

Overview of public procurement reform in Russia

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Abstract. Reforms in the sphere of public procurement has been conducted since 1990-s in Russia after long period of command economy. This article briefly examines significant steps in public procurement reforms, challenges in formation of the frame-work regulation and institutional environment of public procurement. The article reviews administrative and judicial practice against infringements in public procurement. One of the main question raised in the article is implementing effective remedies for contracting authorities and bidders. The article consists of several important court cases concerning recent problems in public procurement.

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Introduction

Public procurement has a decisive impact on economic and social development in Russia. According to the official statistics in 2011 the total volume of public (state and municipal) procurement in Russia was 8 310 billion rubles (~203 billion euro), which is about 14,9% of GDP in Russia. The volume of public procurement, advertised in the official website, is 4 182 billion rubles (~102 billion euro) or 7,5% GDP in Russia.

The development of public procurement in Russia began after long period of command economy where economic entities could have no initiative. After the collapse of the Soviet Union centralized distribution of material resources and mandatory state order were abolished [1].

First regulations in the area of public procurement, appeared in 1992 [2]-1995 [3], did not provide for any procurement procedures or state any obligations and liabilities. So it became fertile ground for corruption.

An important stage in the development of the public procurement legislation was Presidential Decree No. 305 [4]. It stipulated several procurement methods, set complaints procedures. Territorial units of Russian Federation had to bring regional legal acts into compliance with the decree. The Decree was partly replaced later by the Federal Law No. 97-FZ [5].

In summary, public procurement in Russia in the mid 2000s was characterized by the following factors:

- inconsistency between acts regulating public procurement;
- lack of unified regulation for procurement at the federal, regional and local levels;

- lack of sanctions for the violation;
- large quantity of restricted tendering.

As a result, there was a strong need for substantial reform of public procurement legal regulation.

The Federal Law No. 94-FZ [6] came into force 1 January 2006 and replaced the Presidential Decree No. 305 and the Federal Law No. 97-FZ. The law eliminated previous inconsistency in regulation of public procurement, set uniform rules for procurement at federal, regional and local levels. All regional acts regulating procurement were canceled after the law came into force.

The Federal Law No. 94-FZ was aimed at formation of the institutional environment of public procurement, including information infrastructure, authorized bodies, specialized organizations, agencies with controlling responsibilities.

The information infrastructure has been primarily supported by the official Internet site of the Russian Federation which has been the main source of information concerning public procurement at federal, regional and local levels. The order for publishing information has been strictly regulated. To publish information on the official website, contracting authorities have been obliged to use electronic digital signatures (equivalent to holographic signatures) [8]. More than two million contract notices were published on the official website in 2011.

The official website interacts with the five electronic trading platforms for holding electronic auctions. The electronic trading platforms ensure complete electronic document management. The electronic digital signature is used by contracting

authorities and economic operators, it is also used in the execution of contract.

Holding an electronic auction and participation in it are free of charge. The main income of the electronic trading platform is from placing funds formed by tender securities on the banks accounts. Experts estimate that the total volume of deposits is about 100 billion rubles (~2,5 billion euro).

The Federal Law No. 94-FZ provided strict rules concerning publication of the procurement information on the official website. The administrative penalties may be imposed for violation of procurement regulations and the court may be able to declare the contract ineffective. However, there are well known cases when contracting authorities or specialized organizations [6] used some tricks when publishing notices on the official website.

As a general rule, the official language for the information on the official website is Russian. The Russian alphabet is a form of Cyrillic script. However, some of the contracting authorities use Latin characters identical to Cyrillic characters in Russian words to make the search of the specific notice difficult. For example in the word "postavka" (English: supply) instead of using Cyrillic characters they switch the keyboard to English and type Latin characters "o", "a" in the notice. The other trick is to type all words in the title of notice together without space. There are different methods for search on the official web site but substitution of characters made search complicated.

