminate corruption as the actual effectiveness of the fight against corruption.

To make this behaviour credible, it seems a good strategy to concentrate the counter-corruption regulation on the areas in which even the public opinion suspects a frequent occurrence of corruption. At the same time, the boundaries of the concept of corruption are not defined by society as a whole, but by the political elite who will then determine the directions of the counter-corruption regulation accordingly. By quoting Hungarian examples: the counter-corruption regulation – including the public procurement system – is strikingly permissive in respect of the confidentiality section of the business agreements concluded with government participation (i.e. permitting the exclusion of publicity from the evaluation of

such agreements), whereas it rather strictly insists on the practically unnecessary technical details of public procurement tenders.

Consequently, public procurement is clearly an area in which the political elite try to assure and win the support of the public with strong counter-corruption regulation (or the semblance of it). The implicite suspicion against the public administration may, of course, hit back, for the public could ask how much it can rely on a government system which, in the first place, starts with the assumption that its lower levels of public administration are vulnerable to outside influence, and therefore deprives them from the opportunity to take market-based regular decisions when decisions are made on the purchases needed for their organisational operation.

The price decline achievable due to large quantities contracted in advance is naturally a significant advantage of the public procurement system. This may, however, be countered by the impact of periodical monopoly positions on driving prices up in such a way that when concluding public procurement contracts the contractor may in principle force out a much lower price than the current market level, however, in periods of decreasing prices (for example, on markets undergoing liberalisation and integration or in the case of products showing fast technical development) it prevents the demand-side from adjusting to the price decline. The price decline due to large quantities contracted in advance may also be curbed if this price decline – or price advantage – is not measurable or interpretable in the case of highly differentiated products.

An often mentioned example of overregulation is the limited application or even the penalising of negotiated procedures, as a result of which the number of such procedures is falling year by year in Hungary. The proportion of open procedures is around 80 per cent in the county, a very high percentage in comparison to the average 55 per cent of EU Member States. It is a mistaken view that there is a higher risk of the incidence of corruption in a negotiated procedure than in an open procedure.

The interviews make it clear that even an open procedure may give rise to corruption, for instance, when preference is granted to a particular company through "a tailor-made call for tenders" (by requesting special references or specifying qualification requirements). Most of the responders came across with such an incidence, but there were a few who stated that they had regularly encountered this problem. So the open procedure is lacking the kind of flexibility (which could in many cases minimise the risk) that is based on a more informal information exchange between the contracting entity and the tenderer and could lead to a long-term relationship built on security. It often poses a serious problem in public procurements that no long-term co-operation can be formed during the procedures. This is not permitted by the Act even in the areas (such as services), where it would be justified. This probably helps understand why many believe that a more frequent application of the negotiated procedure could improve the efficiency of public procurement without the increased danger of corruption.[39]

One of the interviews reflected an astonishing view: 90 per cent of Hungarian public procurements are unfair and unprofessional. This standpoint cannot be automatically brushed aside if we consider that this statement connects the concepts of professionality and fairness. The responder must have meant that poorly compiled public procurement tenders giving priority to bureaucratic requirements are often professionally far from being satisfactory.[40] For this reason, they cannot be considered fair, because the government contractor has to make do with a low-priced, albeit professionally not necessarily satisfactory bid and it can hardly apply higher professional criteria

in selection than published in the tender criteria. Selection on the basis of outstanding quality is virtually totally excluded according to the logic of the Hungarian system effective in 2006.

The majority of those polled think that the absence of legal security and the constant change in the regulatory environment *("Sixty amendments in a year and a half, it is unacceptable!")* are generally the reasons behind an unprofessionally conducted public procurement procedure rather than the unfairness of the actors involved. Nevertheless, both the contracting entities and the tenderers believe that from the aspect of corruption, the invitation to tender is the area most prone to criticism (signifying the huge responsibility of tender announcers), and in the course of the procedures contracting entities are the first who may become aware of market irregularities. Based on the experience gained from numerous public procurement cartels, the Economic Competition Office offered its assistance to contracting entities to help them recognise the market segmentation, as well as reveal collusions.

The responders identified as the greatest problem that despite several amendments, there is still a great deal of uncertainty, for example, in certain questions governed in the special provisions of the Act. Moreover, some voiced the opinion that since the coming into force of the new Public Procurement Act (i.e. Act CXXIX of 2003), the regulation had become really complicated, almost untransparent, and thereby especially difficult to apply.

It may lead to a problem of legal interpretation that it is not clearly defined whom and what the rules are applicable to, and there is a large number of references in the law. It is an often cited prescription, for example, that each candidate is to obtain a certificate in proof of the due payment of taxes towards government agencies (e.g. atomic energy agency) with which the candidate could have no contact whatsoever because of his professional profile. As a consequence of the complexity of the procedures, the rigorous prescriptions, the required certificates and statements, the onerous administrative duties and of overdocumentation, now the procedures often only undergo legal interpretation to the detriment of professional content. In many instances, attention is focused on a single consideration: *"to comply with the formal requirements of the system in self-defence."* In view of the strong competition, it may happen that the candidate offering an unrealistically low price had won the tender on the strength of that criterion, and later the government contractor was not able to enforce his qualitative requirements vis-a-vis the candidate.

The majority of responders believe that the judgement of public procurement is affected by the kind of media publicity that very often focuses on professionally groundless news which gives a one-sided report by solely covering scandals and abuses. These are suitable for reinforcing the view that public procurement is equal to corruption. Naturally, there was general agreement among the responders that publicity and the awareness of public opinion are vital parts of the smooth functioning of public procurement.

As a rule, the responders (with one exception) share the view that despite its weaknesses, the public procurement system is still the most suitable tool for ensuring the transparency of public spending as opposed to other procedures conducted without it. All were in agreement that this was true even if everyone thought there was a need for a change, especially, in attitude and approach. Noone believes that the public procurement market can be made corruption-free by mere legal regulation. The dominant part of the responders expressed their absolute certainty that the state of affairs would be far worse in Hungary without the

Public Procurement Act. Opinions were, however, divided on what an ideal public procurement regulation should effectually be like. While the system is accepted on the whole, its practice received express criticism from several aspects.

Rationality, efficiency, equal opportunies and competition

The responders all agreed that it was extremely difficult to measure the efficiency of public procurements. There are no accurate data available either in the European Union or in Hungary. The amount of the saving achievable through public procurements is a much debated question which is also shown by the diversity of opinions.

