PART I

The essentials of framework agreements

Basic definitions, main economic forces and international experience

CHAPTER 1

Introduction

Public procurement policy is commonly grounded in terms of promoting best value for money and avoiding corruption, waste and abuse.[1] Well-documented experience of failures in this regard, the enormous economic power of public procurement and the expansion of world trade and efforts to liberalise it have led to the development of formal rules governing public procurement at both the international and national levels.[2] Many of those rules, in addition to requiring that procurement officials follow open tendering (considered to be the most effective way of securing best value for the government), stipulate 'honesty and integrity in source selection, and equality of opportunity for would-be contractors',[3] together with requirements for internal controls, such as documenting decisions and formal approval processes.

[1] Preamble to the UNCITRAL Model Law (UNCITRAL Model Law on Public Procurement (2011)), *Official Records of the General Assembly, Sixty-sixth Session, Supplement No. 17* (UN document A/66/17). The text of the Model Law is available at www.uncitral.org/uncitral/uncitral_texts/procurement_infrastructure.html. Hereafter, Model Law. See, also, Steven L. Schooner, Daniel I. Gordon and Jessica L. Clark, 'Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations', GWU Law School Public Law Research Paper 1133234 (2008), available at http://ssrn.com/abstract=1133234, p. 32.

[2] United Nations Convention against Corruption, UN General Assembly (hereafter, UNCAC), 31 October 2003, A/58/422, available at: www.refworld.org/docid/4374b9524.html, Article 9(1)(c); The World Trade Organisation Revised Agreement on Government Procurement available at www.wto.org/english/docs_e/legal_e/rev-gpr-94_01_e.htm. Hereafter, WTO GPA; Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC Text with EEA relevance, OJ L 94, 28 March 2014, pp. 65–242, available at http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32014L0024. Hereafter, the EU Directive; The UNCITRAL Model Law (UNCITRAL Model Law on Public Procurement (2011), *Official Records of the General Assembly, Sixty-sixth Session, Supplement No. 17* (UN document A/66/17). The text of the Model Law is available at www.uncitral.org/uncitral/uncitral_texts/procurement_infrastructure.html. Hereafter, the Model Law; Federal Acquisition Regulation (FAR), Code of Federal Regulations (CFR) Title 48. FAR 2005-83/07-02-2015, available at www.acquisition.gov/?q=browsefar.

[3] Joshua I. Schwartz, 'Katrina's Lessons for Ongoing US Procurement Reform Efforts', *Public Procurement Law Review*, 6 (2006): 362–373.

The introduction and growing use of framework agreements in many systems have coincided with three main policy developments in public procurement, which we present in broadly chronological order. The first is a growing focus on anti-corruption, reflected in the agreement of the United Nations Convention against Corruption, the relative speed at which it was ratified and came into force and in implementation activities;[4] the second is a near-universal attempt to reduce the cost of public procurement in national systems, given the impetus by what is generally referred to as the worldwide financial crisis starting in 2008;[5] and the third is the growing emphasis on 'sustainable procurement', which can include policies to support environmental, social and economic objectives in public procurement. Most public procurement systems seek to address all three policy areas – which can be expressed as objectives or constraints, depending on the reader's point of view – and, as has long been noted, they are not always mutually compatible.[6] Balancing the competing considerations – often described in terms of discretion versus efficiency – has been the focus of policy debate in public procurement for decades.

Framework agreements involve a two-stage procurement procedure to secure the supply of a good or service in the future, used primarily where the procuring entity does not know the exact quantities, nature or timing of its requirements over a given period. The first stage leads to the identification of one or more suppliers on the basis of a tender or similar offer and conclusion of a framework agreement (in essence, a master contract) for the future supply. At the second stage, when the need arises for the subject matter of the framework agreement, the procuring entity places an order or enters into a contract (in the European Union (EU), generally referred to as a 'call-off') for its need with the supplier or suppliers that have entered into the master or framework agreement.

Thus, the main potential benefit of framework agreements is that they can reduce transaction costs and time by aggregating purchases, so that some procedural steps, such as advertising and assessing qualifications or

[4] UNCAC, supra, note 2. For the Status of UNCAC, see www.unodc.org/unodc/en/treaties/CAC/signatories.html; for activities of the Conference of States Parties, see www.unodc.org/unodc/en/treaties/CAC/CAC-COSP.html.