There is established administrative and judicial practice concerning above mentioned infringements. Here is one of the cases. Specialized organization published the notice titled "Supply of computer peripheral equipment" on behalf of the contracting authority. The specialized organization substituted Cyrillic characters by Latin characters in the title of the notice. Based on the inspection results The Federal Antimonopoly Service found infringement of public procurement rules. The specialized organization filed a claim to the Commercial Court to attack the decision of FAS. However, the court in this case and in similar cases confirmed the position of FAS. The court held that substitution of characters does not allow contractors to search the information on the official website using Russian words because the title of the notice contained words composed of Russian and Latin characters, in consequence such conduct restricts participation and violates the rules stated in Federal Law No. 94-FZ [9].

The developer has improved search on the official site, so the mixture of Cyrillic and Latin characters does not affect the result. Nevertheless the

official site needs some improvements, for instance the development of data analysis system. At present day the official website lacks the function of presenting the results of search in statistics mode as it is possible on the Official Journal's public procurement website.

The Federal Law No. 94-FZ provided establishment of authorized bodies to exercise functions in public procurement at the federal, regional and local levels [6]. An example of an authorized body established at the regional level is The Competition Policy Department (Tender Committee) of Moscow [7].

This Department provides functions of public procurement in Moscow. A contracting entities in some cases are obliged to delegate functions to the Department (except transferring the right to enter into contract).

Public procurement is divided into two levels in Moscow. The procurement procedures are conducted by the Department at the first level and by contracting authorities at the second level. The first level contains contracts with estimated value over 50 million rubles (~1,2 million euro), secret contracts, contracts awarded through the procedures conducted jointly by several contracting authorities if the estimated value of contracts exceeds 3 million rubles (~75 000 euro). The second level contains all other contracts.

The total volume of public procurement in Moscow was 691 billion rubles (~17,3 billion euro) where 450 billion rubles (~11,3 billion euro) refers to the first level in 2012. The contracting authority may delegate some functions to the specialized organization to perform the following services: prepare tender documentation, publish notices and documentation on the official website. The other functions are performed by the contracting authority. Usually specialized organizations become involved in procurement conducted by contracting authorities placed significant number of orders.

The contracting authorities, the official website operator, the authorized bodies and specialized organizations are subject to the administrative control exercised on the federal level by the Federal Antimonopoly Service of Russia, on the regional and local levels - by authorities with controlling responsibilities.

Any supplier or contractor may apply to FAS or authorized control authorities for review of a decision or an action taken by the procuring entity, authorized body, or specialized organization in the procurement procedures.

FAS carried out 36 921 inspections and issued 14 253 infringement notices in 2011. FAS examined 26 263 complaints, the share of complaints

found reasonable was 42%. FAS commenced 17 626 administrative cases, most of them concerned infringements of rules for award procedures and publishing documentation which are inconsistent with the legal requirements.

There are statutory administrative penalties for the violations imposed on the officials of the contracting authorities. For instance, the following violations are subject to administrative penalties up to 30 000 rubles (~750 euro): infringements of rules concerning examination and evaluation of tenders, setting out criteria inconsistent with the Law, inclusion in one lot of goods, services and works which are technologically and functionally unrelated.

Federal Law No. 135-FZ "On protection of competition" [10] prohibits to include in one lot products unrelated to the products which are the subject-matter of the contract. The court has the power to declare a contract ineffective where award of the contract was in breach of this rule. However, the legislation does not define criteria for determining the functional and technological interrelation. The administrative and court practices are quite controversial.

FAS and the courts held that it is prohibited to include goods, works and services in one lot if:

- works (services) are subject to separate licensing;
- goods, works and services related to different groups and codes of the Classifier [11].

In this regard, the recent case concerning the above mentioned problem might be of interest. The case has reached The Supreme Commercial Court of the Russian Federation. Parties to the case were: Limited Liability Company "ElektroLab" (hereinafter - the Company, the plaintiff), The State Atomic Energy Corporation "Rosatom" (hereinafter - the Corporation, the co-defendant) and The Federal Antimonopoly Service of Russia (hereinafter - FAS, the co-defendant) [12].

The Company applied to FAS for review of unlawful actions taken by the Corporation. The Company pointed out that according to Part 3 of Article 17 of Federal Law No. 135-FZ it is unlawful to include in one lot technologically and functionally unrelated works, such as:

- design drafting;
- manufacture of equipment; and carriage of nuclear materials.