> *"Against all rumours it has a price-decreasing effect."*
> *"The fact that it's more expensive is not a problem. Democracy is more expensive than dictatorship."*
> *"Surely, it costs more than what can be saved."*
> *"The question is here what is the real weight of the lawful approach."*

It makes one ponder that one of the interviewees (a tenderer) was not willing to disclose the possible extent of the price margin arising from a public procurement. However, it was generally agreed that (although there was hardly any impact assessment available on the subject) the simpe public procurement procedure should be abolished, because small purchases are specially expensive and thereby not activating the market.[41] *"In the case of small purchases, publicity is needed rather than public procurement." "It is an irrational category."*

Some expressed the view that it was an unnecessary requirement to take account of the Hungarian acquisition value, only the EU's set of rules should be applied. The majority were of the opinion that the Community thresholds are very high for e.g. construction projects, and in this way very few projects would fall under the public procurement procedure (excluding also local government investments), and *"this country is not prepared for it"* yet. On the other hand, several of the responders argue the justification for discrimination in the field of services and the puchase of goods. They think if feasible to abolish the Hungarian system, since there is scarcely any difference between the national and Community value limits.

The introduction of new, higher thresholds, effective from the year of 2006, was welcome by most public procurement actors (it is especially true for the fourhold rise in the simple value limit of purchasing goods and services!). One tenderer, however, believes that this may give rise to the appearance of loopholes. A contracting entity questioned in the interview identified the value limit at HUF 10 million, below which no significant saving can be made, but above that a contractual price may be even 30–40 per cent lower than the expected (=market) price in the case of professional services. It was highlighted though that as a rule, the lower bids for construction projects represented detriment to quality.

The responders, without exception, believe that the public procurement market will never be as efficient as the profit-oriented sector, but it could be far more efficient than today. *"There is a need to approximate the private sector"*. The main problem is that Hungarian public procurement is principally treated as a legal and administrative issue, thus its economic aspect is being ingnored; namely, the project approach is missing from the treatment of public procurement. In this context, public procurement would begin with preparation, followed by invitation to tender and concluded with post-analysis. Another obstacle is the Hungarian practice, which gives priority to purchasing at a lower price over the principle of value for money, hence *"sometimes the cheap costs twice as much"*. As a matter of course, this is partly

attributable to the fact that legislators laid too much emphasis on the strong political sensitivity of public procurement and supposed that the system should in each case encourage the saving pf public funds instead of the efficient spending of them.

This problem came up often. It is rather difficult to deal with it in the case of procurements, where, let us say, preference should be given to subjective considerations (such as works of art or intellectual property). In the instances where professional quality can be tied to a person, public procurement is an unsuitable solution (think of the Mass which was commissioned, without tendering, from *Ferenc Liszt* for the inauguration of the Esztergom Basilica in 1856 …). It is not necessarily the lowest bid that is the most suitable for procuring these services. Contracting entities may find themselves in a situation in which they are fully aware that the higher bidder would be much more suitable for performing the work concerned (such as contracts for research), but because of the inflexibility of the regulation they have to rest satisfied with an inferior quality but lower offer.

While our interviewees were seeking the answer to our question as to why efficiency is falling behind of what is experienced in the competitive sector, they concluded one by one that public procurement simulates a rational purchasing activity. The rational management of public funds is expected in the field where market operators are not motivated by self-interest for spending money in the most efficient and economical manner possible.

Proposals were also made for solving this problem. According to one proposal, personal responsibility should be extended to cover the efficiency of individual purchases, and the fear from losing one's job on account of a wrong and unprepared decision could replace the absence of self-interest. As an extreme illustration for presonal responsibility, one of the responders raised that the Public Procurement Act as such would be dispensible if publicity and calling to account could be instituted in a truly accountable way in the constitutional state.

The majority of responders shared the view that public procurement is not more efficient than other purchases. The administration costs impose a great burden, the invitation to tender itself, the requesting of documentation or, for instance, the mandatory control of tender announcents. Nor does it make public procurement less costly if long-term contracts are concluded, because, in such cases, the more flexible procedures are used for short-term cannot be applied.[42]

It was stated in the interviews many times that contracting entities were often not sufficiently prepared. As a result of the absence of the necessary professional knowledge and, at times, the lack of experience, there is still a lot of unprofessionally conducted public procurement procedures. It is a generally expressed view that the invitation to tender is inaccurate. It mainly applies to the field of information technology investments where the market changes very quickly, and contracting entities (in the absence of professional competence and knowledge of the market) cannot even specify their own needs and the characteristics of the product searched.

The new legal institution, i.e. the competitive dialogue, is designed to make improvement in this area. Its usefulness and applicability were, however, not uniformely judged by those questioned. The competitive dialogue provides help to contracting entities in rapidly changing markets when dealing with complicated public procurement procedures by enabling them to define the object of the purchase together with tenderers. The aim is of course to assist contracting entities in formulating the conditions for invitation to tender and for tender documents precisely by means of collecting market

information obtained before the tender announcement.

Many say that seemed the new legal institution to be launched seems easy to apply only at the first time, for there are strict conditions for its use. It can only be used within narrow bounds and an official procurement consultant needs to be engaged, and if the tender announcer decides to conduct a joint negotiation, then the consent of all interested parties is to be obtained. Many examined the question from a totally different aspect. According to them, it is quite obvious that potential tenderers will be reluctant to reveal their buisness secrets to their rivals. The successful outcome of the competitive dialogue cannot be guaranteed for the contracting entity cannot predict how communicative the other actors will be. The assumption that this will make it easier to launch a tailor-made announcement of tender for one particular company was raised as a problem. *"It will not work. It will all be a matter of brainstorming and stealing ideas".*

Promoting the involvement of small and medium-sized enterprises and creating equal opportunities in the public procurement market as well are priority issues. Several responders also pointed out that although granting preference is forbidden in the union, well-proven and naturally legal practices are to be found in almost all countries which practices ensure that support can still be given to local enterprises in the given public procurement markets. One of the well-proven "tricks" is that the time for requesting tender documents is limited in the majority of the countries (as it is not regulated), thereby making the application and participation of foreign companies rather difficult. On the other hand, in Hungary the documents can be obtained until exiry of the deadline for submitting tenders. Many were concerned that when creating the very strict Hungarian regulation, legislators had ignored the interests of local enterprises. Moreover, these very strict regulations are not only applicable for EU public procurements, but they are also compulsory for all types of Hungarian procedures.[43]

It is a general view that smaller enterprises cannot afford tendering which requires high professional knowledge and implies disproportionately high costs so they can mainly be involved as a subcontrator in the public procurement market. However, in this defenseless situation they can almost always make a contract at an exceedingly reduced price, and often receive payment for the work performed after 60–90 days. As a remedy, it was suggested that the law should provide that once the contracting tenderer was paid by the state, he would be obliged to pay his subcontractor within 30 days. Otherwise, violation of the law committed in public procurement could be established. Many believe that smaller businesses cannot gain access to the European market, but they are slowly driven out of the Hungarian public procurement market too.[44]

The issue of equal opportunities also arose from other aspect during the interviews. Several contracting entities think that there is a contradiction between the importance of ensuring equal opportunities and the impossibility of giving preference to or exclude the enterprises that perform well or poorly respectively. It occurs often that the tender is won by enterprises (with the lowest bid) which – as it is found later – cannot fulfil the contract. The seemingly stringent regulation is unnecessarily loose at this point, since it does not allow exclusion of the enterprise with a negative reference or the preferencial treatment of the enterprise with a good performance.