[5] Providing a broader context: as procurement is 'politically less sensitive' than other government expenditure, it is a target for cost-controlling policies for governments – G. L. Albano and M. Sparro, 'Flexible Strategies for Centralized Public Procurement', *Review of Economics and Institutions*, 1, No. 2 (2010); retrieved from www.rei.unipg.it/rei/article/view/17, at p. 2.

[6] Joshua I. Schwartz, 'Regulation and Deregulation in Public Procurement Law Reform in the United States', in G. Piga and K. V. Thai (eds.), *Advancing Public Procurement: Practices, Innovation and Knowledge-Sharing* (Boca Raton, FL: PrAcademic Press, 2007), pp. 177–201.

tenders, are conducted once for the group of purchases, rather than individually for each purchase. The procedural costs concerned are aggregated over a series of purchases, and the time to issue purchase orders is generally far shorter than in traditional open and competitive procedures. Framework agreements and the procedures to conclude them are therefore primarily designed to improve procedural efficiency in public procurement,[7] resulting from, at least in part, a perception that anti-corruption measures had led to an overly complex, inefficient procurement process.[8] In addition, framework agreements are considered to have the potential to 'increase dramatically the freedom [given to] public officials to use their judgment in the procurement process' to enhance value-for-money outcomes, as the then head of the United States (US) Office of Federal Procurement Policy urged the procurement community to adopt back in 1990.[9]

From this perspective, framework agreements are particularly suitable for repeat purchases of relatively standard goods or services (office and simple information and communication technology [ICT] supplies, and simple services such as maintenance contracts), in which the procedural costs could also become disproportionate to the value of the procurement if conducted on a one-off basis. The savings of time mean, too, that framework agreements can be of assistance in circumstances that would otherwise justify less open and competitive procedures – such as emergencies and other urgent situations – where framework agreements have been concluded in advance. The aggregation of the purchases, so they are not undertaken through less open and competitive procedures, also offers potentially better outcomes in those procurements themselves. It is often assumed that framework agreements are used only for simple, standardised purchases but, as we shall see, the technique is of potentially much wider beneficial application.

Nonetheless, framework agreements are not always appropriate. Procedurally efficient procurement does not guarantee overall value for money. The second stage is considered to be more at risk from this perspective, as it may involve the use of considerable discretion and is not always fully transparent and competitive,[10] which may result in higher

[7] 'Efficiency' in this context refers to the administrative costs of engaging in a particular procurement process, rather than in the economic sense of allocating resources in an optimal way.
[8] 'Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations', note 1, supra.
[9] S. Kelman, *Procurement and Public Management: The Fear of Discretion and the Quality of Government Performance* (Washington, DC: The AEI Press, 1990), p. 90.
[10] It has been observed that 'once a master agreement is in place, an order for goods or services can be issued against that agreement with far less notice and process, often with little risk of accountability'.

prices exceeding administrative savings. In addition, the procedure as a whole can limit rather than expand market access. These potential risks also increase with framework agreements of longer duration.

In aggregating procurement, framework agreements also involve some complex design issues, so a robust planning process is required. For example, different structures of framework agreement will reflect whether the need for what is to be procured is narrowly defined or stable, and/or whether the relevant markets are volatile. Related questions include whether the offer that will best meet the needs of the procuring entity can be determined only when needs arise or at the first stage, the extent to which there is homogeneity of demand, and the extent to which standardisation can be imposed or encouraged. Clearly these issues need to be addressed as part of the planning process, so the first stage is a relatively complex one. On the other hand, the second stage is intended to be procedurally swift and straightforward, without complex assessments.

Consequently, and for the same reasons noted for public procurement systems as a whole, a consensus is emerging on the need for effective rules on the operation of framework agreements and the procedures to conclude them. This consensus is reflected in a trend towards express regulation of the technique, as noted in a study conducted by the United Nations Commission on International Trade Law (UNCITRAL) in 2006,[11] a process that is continuing at the national level. Formal rules for the use of framework agreements will reflect a series of key decisions, including regulating whether or not to use a framework agreement, how to ensure effective design and use, and providing for monitoring and *ex-post* controls.