The applicant considered that the inclusion in one lot of the above works led to competition restrictions. However, FAS dismissed the applicant's complaint. FAS Russia ruled that:

- the subject of the contract is the single package of work;

- according to the documents of the Corporation there were at least fifteen companies licensed to carry out such works, and the applicant had not presented evidence that requirements of documentation limited the number of contractors.

The Company filed claims to the Moscow Commercial Court to attack the decision of FAS, to find such conduct of the Corporation wrongful, and to annul the contract award. The Moscow Commercial Court agreed with the Company's argument that the Corporation violated Federal Law No. 94-FZ, as well as Federal Law No. 135-FZ.

The absence of technological and functional interrelation between these works was supported by the reason that these works related to different codes of the Classifier, and also to the different chapters of the Civil Code, which regulate different types of contracts. The Moscow Commercial Court held that the conduct of the Corporation was illegal and declared the awarded contract ineffective. The court of appeals upheld the decision of the lower court. Finally the case reached the Supreme Commercial Court of the Russian Federation.

A panel of judges of the Supreme Commercial Court found that the case was subject to judicial review. It was pointed out in the court ruling concerning the transfer of the case to the Presidium of the Supreme Commercial Court of the Russian Federation that:

- the general principles of legal regulation in the area of nuclear energy ensure security and protection from radiation hazards;
- the courts had not taken into account that the purpose of the contract was the removal of spent nuclear fuel from the nuclear power plant, and it could be performed only by the package of works;
- courts findings that technological and functional interrelation depends on the same name, similarity and interchangeability with references to the Classifier and the Civil Code were incorrect;
- courts findings that there was no technological and functional interrelation between the above works were unlawful.

It is expected that the Supreme Commercial Court's decision may contain:

- the complex approach for determination of possibility to include technologically and functionally interrelated goods, works and services in a single lot; or
- the individual approach concerning that the possibility of including different types of goods, works and services in the single lot depends on particular situation.

However, the decision of the Supreme Commercial Court will have a positive impact on application public procurement rules.

The law provides for the Register of unfair suppliers. The Register contains information about the unfair supplier for two years. FAS enters the information in the Register in the following cases:

- the successful tenderer rejects to enter into contract;

- the supplier breaches the contract and the contract is rescinded by the court.

The Law does not provide other grounds, such as fraud and corruption, for entry into the Register.

The Federal Law No. 94-FZ set forth details of procurement procedures:

- open tendering;
- closed (selective) tendering;
- open electronic auction;
- closed (selective) auction;
- request for quotations;
- single source procurement.

Every procedure was properly detailed. The law clearly stated, in which cases the contracting authority may use a particular method of procurement.

In practice, the main procurement method in Russia has been an open electronic auction. According to the official statistics, open electronic auctions represented 40,1% of the total number of notices and 62,4% of the total value of contracts, advertised on the official website in 2011.

The open electronic auction is a separate kind of procurement procedure. It is not used as part of another procedures as it is stated in Article 54 (2) of the Public Sector Directive 2004/18 [13].

The open electronic auction is based solely on prices: the contract is awarded to the lowest price. The procedure of open electronic auction is anonymous. So the operator of the electronic trading platform keeps the names of the participants in secret till the end of the auction.

There are no rules concerning full initial evaluation of the tenders prior to proceeding open electronic auction. As a result, the area of public procurement is affected by the very low quality of competition. For instance, the percentage of unsuccessful open electronic auctions in 2011 was 50%.

According to the official statistics, the open tenders represented 5,1% of the total number of notices and 22,3% of the total value of contracts, advertised on the official website in 2011. The successful tender is the most advantageous tender ascertained on the basis of the criteria and procedures for evaluating tenders. There is an exhaustive list of criteria that may be used.

A request for quotations represented 52% of the total number of notices and 4,9% of the total

value of contracts, advertised on the official website in 2011. The successful quotation is the lowest-priced quotation. The suppliers criticized this method for the reason that, according to the rules provided by the Federal Law No. 94-FZ, quotations were presented without sealed envelopes.

The single source procurement represented 45,7% of the total value of contracts concluded in 2011. Article 55 of Federal Law No. 94-FZ stated grounds for entering into contract with a single supplier. This article has been amended several times since the law entered into force.