A neuralgic point of Hungarian public procurement is centralised procurement. The organisations within its framework may purchase goods falling under the category of specific products through the Central Services Directorate General (CSDG). The activity of

the CSDG is unanimously judged as negative by the responders, because it creates monopoly, it is inflexible, not efficient enough and often high-priced. According to most interviewees, the homepage of the CSDG is complicated, there are a lot of problems with the publication of announcements, and the desired information flow is missing. It is often experienced that products cost comparably more than they would have cost if purchased by the given institution within its own competence. As the CSDG explains this is due to extra services and guarantees they provide (which are, in most cases, regarded as irrelevant for the institution). The organisations are occasionally obliged to buy a product that has more features and is more expensive than needed.

According to some opinions, the CSDG is interested in keeping prices high (because of their 2 per cent fee). *"The CSDG favours itself".* Many are concerned about the unsteady supply which in a given case could be detrimental to the institutions. In spite of this, none thinks that the centralised public procurement system has no justification, but many believe that it should be left to the institutions whether they want to join. The interviewees agreed that we could get a more complex picture by studying the system of centralised purchases from different angles. It cannot be disregarded that a number of higher educational institutions rejoined the system voluntarily after having been removed from the statutory scope.

Motor-vehicle acquistions represent a frequent problem in centralised procurement, since every year a different type of vehicle can be purchased in the same categories in the wake of the annually changing framework agreements. As a consequence, it is not possible to build a "fleet", i.e. a uniform motor-vehicle pool, which would be a more acceptable and cheaper solution in terms of guarantee and service. The majority of the responders believe that the main operational disorder of centralised procurement is caused by the fact that it is impossible to plan purchases. The size of the budget line is not known in due time, and thus the institutions cannot make accurate plans for their public procurement procedures.

Controllability and the institutional system

There is almost general agreement among those polled that the concept of controllability is basically absent from public procurement procedures. Internal control is conducted at few places, although it could have preventive effect and as such it would be more suitable for enhancing efficiency than subsequent control, which in the majority of cases is no longer able to mitigate damages. The interviewees specifically emphasised that, as a rule, control is not aimed at the procurement process as a whole, at the content of contracts and at the level of compliance, but rather it focuses on formal requirements, thus only concentrating on the regularity of the procedure. The comprehensive control of public procurement procedures is performed by the State Audit Office and the Government Control Office. Most responders are of the opinion that the powers of these agencies are weak and they have no official capacity, which would be an indispensible condition for enforcing the various penalties. Instead, they can only submit proposals to the Government.

The Public Procurement Council, the highest control body for public procurement, does not enjoy too much popularity. The vast majority of the responders believe that there is a need to modify the institutional system of public procurement. An often-mentioned deficiency is that the electronic publication of announcements is slow to be introduced. As a result, public procurement market actors were in a hugely disadvantageous position when they applied for supports, since from 2005, the publication of announcements exceeding 650 words can only be made electronically in the

EU. Due to the unpreparedness of the Public Procurement Council, in many cases, the procedure could not even be launched.

It was also agreed that the effeciency of public procurement is largely undermined by the continuously growing number of Hungarian requests for legal remedy. Remedy proceedings were initiated in respect of more than 20 per cent of the procedures (20 per cent in 2003, and 23 in 2004)[45], an unparallelly high ratio in Europe. The high proportion of unfounded and unreasonable remedies (according to the Public Procurement Arbitration Board, merely 40 per cent of the procedures were based on infringement[46]) disturb the operation of the market, and there is no opportunity to cut down this number, because everyone has a right to remedy.

It repeatedly came up as a potential solution in the the interviews that unsubstantiated (mala fide) complaints should be penalised. The responders could envisage penalties which prohibit the interested parties from taking part in a public procurement tender for a certain period of time. The other problem arising from the remedy request is that the party who challenges a public procurement procedure gains automatic access to all bids. In several cases, this is the real reason why remedy proceedings are initiated.

Opinions are also divided on whether the fee of submitting requests for legal remedy (HUF 150 000) is high. It is a frequently voiced opinion that the sum is not high enough to have a deterring effect, but it is too high for smaller enterprises to afford it. Many believe that it would be fair if the sum were commensurate with the given public procurement, i.e. if it were established in proportion to the acquisiton value.[47]

The public procurement remedy system consists of two levels. In the case of alleged or real infringements, both Hungarian and Community-level remedies can be applied, but the remedy of infringements is primarily pursued at national level. There are two authorities for legal remedy within the Hungarian public procurement system: the Public Procurement Arbitration Board and the Municipal Court of Budapest. The Public Procurement Arbitration Board established by the Public Procurement Council is an agency with national jurisdiction which takes action if legislative provisions are violated. All legal disputes in connection with its rulings fall under the jurisdiction of the Municipal Court of Budapest. Review of the decisions taken by the Municipal Court of Budapest can be requested from the High Court of Appeal of Budapest.

The judgement of the work done by the Public Procurement Arbitration Board shows a rather mixed picture. Although one of the legal remedy principles stresses the importance of the fast and efficient administration of legal remedies, there was only one responder who said that the Public Procurement Arbitration Board was a well-functioning, fast and efficient body. The majority consider it an extremely bureaucratic institution, where the control is confined to interpretating the law and to monitoring compliance with law. It is not process-oriented and not centred on the procedure; there is no chance for a dialogue and for enumerating professional arguments.

Several contracting entities mentioned to us in connection with the above that the Public Procurement Arbitration Board almost never accepts that subjective components are justified in the invitation to tender, but often the differentiation between one service and another or one product and another can only be made by taking account of such components. In the contracting entities' view, it is very difficult to incorporate this aspect into the invitation to tender, and they seem to be afraid of grasping this opportunity, because in their experience, the Public Procurement Arbitration Board systematically "weeds out subjective components". Thus, contracting entities have to be on the

defensive in every case. This forces them to do even more paperwork with which the legality of their procedure could be proved if need be.

The institution of the generally applicable statutory fine has been abolished (except, for example, in the event of bypassing public procurement, or if the contracting entity fails to submit the annual statistical report to the Public Procurement Council). But after investigating the circumstances, the Arbitration Board has discretionary powers on every occasion to establish whether the fine has been justified, and if so, how much it should amount to. The general experience shows, however, that the Arbitration Board imposes a fine in the case of every infringement.