The importance of the above considerations also means that the appropriate level of flexibility in any particular system needs to reflect the capacity of its participants, and the system may need a dynamic approach, as experience in the use of framework agreements may indicate a change in parameters. The different considerations for the two stages of the

See Christopher R. Yukins, 'Are ID/IQs Inefficient? Sharing lessons with European Framework Contracting', *Public Contract Law Journal*, 37, No. 3 (2008): 546–568.

[11] 'Possible revisions to the UNCITRAL Model Law on Procurement of Goods, Construction and Services – the use of framework agreements in public procurement', UN documents A/CN.9/WG.I/WP.44 and A/CN.9/WG.I/WP.44/Add 1, available at www.uncitral.org/uncitral/en/commission/working_groups/1Procurement.html. UNCITRAL Working Papers are designated by 'A/CN.9/WG', to represent a Working Group document under a General Assembly mandate, and then have a consecutive number assigned to the specific document (e.g. UN document A/CN.9/WG.I/WP.44, note 13, supra). Reports of the Working Groups do not have the 'WG' designation, as they are reports to UNCITRAL in plenary session (known as the Commission sessions), and so are, for example, A/CN.9/752.

procedure involve a dual approach from the policy perspective, so that the second stage in particular is not overburdened by procedural rules, though sufficient safeguards to protect transparency and competition are necessary.

This book seeks to tackle all these issues, drawing together the economic considerations underlying effective use of framework agreements and how those considerations should be reflected in the policy choices and rules implementing them. We will analyse the business case for the use of framework agreements procedures, and outline the policy considerations that their use raises, and then consider how the policy choices made can be best reflected in the regulatory rules and other tools and documents that will govern the system concerned, in the context of the system as a whole and as applied to a particular procurement procedure. A natural focus where rules are concerned is to discourage inappropriate use or misuse through procedural safeguards, but we shall also provide examples from practice designed to illustrate how the tool can be harnessed to support overall policy objectives in public procurement and to introduce innovation both in procedures and in what the government purchases. The regulatory rules enabling the use of framework agreements procedures should reflect an appropriate level of flexibility in rules and guidance by reference to existing capacity and levels of governance, and allow for development as experience in the use of framework agreements is acquired. We will make some recommendations, too, on how these policy objectives can be reflected and expressed in legal rules, guidance and other tools, with a view to maximising comprehensibility for those users and the bidders they are seeking to attract.

Framework agreements can be concluded by a procuring entity for its own use, by a 'buying club' of procuring entities for their collective use (generally with a lead procuring entity as the main contractor) or by an agency established for the purpose of procurement of goods and services for procuring entities (a 'centralised purchasing agency'). We will conduct the main analysis by reference to a procuring entity setting up a framework agreement for its own use, and subsequently consider additional issues where more than one procuring entity or a centralised purchasing agency sets up a framework agreement for other public bodies to use.

We will address the key decisions required for introducing, designing and using framework agreements: the decision whether or not to use a framework agreement; the need for effective planning; deciding among key variables in form, structure and other elements; monitoring; and implementing remedies for breaches of procedures. Designing the system

for and setting up framework agreements, however, is only part of the question: data-gathering and empirical analysis of their operation in practice are crucial elements necessary to identify whether or not the potential benefits are materialising in practice.

Thus, we are addressing our thoughts to a wide audience, at the international as well as national level. We address both law and economics, with a view to ensuring that the use of framework agreements can be undertaken in as efficient and effective a manner as possible. In this regard, we ask how the legal rules on framework agreements and the procedures to procure using them can achieve the rather demanding objectives placed on the technique, and thus hope to provide comments of interest to those creating legal and regulatory frameworks. We also consider how the design and use of framework agreements in practice can contribute to (or compromise) the achievement of those objectives, and, in this regard, address our comments to public officials who are responsible for the organisation of public procurement, procurement officials and suppliers alike. This book is far from a comprehensive guidance to all legal issues arising, and still less an operational manual, though we identify the major issues concerned. We look at the individual framework agreement and the use of the technique for the aggregation of the needs of procuring entities through centralised purchasing.