It should be mentioned that after Federal Law No. 94-FZ was implemented the number of closed (selective) tenders fell down dramatically. Thus, in the first year after the Law was enforced the number of close (selective) tenders decreased by 21%. The total value of all contracts awarded with close (selective) procedures was nearly 4,6% in 2011.

The close (selective) tenders or auctions are allowed only if:

- the tender documentation contains data constituting a state secret; or
- the subject-matter of the contract is insurance, transportation and security services of museums and archives valuables.

Public procurement in Russia is among the most corrupted areas. A number of scandals has occurred in recent years. A permanent negative reaction in society cause the purchases of premium cars and expensive furniture by contracting authorities. Amendments have been introduced to the State Duma concerning restrictions of purchasing cars the price of which is more than two million rubles (~ 50 000 euro). However, it has not been adopted yet.

There are famous cases of medical equipment procurement for contracting authorities (computed tomography scanners, ultrasound equipments and etc.). Fraudulent schemes are focused on the illegal increasing of the estimated value of public contracts for medical equipment supplies. In several regions the medical equipment has been purchased at prices much higher than manufacturer prices.

According to the Prosecutor General Office, of particular concern are misappropriation of budget funds, inappropriate and inefficient spending, collusion in public procurement and other forms of corrupt activities. Ministry of the Internal Affairs of the Russian Federation and the Investigative Committee of the Russian Federation are investigating several criminal cases in this area, some of them related to medical equipment procurement.

Nevertheless, the development of public procurement has been significantly improved since

1990-s. The legislation for public procurement has been adopted, the institutional elements have been formed. At the same time, the practice has revealed problems:

- strict control and simplification of procurement methods leads to reduction of qualification requirements;
- the procurement procedures are focused on the purchase products of mass consumption, the using of specified methods to procure high-technology goods is challenging;
- public procurement is affected by low quality of competition;
- the calculation of the estimated value of a public contract is not transparent, large number of cases when the value is overestimated.

The current state of public procurement in Russia can be characterized as transitional, so there is a great demand for further reform measures. The Ministry of Economic Development started a reform of the public procurement regulations. Two main elements of the reform are:

- enforcement of procurement regulations for state-owned corporations and companies, natural monopolies and utility companies;
- replacement Federal Law No. 94-FZ with the new federal law.

Federal Law No. 223-FZ [14] (the first element of the reform) came in to force 1 January 2012. This Federal law establishes general principles for the procurement of goods, works and services by state-owned corporations and companies, natural monopolies and other legal entities.

Federal Law No. 223-FZ declares that purchasing activity of contracting authority is regulated by legislation and by their own standards [14]. These standards should establish procurement methods, requirements for preparing and conducting procurement procedures, procedures regarding conclusion and performance of contracts, and other related procurement provisions. Information about procurement under the Federal Law No. 223-FZ is available on the official site.

Regulation for the procurement activities of certain legal entities plays a significant role for the Russian society. According to the Ministry of Economic Development, the total volume of procurement by the state-owned corporations and companies, natural monopolies, and utilities companies is estimated around 7 000 billion rubles (~175 billion euro).

The second element of the reform is the Federal Law No. 44-FZ [15] which came into force 1 January 2014. The law is focused on three interrelated stages: 1) forecasting and planning; 2) purchasing; 3) control and audit.

According to Federal Law No. 44-FZ, the key element of the contract system will be consolidated and integrated information environment. It is assumed, that system will be based on the existing official website www.zakupki.gov.ru.

Procurement plans of all levels (federal, regional, local) will be available to the public. Price monitoring and advertising the results of the contract will help to prevent situations similar to notorious medical equipment procurement.

The Federal Law No. 44-FZ incorporates procurement methods of Federal Law No. 94-FZ and add several more, including restricted tender, two-stage tender, request for proposals.

According to The Federal Law No. 44-FZ, there is additional reason to exclude the contractor from participation in a public contract - conviction of economic crimes.

The law provides for the contract audit. Contract audit is the process of verifying how effectively the contracting authority conducts its function in planning and procurement. Contract audit is conducted by the Accounts Chamber of the Russian Federation.

The law lists essential steps for improvement in the area of public procurement: forecasting and planning, personal responsibility for the result of the contract, additional procurement methods which give an opportunity to conduct purchasing more effectively.

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