Several responders were concerned about this practice because, in their view, in levying a fine it should be taken into condieration whether it has occurred as a result of wilful infringement or by mere oversight. It should be examined how much damage has been caused by the particular infringement. It happens often that a fine is to be paid for mere formal discrepancies which many named as a "collection technique". Most interwiewees deem it unfortunate that 50 per cent of the fine imposed goes to the Arbitration Board, which makes it inevitably interested in the proceeds, and thereby its business and public functions are intertwined. Many think that this is the reason why there is no penalising below HUF 1 million.

The introduction of preliminary examination was originally aimed to help the President of the Arbitration Board to take preliminary decisions on the foundation and legality of selecting the procedure. According to the law, the President of the Arbitration Board has fifteen days to carry out the examination; the very advantage of the institution of preliminary control would be quick decision-making. This almost never takes place, because the President of the Arbitration Board institutes legal remedy in nearly every case citing the presumable infringement. If it were not to take place, then on every occasion the period of fifteen days should elapse before a ruling is made on whether or not legal procedings are instituted by the Arbitration Board, and even positive decisions are not made known before that time.

The parties interested think that theere is too much workload on the President of the Arbitration Board. Fifteen days is too short a time, and due to the very high number of cases, he is not able to carry out the necessary investigations. This is the reason why he initiates and holds the hearing every case, thus extending the prodeeding by 30 or 40 days even if it is eventually deemed unjustified. Many believe that so long as the Arbitration Board struggles with the lack of capacity the system of preliminary examination will not be able to fulfil its function, because it is exactly the quick decision-making that becomes impossible.

One of the strongest objections in connection with the Arbitration Board is that commissioners are not equally well-prepared. Every so often, they give different interpretation to the same case, which clearly jeopardises legal security and makes it impossible to consider the decisions as precedents. It is exemplified by the case of the Hungarian State Railways (MÁV in Hungarian) where the case was interpreted differently in each of the three rulings delivered by the Arbitration Board. The requirement was worded that in many cases it would be desirable to restore the state of affairs before the violation of law. This could be achieved if legal remedy was delegated to the court. Should it occur, then the accelerated procedure would be a simple matter of resolve. If no decision is made within eight days and no contract can be concluded during same time the original state of affairs could be restored. Under the present conditions, 1.5–2 years pass before the particular contract becomes null and void in a civil action, and it is practically impossible to restore the original state of affairs .

The system of legal remedy relating to public procurements gives an opportunity for the parties to opt for conciliation in the case of a dispute instead of a legal remedy proceedings. Conciliators listed in the schedule held by the Public Procurement Council are authorised to conduct the proceedings. This opportunity has not been chosen in practice yet. It is not a coincidence, since in 2005 there were altogether four persons in the whole country who undertook conciliation, three of them in Budapest.[48]

From 1 January 2004, the Public Procurement Council supports, supervises and co-ordinates the training of public procurement actors. It was generally agreed that there was an increasing need for the involvement of experts in Hungarian public procurement. At the outset, it was only needed by contracting entities, but by now a dominant part of the tenderers, too, assign experts with the peparation of applications. In respect of the projects financed from EU funds, it is obligatory to employ an independent public procurement consultant for purchases in excess of the Community thresholds. It is obligatory even if there were a paid expert with appropriate profeesional konwledge within the institution.

There is now a new profession, the profession of public procurement consultants, which may be instrumental in raising the level of public procurement. Naturally, this system will make the procedure more expensive, in some cases to such an extent that small businesses will almost be excluded from the competition. A proposal was made to solve this problem: offices should be set up to prepare bids for small businesses free of charge or at a low rate, as another form of support offered to small businesses.

There was full agreement among those questioned that training was very expensive and there were countless organisations involved in it (namely 52). In spite of that there are very few good training courses; it seems that by now there is over-education even in this area. It is not true that by completing one of these courses, someone will get a job as a consultant, because this profession only provides a means of subsistance or maybe profit to a very small group of people. Opinions vary on whether there is an urgent need to unify the educational system (in a controlled way, using uniform curricula in state-financed higher educational institutions), or the natural selection of educational facilities should clearly rest with the market.

Those polled, however, agreed that the present situation is intolerable according to which there is no legal regulation relating to the issue of references. Based on the general rule, to meet this criterion it is compulsory to conduct twenty procedures, but there is no obligation that within these there should be at least one EU procedure. Similarly, there is no feedback on whether a procedure has been conducted successfully, so the twenty procedures performed may include even unlawful or incomplete ones.

Electronic public procurement

It is a characteristic feature of the state of affairs of Hungarian electronic public procurement that there is a Government Decree (167/2004), already in force, which regulates the service provider and services of the electronic public procurement system in such a way that the system developed could not be operated successfully so far. It is thus not surprising that the launch of electronic public procurement was identified as a number one priority by the responders, however limited experience is available about it. The responders are not familiar with the institution of electronic public procurement, its detailed future operation and the technical particulars ralating to its security, and many identify it with offers made electronically. There is a general lack of information and the majority of the interviewees are not aware of the European tendencies. To illustrate this: there is hardly any of them who has already taken part in an electronic auction.

The few who are familiar with the system of electronic auction, already applicable from 1 July 2006, find it a good tool if its application is not an obligation but a possibility. They also fear that this field is going to be overregulated. In their view, it may make the system unserviceable if the lauch of the procedure implies an obligation at the same time. In other words, there is no chance for backing out even if there is an insufficient number of tenderers for conducting the electronic auction. Under so severe conditions, market operators are not likely to choose this solution.[49]

The Hungarian public procurement system, which is much more rigorous than the West-European, contains a number of components hindering the advance of electronic public procurement. One is the compulsory control of tender announcements, which is only applicable in Hungary within Europe (it has, among others, financial implications, such as the financing of the Public Procurement Council). Although this ensures that the tender announcements forwarded to the Publications Office of the Official Journal of the European Union are uniform, controlled and of a consistently high standard (which generally brings credit to the Hungarian party), nevertheless this action clearly breaks the electronic process.[50] It is a meaningful fact that while the on-line tenders database of the European Union, the TED (Tenders Electronic Daily), has no paper-based verison, the electronic version of the Hungarian Public Procurement Bulletin is for guidance only, but not officially accepted.

Only three of the responders reckoned that it would not be possible to ensure secure data handling in the case of electronic public procurement. *"It is perilous! The fairness of the procedures is at stake! Let alone, it is much more expensive!"* The dominant part of the interviewees think that public procurement will not inevitably become cheaper by electronic management (data maintenance, registration and advertising fees, etc.), but it will definitely make the system more transparent and faster. However, as regards products and services characterised with standardisable and widely known quality features, some interviewees consider the electronic form (a typical example: office paper purchase) as an effective procedure to cut down prices.

It was agreed that electronic public procurement makes it possible to increase efficiency, it reduces administration costs, as well as promoting the modernisation of the market and shortening purchase time.[51] In one case, it was brought up as an argument that the advantages shown in public procurement markets may have an indirect impact on the economy as a whole in such a way that the opening up of the European public procurement market and the easier flow of information may dynamise competition.

