THE RULES ON PUBLIC CONTRACTS IN ITALY AFTER THE CODE OF PUBLIC CONTRACTS*

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Abstract

The approval of the Code of Public Contracts, in implementation of the European Directives, has changed the traditional approach of the Italian legislator to the regulation of public contracts. However the public contracts sector is still unstable from a legislative perspective and the application of the rules is characterised by uncertainty and variations. All this has negative repercussions on the activities of the contracting authorities, the undertakings and, more generally, legal operators. The author calls for a legislative moratorium in order to stabilise and complete the regulatory framework.

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1. Introduction.

Under Italian law, the execution of a contract with the public administration is preceded by an administrative procedure in which the contractor is selected (the "tender process" or "*public tender process*"). Therefore, negotiations with private entities take place in accordance with public law in implementation of the relevant European directives.

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Thus, while the selection of contractors in agreements between private parties is left to the individual's transactional autonomy in accordance with the Italian Civil Code Italian law and is, therefore, tendentially free, the public administration is required to act through administrative measures and procedures in accordance with a series of principles of European origin (freedom of competition, equal treatment, non-discrimination, transparency, proportionality, advertising, etc.) which are intended to protect the public interest that it represents.

The current tender process rules on the selection of contractors are contained in the Code of Public Contracts, which was adopted by Legislative Decree no. 163 of 11 April 2006 and includes all the relevant provisions that were previously contained in separate laws[1]. The legislator has also implemented in the Code of Public Contracts the new European Directives 2004/18/EC, on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts in ordinary sectors, and 2004/17/EC which coordinates the procurement procedures of entities operating in the water, energy, transport and postal services sectors (so-called special sectors)[2].

The Code is a detailed, complex act (more than 250 articles) and is supplemented by the implementing Regulation, which is primarily dedicated to the execution of public works (more than 350 articles contained in Presidential Decree no. 207 of 10 October 2010).

From an institutional perspective, the Code of Public Contracts is of great significance as it brings together in a single

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[1] Legislative Decree no. 157 of 17 March 1995 was dedicated to public service contracts, Legislative Decree no. 358 of 24 July 1992, to public supply contacts and Law no. 109 of 11 February 1994, to works. The rules for the excluded sectors (now defined as "special sectors") were contained in Legislative Decree no. 158 of 17 March 1995.

[2] For a general framework about the discipline of European Directives no. 2004/18/EC and no. 2004/17/EC, see S. Arrowsmith, *The Law of Public and Utilities Procurement*, Sweet & Maxwell, 2005; C. Bovis, *Public Procurement in the European Union*, Palgrave MacMillan, 2005; J.M. Hebly (ed.), *European Public Procurement: History of the 'Classic' Directive 2004/18/EC*, Kluwer Law International, 2007; S.E. Hjelmborg and P.S. Jakobsen, *Public Procurement Law – the EU directive in public contracts*, Djøf, 2006; R. Nielsen and S. Treumer (eds), *The New EU Public Procurement Directives*, Djøf, 2005.

text the rules on works, services and supply contracts. Just the name "Code", which the Italian legislator has recently used in many sectors (environment, electronic communications, insurance, consumers, etc.) [3] ought to suggest a stabilisation of the rules after a series of legislative amendments that have not always been properly coordinated.

As for its general objectives, the Code's approach is to promote a greater opening to competition in the sector and it is permeated by principles of European origin which are intended to lend greater flexibility to the procedures.

This does not mean that the Code contains uniform rules that apply to all public contracts. In fact, the public works sector, in particular, is characterised by specific rules (such as, for example, those relating to the contractual relationship following the award procedure), which must be taken into account. Even contracts whose value is below the European threshold are subject to particular, simplified rules, although many aspects are regulated in the same way as contracts that exceed the threshold.

The first few years of the Code show that there is still uncertainty as to its application and the period of adjustment has been difficult. Indeed, three corrective legislative decrees have been issued since the Code came into force in 2006. These legislative decrees were envisaged by the original enabling law for the issue of the Code which, like many enabling laws, grants the Government a considerable amount of time in which to make the necessary amendments to the legislative decrees so as to take into account any difficulties that may have emerged during the initial phase of their implementation[4]. Moreover, the aforementioned implementing regulation of the Code was only adopted in 2010; it

[3] Article 1, Law no. 229 of 29 July 2003 envisages the Code as a general instrument for reorganising the laws in force, rather than a Consolidated Law, which is instead envisaged by article 8 Law no. 50 of 8 March 1999, which has now been repealed. In practice, there are no particular differences between the two instruments, except for their names.

[4] The corrective measures were introduced by Legislative Decree no. 6 of 26 January 2007, Legislative Decree no. 113 of 31 July 2007 and Legislative Decree no. 152 of 11 September 2008, which were necessary, *inter alia*, to address certain objections to the rules by the EU Commission. In particular, the Commission had objected to several provisions in the Code relating to project financing in a letter of formal notice, no. 2007/2309.

contains detailed rules on the individual procedures and its issue was the pre-requisite for the application of various provisions of the Code. Essentially, the entire codification process has taken more than four years.