The book is organised in three parts:

- Part I: *The essentials of framework agreements: Basic definitions, main economic forces and international experience*
- Part II: *Fostering competition and preventing collusion in framework agreements*
- Part III: *The design of framework agreements*

Part I introduces the reader to different families of framework agreements. While recognising that different approaches might be used to classify framework agreements, the book adopts a three-model approach: Model 1 comprises those arrangements whereby the master contract – that is, the framework agreement – contains all relevant clauses for awarding procurement contracts, and thus offers a straightforward purchase-order approach once the framework agreement is in place; Model 2 comprises those cases whereby the master contract is to some extent incomplete, hence a second round of competition is necessary for awarding procurement contracts. Moreover, both Models 1 and 2 are *closed* in that procurement contracts can be awarded only to those suppliers selected at the first stage of the process. Model 3, instead, is an *open* family of framework agreements,

whereby new firms can enter the system at any time so they can then compete for each procurement contract thereafter.

Although aiming principally at enhancing process efficiency and at a better exploitation of economies of scale, the *practice* of framework agreements has gradually showed that such purchasing arrangements can be used to better guarantee readiness and security of supply especially for crucial products (e.g. medicines) and in emergency circumstances. Different objectives generate quite diverse economic forces that need to be pondered and anticipated in order to reap framework agreements' potential benefits.

The precise nature of the contract between the public purchaser and the seller(s) to the government concerned will depend on many elements, among which one of the most important is the extent to which the purchaser's need is stable over time (and, where there are multiple purchasers grouped together, the extent to which their needs vary). To this factor must be added the degree of concentration of the supply market, the extent to which the master contract is complete or incomplete, the nature of the award criteria and the number of awardees with which the framework agreement is concluded. Part I will flesh out a methodological approach not only to assess the impact of each of the above factors on the desired outcome but also to evaluate how they may interact (and potentially interfere) with each other.

In the last two chapters of Part I we shall examine international practice on framework agreements. We shall consider how the development of regulation and practice of framework agreements procedures in various systems has evolved over time, and identify some areas of concern of regulation and practice. For example, some aspects might be contributing to or detracting from the achievement of the potential benefits of framework agreements, and others to how they avoid, or fail to avoid, some common pitfalls. Our presentation of this international experience cannot rely on much data and formal analysis, beyond limited aggregate information from certain centralised purchasing agencies. Nonetheless, we have identified consistent elements of practice that emerge from existing systems, some positive and some less so.

Part II will be entirely devoted to the issue of anticompetitive conduct on the part of suppliers in the operation of framework agreements. A feature of framework agreements is that the *closed* varieties in particular can limit the market to a limited number of suppliers and so create a temporary shelter from competition from outside the framework agreement. This quasi-oligopolistic situation may facilitate collusion at either

stage of the procedure, but the major concern arises at the second stage of some types of framework agreement (multi-supplier, Model 2 variants in particular). Some advances in the modern economic analysis of collusion are adapted in Part II of the book to highlight the extent to which different design solutions normally encountered in practice may raise the risk of collusion.

It is a widely held view that transparency of public procurement processes, while lowering the chances that an opaque relationship emerges between suppliers and procuring entities, may strengthen collusive agreements. The last chapter of Part II aims at opening up the black box of the 'transparency dilemma' by raising the following question: which pieces of information at what stages of the framework agreement procedure may have a pro-collusive impact on market conduct? While recognising that, in fact, cartels need very little information to implement collusive agreements, the analysis emphasises that procurement officials are in a position to withhold some pieces of information that are deemed to have an anti-competitive impact. Using discretion in this matter requires, needless to say, both a well-trained workforce and, perhaps more importantly, some explicit forms of cooperation between procurement organisations and antitrust authorities.

Part III of the book will lay down some 'nuts and bolts' for framework agreements design, both at the regulatory and operational levels. The main lesson coming from the earlier two parts of the book is that multiple layers of economic forces are at work in frameworks agreements, hence sound design requires: (i) a clear understanding of procuring entities' needs and of the main features of the relevant supply markets; (ii) a recognition that no 'free lunch' applies, either, in framework agreements markets, so that pursuing a specific objective may be feasible only to the extent that another goal is let go; (iii) the ability to assess, at least qualitatively, the magnitude of different economic forces that are likely to emerge from any feasible scenario; and (iv) a willingness to adopt a trial-and-error approach, which necessitates the recognition that there is no 'right' framework agreement solution. Avoiding over-ambition is vital, especially where framework agreements are used for ambitious projects of centralising public procurement, even in part.

Finally, we draw together the main conclusions that we have reached. Key among them is the need for a more coherent debate on economics in policymaking. We consider that economics and business practice should be the foundation of public procurement policy and how it feeds into the regulatory system, and – at the risk of proselytising – encourage all involved