The responders look upon it as a principal fault that there is a division in the scope of responsibilities in Hungary. For before July 2006, the Electronic Government Centre of the Prime Minister's Office and the Ministry of Informatics and Telecommunication were both responsible for implementing and launching electronic public procurement. *"It is not a coincidence that there was no palpable results even in four years."* Although nearly all interwiewees heard about the Oracle-based system development of the Hungarian Post, which had caused a great political stir, many could not or did not wish to express their view on the matter.[52] But the few who declared views on it agreed that the main reason behind the failure was the treatment of the system development as a political question. *"It is not going to be a cheap system if HUF 3–4 billion will be spent on it every time there is a change of government."* However, one of the responders believes that the system would have been capable of electronising public procurements and handling the complete ordering and monitoring process. Several favoured the decision that the system had not been authorised, since the concession right (which applied to sys-

tem development and operation alike) granted monopoly to the service provider.

The majority of the responders are aware that an action plan concerning electronic procurements has been developed by the European Commission, and its fast introduction is regarded vital by most of the Member States. The responders believe, however, that there are huge regional differences in this field, and building up electronic procurement is still in a preliminary stage even in the most developed countries. The directives merely lay down general duties, so numerous versions electronic public procurement exist in Europe.

The majority think that the system is going to be inoperational for a long time, because of the absence of both the appropriate institutional and user environements. It is commonly known that there is a strong aversion from new technologies (opponents to e-procurement include senior managers who only use the computer out of necessity and print all e-mails to read them in paper format). It is also a serious obstable that the everyday use of electronic signature is not yet wide-spread in Hungary.

THE FUTURE OF PUBLIC PROCUREMENT

The duties of public procurement continually narrowed in the course of time, by now only implying transparency and accountability. In terms of its present content, its sole role remains to be driving away corruption. This role is, however, very important from economic and social aspects even if it is not entirely fulfilled. There are several other institutions in public finances that – similarly to public procurement – were not assigned an active role, but that o problem solving or problem prevention. In our view, in 2006 public procurement falls wihin this category together with the police, health-care and the fire guard. It is a 'young' system, only established in this form in Hungary 10–11 years ago, therefore the actors involved need time to get familiar with the rules of the game. The crooks are always one step ahead than the inspectors in finding the loopholes.[53]

If we presume that the economic environment of public procurement, taken in the widest sense, is unchangeable we realise in no time that the former goals (industrial protection, promotion of local economy, job protection and job creation) will not return. However, we should not give up that there may be a change in the content of public procurement with new aims emerging.

The components of the operation to be improved

By reviewing both the theory and practice of public procurement, it seems that improvements can be made to the following components of the system in operation in 2006.

❶ The extension of electronic public procurement, the full development and operation of the service system would efficiently further transparency and controllability. After familiarising with and using the system for several years, we will be able to see how much time and operational cost-saving can be achieved through its operation. In the case of ordinary goods, the electronic price competition would undoubtedly result in measurable price reduction.

❷ We propose the following modifications should be made to the Act effective in 2006:

- when evaluating tenderers, the Act should give an opportunity to take account of long-term relationships;
- the system should be modified in such a way that the actors who proved to be correct and law abiding for a longer period of time should have less formal requirements to comply with. They should therefore not be required to obtain a tax clearance certificate, which is irrelevant in their case anyway, as well as to comply with the same

regulations time and again. In a broader sense, it should be considered to build the system on the principle of trust, namely to allow candidates to make a declaration about fulfilment of their preliminary obligations, but to impose serious penalty on those who fail random tests.

❸ The most important area which necessitates changes: dissemination of knowledge concerning public procurements and continuous information to the professional community and, in general, the public opinion. The law would make it posible to apply much more flexible and simple public procurement procedures than contracting entities very often choose, presumably, in fear of violating the law. In addition to the overjudicialised public procurement tenders, which indicate the tender announcer's excessively strong efforts to avoid risks, even the invitation to tender is unlawful. Both problems spring from insufficient knowledge of the law and the absence of wellqualified experts. Based on our relatively wide experience, heads of government offices in Hungary ignore the significance of legal specialisation within their organisation. Thus, for instance, the announcement of public procurement tenders are frequently not assigned to specialised lawyers but only to graduated lawyers, and many times obtaining qualifications in public procurement by employees is not supported.

Public procurement is a government task: it is not appropriate to leave the training of procurement actors exclusively to the market, especially if there is no efficient quality assurance in the given market, and professional further training can be launched by merely satisfying minimum preconditions. The inspection of educational and training facilities as well as the launch of central training courses would increase the number of experts who have both documented qualifications and professional knowledge covering every details as well as maybe practice obtained during training.

Further development of public procurement

The possibilities of broadening the content of the public procurement system have to be searched horizontally. New purposes need to be identified that not only affect public procurement actors but also have an impact on a large part of the economy or economy as a whole.

One of these potential purposes, also proritised by the Commission of the European Communities, is environmental protection and, within its framework, sustainability[54]. Environmentally responsible public procurement[55] means the practice when the parameters of a product or service to be purchased are set by the contracting entity of a public procurement procedure in such a way that they meet the criteria of "minimum environmental impact" in the largest extent possible.[56]

Public procurement in concerned with great many products and services. It may therefore represent a significant problem that the environmental parameters which may characterise a given good show enermous diversity. This problem can be overcome by labelling if there is of a large number of goods. The first "green" product label, the Blue Angel (Der blaue Engel), was introduced by the former Federal Republic of Germany in 1977. Today, eco-labels are used in 33 countries, sometimes maybe more than one at the same time.[57] It is no longer necessary to enumerate the green parameters when a prodedure is launched; it suffice to refer to the label, and it automatically signifies a set of parameters.

Let us imagine that the criterion of minimum environmental impact is included among the conditions of the next public procurement procedure concerning a government construction project of several billion Hungarian Forints. Let us also imagine that next year's central computer purchase specifies that only computers possessing the strictest eco-label may be included in

the tender. Finally, let us suppose that in its forthcoming vehicles acquisition the Ministry for Environment and Water gives preference to hybrid cars with low environmental impact and low fossile energy consumption, and as regards its paper purchase, the tender announcement will only apply for re-cycled products.[58] These procedures would automatically mainstream environmental responsibility in the economy.[59]

All political forces could identify principles other than environmental ones – such as social solidarity, Corporate Social Responsibility, reducing discrimination at international level – which principles could be integrated into public procurement. One of the main complaints against the public procurement system is that it is too administrative and impersonal, i.e. tender announcers and evaluators can, without any risk, stick to the letter of the law even if this may cause severe economic or other damages. Another general objection is that the system is insensitive to quality, and low price is almost the exclusive qantitative consideration of evaluation taken into account in evaluation. The proposed, environmentally and socially sensitive practice may contribute to more flexible and socially more sensitive procedures even within the given limited framework of the law.

The comprehensive modification of the Hungarian public procurement system would undoubtedly need more than the solutions which promote fulfilment of crucial social objectives but which remain within the given framework of the law. First of all, it should be clarified what strategic purposes public procurement serves as well as the hierarchy among them. Different rules are needed if the key objective is to reduce corruption, and again different if the main emphasis is on protecting public funds. It is, however, rather non-productive if the regulation and the institutional system behind it are primarily designed to soothe public opinion and to dispel suspicion, and if it wants to communicate the message that we have to put up a fight for the public funds.

One of the weakest points of the Hungarian public procurement regulation, effective in 2006, is that it wants to treat public procurements not only as a part of the market, but – to some extent – as a moral issue. Since ethical norms are generally lower in the Hungarian economy than in Western-Europe, the then-democratic governments are the slaves to some kind of regulatory illusion. The government's determination to replace ethical norms with detailed regulation will ultimately remove this system from the operation of the market, while establishing office positions and functions that hamper the very compliance with ethical norms, and thus creating a vicious circle in which a more detailed regulation appears to be the most convenient solution.

NOTES

[1] Guidelines, 2004

[2] This is referred to in the specialised regulatory literature as the overjudicialisation of procedures, a primary criterion of which is that the regulation endeavours to exclude any communication between government decision- makers and market actors in the procedures in the interest of transparency, in particular (Kahn, 1988, II. 87).

[3] For some reason, the Competition Act in force does not include the term "public procurement", although the competition law is evidently applicable in public procurement procedures.

[4] At the end of the chapter (I. 5) in our paper dealing with corruption we present a view based on macroeconomic analysis which predicts a possible increase in corruption in parallel with the growing competition.

[5] The principal is the state institution that announces its need to purchase a certain product or service, the agent is the institution or organisation that drafts the invitation for bids.

[6] The three groups: 1 the professional careerist whose long-term life strategy is linked to the regulatory organisation and therefore it is in his interest that this organisation has at least non-decreasing rights and duties; 2 the political careerist for whom the regulatory job is solely a stepping stone, and 3 the expert who adheres to professional values in the first place, and therefore puts all other – political or organisational – considerations on the back burner. An important lesson of the model is that professional employees who are motivated by professional interests can influence the decisions of the regulator and thus public procurement organisations only in a degree conforming to their numerical proportion.

[7] It is to be noted that in his article, Eső considers solely the purchase of experience goods as a public procurement task, although, as a matter of fact, all three categories of goods fall within the scope of public procurement – but we will also see later on that the proportion of public procurement procedures aimed at the construction industry and services, which predominantly means the purchase of experience goods, shows an increasing growth.

[8] The essence of the Vickrey-tender, also referred to as second-price sealed-bid auction, is that each bidder submits a sealed bid; the bidder submitting the lowest bid wins the tender but receives the price equal to the second-lowest bid. The price floor, namely the setting of a minimum price for purchase below which the bid is rejected, results in the appearance of counter-selection, and thus quality reduction. Apart from a very few exceptions (works of art), even in the case of experience goods, certain quality parameters can be pre-set and subsequently checked, but these are not included in the model.

[9] Gál, 2004. page 14

[10] Its exact title: Decree No. 50,000/1934 K.M. of the Hungarian Royal Minister of Commerce and the Hungarian Royal Minister of Interior on public supply and Hungarian procurement obligations.

[11] See e.g. the procurement rules of the European Union where directives were available by objects (good, service, construction project) and by subjects of procurement up until the recent past (in 2004 the Council and the Parliament adopted a directive summarising all objects of procurement, whereas the rules on public utilities will continue to be provided for in separate directives even in the future).

[12] "First, the bid of the contracting tenderer, established in Hungary, shall be considered, who seems the most suitable for fulfilling the public supply in the desired quality and according to the interests of the service by using Hungarian products and local Hungarian labourers, and whose price offer is realistic and relatively the lowest, and thus most favourable.
...practically the lowest price is the realistic price which is established in such a way that the contracting tenderer pays his taxes and fulfils his social commitments, and wants to meet his obligations using good-quality materials and by properly providing for his employees, and to act loyally, i.e. without expecting overcharges and additional works, and such price is the most favourable for any public body that in the long run maintains its institutions from public funds (or in fact, mainly from taxes paid by contracting tenderers). Only thus can a public body expect that public considerations that are to be represented by it ex officio will, in all respects, be implemented. Consequently, under the correct interpretation of public interest, realism is a concept equal to inexpensiveness. Only hard and short-sighted fiscal approach may seek numerical inexpensiveness." (Kőházi, 1941, pp 143, 146)

[13] It did not apply to major central government procurements and to procurements of corporate enterprises, since in this particular area purchases were made upon decisions of the minister and the Council of Ministers.

[14] Gál, 2004, page 24

[15] Act I of 1994 on establishing an association between the Republic of Hungary and the Communities and its Member States in Brussels, on the promulgation of the Europe Agreement signed on 16 December, 1991.

[16] One of the favourite examples in public procurement training courses is why no tender is announced by the Prime Minister's Office for the protection of the Prime Minister's residence although the threshold for the purchase of services is exceeded. Do we want that the call for tenders and the accompanying documents (layout drawing, etc.) be freely available to any organisation?

[17] This subchapter has been prepared on the basis of Bozzai, 2004.

[18] In our paper the Treaty of Rome, the EEC Treaty and the Treaty establishing the European Economic Community are used as synonyms.

[19] These considerations appear as priority objectives in the internal law of the Member States.

[20] Jeney, 2000, page 588

[21] Palánkai, 2004, page 119

[22] See (Gordos, 2004, page 158). The question is whether the price decrease took place under stabile market prices in relation to purchases, or only the prices already decreasing on the market appeared in government purchases.

[23] EU thresholds (net values):
purchase of goods.: EUR 137 000 (HUF 34 422 973 forint)
ordering services: EUR 211 000 (HUF 53 016 404)
ordering construction services: EUR 5 278 000 (HUF 1 326 163 800).

[24] Based on Berényi (2003)

[25] The similar results of an EU-survey are described in the article of Báger and Kovács (2006).

[26] A good example for describing the suspicion in a polite, albeit definite and legally indisputable manner is the article published in the daily paper 'Népszabadság' on 26 August 2006 about the odd extra costs of motorway constructions..

[27] HVG (political and economic weekly), Vol. 2005/44

[28] "Many tenders reveal gross negligence which opens up the doors to corruption." HVG, Vol. 2005/44.

[29] http://www.napi.hu/default.asp?cCenter=article.asp&nID=262587

[30] About Transparency International and the method of calculating the corruption index see http://www.transparency.org/policy_research/surveys_indices/cpi

[31] Dezsériné, 2003

[32] The Lobbying Act was adopted by Parliament in 2006.

[33] Lecture by Árpád Kovács at the conference of the Public Procurement Council, http://www.promoexh.hu/kozbeszkonf/kovacs.htm, downloaded on 11 October 2006.

[34] See also Laffont's analysis: the "corruption yield curve" of political decision-makers always plays a part in the change in the level of corruption, and this curve often shows an increasing yield (Laffont, 2000, page 70). It is therefore questionable whether the intensity of market competition or this yield curve demonstrates a faster advance in the given case.

[35] Parliamentary Journal, 1990-2002. Database containing the full text of the minutes of plenary sessions, Arcanum Database , 2002

[36] Information on the situation of public procurements in 2005 and on certain components of the amendment of Act CXXIX of 2003 on public procurements.

[37] This data does evidently not contain public procurements awarded to foreign-owned but Hungarian resident economic organisations.

[38] Derogation from the rules is only allowed in the cases and to the extent, which derogation and extent are explicitely allowed by the Act on Public Procurement.

[39] The expansion of the negotiated prodecure points to this direction in the amendment to the PP Act made as of January 2006. A negotiated procedure initiated by the publication of an announcement can be employed if the object of the purchase is of the nature which makes the unambigous establishment of the consideration impossible. Negotiations can be conducted concerning goods listed and purchased in the commodity exchange, and if the goods are purchased under exceptionally favourable conditions, through administration of liquidation, final settlement or judicial enforcement or in the framework of other similar procedures.

[40] Let us take a semi-fictitious example: a ministry intends to order expert reports from economic analyst firms. The candidates are required to submit a certificate in proof of their due payment of taxes towards any government agencies listed in a long schedule. These include, for example, the environmental agency which is totally irrelevant in the given sub-market. A candidate may be excluded who submits a competitive bid from all aspects, but fails to attach this single certificate, for instance, due to insufficient time. The discrimination between candidates may be in that where the principal orders some candidates to submit the missing document, while it does not order others, and he has the right to both solutions (more precisely, it is not checked whether he acts at his discretion in respect of this small detail).

[41] Although the simple procedure was not abolished in the amendment of January 2006, but its rules were

simplified. Both the personal and objective scopes of this type of procedure have been narrowed. Thus, exemption is given from conducting the procedure to organisations that are forced to apply public procurement for the purchase of services and goods only on account if a subsidy or support granted. Even central budgetary institution are now exempt from the obligation of puchasing the services listed under Schedule No. 4 in a public procurement procedure and the same applies to public service contracts relating to central budgetary institutions fulfilling their principal duties in the creation of literary works (technical or scientific), or for consulting or interpretation services (professional, scientific) works below the value limit of HUF 25 million. Purchases conducted through an auction also fall under the exemptions, moreover, in the case public contracts with a value below 50 per cent of the national threshold it is not obligatory to send a repeated call for bids to the minimum three tenderers requested even if two or maybe one of them submitted a bid. In addition, references of the provisions applicable in the conduct of the simple procedure were also clarified by the legislator, which makes the practical application of this type of procedure unambiguous and easier.

42 On 15 January 2006 university researchers and researchers of the Academy filed a petition to the President of the Public Procurement Coucil. They pointed out in the petition that the status of several thousand researchers could be improved if the obligation to combine all purchases aimed at research and development financed through tendering, i.e. the obligation of combined calculation in respect of small-value purchases was abolished. Although the university can opt to calculate small items combined with other purchases, economic leaders often combine all items for fear of the public procurement penalty. The signers of the petition believe that in the majority of cases the acquisition of the items may not only be more expensive in this way, but their purchase takes much more time. This procedure, in their view, hinders Hungarian research and development which receives insufficient support anyway. On February 9 2006, the Public Procurement Counncil rejected the request (in addition to 377 signers with PhD, to 126 with CSc and to 158 with DSc degrees, 9 signers are corresponding members of the Hungarian Academy of Sciences (MTI) and 15 are ordinary members of MTI., 15 are directors of institutions, 59 are heads of department, 88 university professors are among the signers of the petition.)

43 Submission in copy format and re-regulation of the submission of missing documents are designed to reduce the costs of the procedure. As a general rule, simple copies of certificates must also be accepted, moreover, attachment of a certified copy may only be prescribed in the national and/or Community system. Another promotion to the public procurement participation of small-sized enterprises is the new regulation according to which the tenderer may comply with the eligibility criteria by relying on the resources of so-called "another organisation". This fact must be supported during the tender by a letter of commitment, and even the organisations thus involved are not subject to disqualification. This latter rule, however, is not popular with contracting entities, because it further broadens the range of subcontractors, already hard to have a grip on, and this may be also detrimental to the quality of performance.

44 According to one of the motions for amendment to the Public Procurement Act, the contracting tenderer should effect payment to his subcontractors within eight days from settlement of contracting tenderer's invoices. If the subcontractor has engaged another subcontractor, then the costs of such subcontractor shall be paid again within eight days. If payment is not received within the time limits, then the sub-contractor and his sub-contractors may post an immediate collection order against the contracting tenderer.

45 Annual Report of the Public Procurement Council for the year 2004, page 10

46 Ibid

47 There will be a significant increase in the management service fee payable in legal remedy proceedings from 15 January 2006, but not necessarily along the above outlined ideas. The fee of public procurement proceedings conducted within the Community-level system rose to HUF 900 000, while it remained unchanged for national and simple proceedings. The increased fee does not apply to the case when legal remedy is applied against the tender announcement which has given rise to the procedure.

48 On the other hand, the legislative authorisation incorporated into the latest amendment of the PP Act for correcting the deficiencies of the procedure offers a good solution. It was maybe forced out by the common practice that the tender announcer may correct the infringement committed in the procedure subsequently, within its own competence. This can be done by the tender announcer by modifying the result on one occasion until the contract conclusion in the event it notices that its procedure

has been unlawful, but remediable by correction. This provision saves both the Arbitration Board and the parties (the interested party and the party recognising and admitting the infringement) from unnecessary procedures.

49 The appearance of the dynamic purchase system is a significant novelty in the Hungarian legal regulation (from 1 January 2007). It is a fully electronic process during which tenderers who have entered the system can make a preliminary bid electronically. Following the publication of simplified announcements, contracting entities must send an invitation to tender to these tenderers with a view to the final tender. The future operation of the system is, to a large extent, dependent on the details of the Decree setting out detailed regulations.

50 Although it was raised as well as incorporated in draft laws on several occasions, the mandatory nature of the control of tender announcements is yet to be abolished. Several arguments are heard for and against the usefulness of this legal institution – so far the former is gaining the upper hand.

51 The opportunities for shortening the deadlines for tender are now added to the potential electronic procedural components (electronic publication of tender announcements, electronic availability of documents).

52 The Hungarian Post published an invitation to tender for the system long before passing the resolution. Why was it so certain that it would get the right or why did Oracle win in spite of offering a ready-made package for the price of HUF 2.5 billion, while Microsoft would have created a customised system for HUF 1.6 billion? These vague elements of the procedure are yet to be appropriately clarified.

53 An example from the operation of another sub-system: a Spanish voluntary fireman set a forest on fire because his wages was proportionate to his participation in fire incidents. It is impossible to close all loopholes in the regulation of large systems. Vas Népe, 12 August 2006

54 This is demonstrated by the fact that the Commission published a handbook in 2004 titled Buying green! Although it only contains recommendations, it is nevertheless indicative of the Commission's commitment.

55 Environmentally responsible public procurement (ERPP)

56 The most important of these conditions are: energy-efficiency, raw material efficiency, the use of raw materials with the environmentally lowest impact, environmental disposal of the product at the end of its life-cycle (demolition, re-cycling in the greatest possible degree).

57 Several eco-labels are is use in Hungary, tied to the manufacturer or to the bio-certification institute, the most well-known of the latter being the Bio Culture Association. Hungarian manufacturers may use the EU's own eco-label, the EU-flower, naturally only for products complying with strict conditions. We have not come across with such a product yet.

58 The Green Point Office of the Ministry for Environment and Water could name only one single product it uses which reflects environmental awareness, i.e. re-cycled envelopes. There seemed to be no "green commitment" regarding any other product.

59 The Commission's handbook titled Buying Green! provides several practical examples from local government as well as from central levels on how to achieve strong environmental impact in a simple way, and it recommends further guidelines.

Literature

Act CXXIX of 2003 on Public Procurements (in unified structure including the amendments made since that time)

Report of the Public Procurement Council for the year 2004, http://www.kozbeszerzes.hu/index.php?akt_menu=149 (downloaded on 22 March 2006)

Bágер, G. – Kovács, Á. (2006): Possibilities for the Control at Audit Office in the Fight Against Corruption, Lecture, *Budapest, www.asz.gov.hu*

Berényi, L. (2003): The Question of Corruption in Public Procurements, Corruption in Hungary III, *Transparency International Hungarian Chapter, Budapest*

Bozzai, E. (2004): Public Procurement in the European Union, European working papers about EU accession, *Centre for Government and Strategic Analysis of the Prime Minister's Office, Budapest*

Carayannis, E. G. – Popescu, D. (2005): Profiling

a methodology for economic growth and convergence: learning from the EU e-procurement experience for central and eastern European countries, *Technovation 25, Elsevier, pp 1–14, www.sciencedirect.com*

CELENTANI, M. – GANUZA, J. J. (2002): Corruption and Competition in Procurement, *European Economic Review 46, pp 1273–1303*

DESSEWFFY, A. (2000): Connections of Public Procurement and Corruption, Corruption Hungary I, *Transparency International Hungarian Chapter, Budapest, pp 71–84*

DEZSÉRINÉ DR. MAJOR, M. (2003): Nature of Corruption in Public Procurement in Hungary, *Budapest http://www.fme.hu/index_hu.html*

EL-AGRAA, A. M. et al (1994): The Economics of the European Community, *Harvester Wheatsheaf, Hemel Hempstead*

ESŐ, P. (1997): Auction and Competition in Public Procurement, *Quarterly Journal of Eeconomics Vol. XLIV, July-August, pp 597–611*

GÁL, A. L. (2004): Public Procurement, EU-Membership, *Challenges in Hungary, Prime Minister's Office, Budapest*

GORDOS, Á. (2004): The Hungarian Yo-yo in Europe, *Savaria University Press, Szombathely*

Guidelines, Procurement under IBRD Loans and IDA Credits, *The International Bank for Reconstruction and Development, Washington, 2004 http://siteresources.worldbank.org/INTPROCUREMENT/Resources/Procurement, May 2004.pdf*

JENEY, P. (2000): Public Procurement Policy. Tamás Kende -Tamás Szűcs (ed.): Policies of the European Union, *Osiris Publishing House, Budapest*

KAHN, A. E. (1988): The Economics of Regulation, Principles and Institutions I–II, *The MIT Press, Cambridge, Massachusets, London, England*

Corruption in Hungary III., *Transparency International Hungarian Chapter, Budapest, 2003*

KOVÁCS, Á.: lecture held on 18-19 February 2002 on Public Procurements at the conference organised by the Council, *http://www.promoexh.hu/kozbeszkonf/kovacs.htm*

KŐHÁZI, E. DR. (1941): Public Supply Code, *Budapest*

LAFFONT, J. J. (2000): Incentives and Political Economy, *Clarendon Lectures in Economics, Oxford University Press*

LAFFONT, J. J. – TIROLE, J. (1993): A Theory of Incentives in Procurement and Regulation, *The MIT Press, Cambridge, Massachusetts, London, England*

LI, L. – GEISER, K. (2005): Environmentally responsible public procurement (ERPP) and its implications for integrated product policy (IPP), *Journal of Cleaner Production 17., p 705–715 www.sciencedirect.com)*

MCDONALD, F. – DEARDEN, S. (1999): European Economic Integration, *Addison Wesley Longman Limited*

NÁDOR, SZ. (2005): Public Procurement Regulation and Practice in the European Union, *Dissertation, BDF (Berzsenyi Dániel College), Szombathely*

Parliamentary Journal, 1990–2002. Full-text database of the minutes of plenary sessions, *Arcanum Database, 2002*

PALÁNKAI, T. (2004): Economics of the European Union, *Aula, Budapest*

RÓMAI, R. (2006): Motorway Constructions which Goobles up Huge Sums. Or: Why and to what extent are Hungarian motorways more expensive than justified? *Népszabadság Weekend supplement, 26 August 2006, pp 2–3*

Report about public procurements in 2005 and about certain components of the amendment to Act CXXIX of 2003, *Public Procurement Council, Budapest, 2006, www.kozbeszerzes.hu, downloaded: 10 March 2006*

TÁTRAI, T. (2005): Public Procurement as a Specific Purchase Activity and Its Development Potentials in Hungary, *Draft doctoral dissertation, Budapest*

TÓTH, P. (2003): Corruption as an Adaptive Strategy, Corruption in Hungary II, *Transparency International Hungarian Chapter, Budapest*

TÖRÖK, Á. (1996): Operation of the Market and Industry Protection, *Janus Pannonius Egyetemi Kiadó (University Press), Pécs*

"Accidentally, you happened to exclude the winner", Interview by Lőke, A. (2005) with György Várday, *HVG, Vol. 44*

VISCUSI, W. K. – HARRINGTON, J. E. JR. – VERNON, J. M. (2005): Economics of Regulation and Antitrust, *The MIT Press, Cambridge, Massachusetts – London, England*

World Bank (2001): Electronic Government Procurement, *Draft World Bank discussion paper*

Buying green! (2004) A handbook on environmental public procurement, *Commission of the European Communities, Brussels*