Further amendments to the rules in the Code were introduced by Legislative Decree no. 53 of 28 March 2010 which implemented European Directive 2007/66/EC on review procedures, whose purpose was to speed up and improve the effectiveness of the remedies available to undertakings that take part in tender processes. These rules – which are now largely contained in the Code of Administrative Procedure, which was approved by Legislative Decree no. 104 of 2 July 2010 – introduce many innovations and, in particular, affect the procedural rules for judicial review and the powers of administrative courts.

Even more recently, the legislator has, as we shall see, intervened on several occasions with amendments to provisions in the Code, mainly with the aim of addressing the financial crisis and promoting economic development by acting on the public administration's demand for goods, services and works, which mobilises huge resources[5]. In reality, the recent measures introduced by Parliament (e.g. speeding up and streamlining the procedures for large-scale works and the involvement of private resources in the execution of public works) are not entirely new. In fact, they have been attempted several times in the past, for example with the so-called *Obiettivo* Law (Legislative Decree no. 190 of 2002), with a view to speeding up the procedures relating to

[5] Starting from *Decreto Legge* no. 70 of 13 May 2011, which was converted with amendments by Law no. 106 of 12 July 2011, there has been a series of legislative intervention: *Decreto Legge* no. 6 December 2011, no. 201 which was converted with amendments by Law no. 214 of 22 December 2011; *Decreto Legge* no. 1 of 24 January 2012, which was converted with amendments by Law no. 27 of 24 March 2012; Law no. 3 of 27 January 2012; *Decreto Legge* no. 5 of 9 February 2012, which was converted with amendments by Law no. 35 of 4 April 2012; *Decreto Legge* no. 16 of 2 March 2012, which was converted with amendments by Law no. 44 of 26 April 2012; *Decreto Legge* no. 83 of 22 June 2012, which was converted with amendments by Law no. 134 of 7 August 2012; *Decreto Legge* no. 52 of 7 May 2012, which was converted with amendments by Law no. 94 of 6 July 2012; *Decreto Legge* no. 95 of 6 July 2012, which was converted with amendments by Law no. 135 of 7 August 2012; Legislative Decree no. 169 of 19 September 2012; *Decreto Legge* no. 179 of 18 October 2012; Law no. 190 of 6 November 2012.

the major infrastructure projects and are now contained in the Code.

2. The traditional approach to regulating public contracts and the new European perspective.

In order to understand fully the new approach of the Code of Public Contracts, a brief mention of the traditional approach to the rules is required.

The idea of promoting competition between economic operators has always, at least since the start of the last century, been a feature of the rules on the award of public contracts.

However, the rules, above all, originally served the financial interest of the Administration, in that the tender process was seen as the most effective way of preventing the waste of public money. It is not a coincidence that the relevant provisions were contained in laws that regulated public accounts and, in particular, spending procedures[6]. In other words, public contracts were mainly considered with a view to properly regulating income (revenue-producing contracts, such as the sale of public property) and expenditure (purchases by ministries and other public administrations)

From the legislator's standpoint, the rules on contracts were also required to prevent corruption, which was particularly widespread in the sector. Indeed, the Italian Criminal Code has always envisaged crimes, such as bid rigging (*turbativa d'asta*), which are specifically intended to protect the freedom of action imposed on, or agreed to by, parties participating in tender processes (*libertà degli incanti*). Since corruption continues to be a major problem, the Italian legislator has recently extended the range of crimes still further, for example by punishing undertakings that attempt to condition the contents of a tender notice in their favour.

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[6] Initially, before European integration, the legislation on public tender processes was distributed among several acts of primary or secondary legislation. In general, the main acts were the Law on Public Accounts, Royal Decree no. 2440 of 18 November 1923, and its implementing regulation, Royal Decree no. 827 of 23 May 1924.

Over the last twenty years, the system defined by the provisions of public accounts legislation has been flanked and gradually superseded by the different approach of the superseding European law. In fact, in the 1980s and 1990s, European law started to take into account the impact on competition that public authorities have when they act as purchasers or grantors by introducing rules to prevent market distortion[7]. Indeed, it is not only in the interests of the contracting authority, but also in the interests of undertakings to be able to participate in the public contract market on an equal footing.

In the European authorities' view, competition serves two purposes. On the one hand, it promotes the free circulation of goods and services, including those required by the public sector, within the community, with the consequent positive effects on demand in terms of greater quality and value of the awards. On the other hand, it helps undertakings that are European in scope to develop in such a way as to allow them to compete with non-EU undertakings at a worldwide level. The creation of "European champions" was one main argument, in support of a single public contract market.

Alongside the contracting authority's interests, the position of the individual would-be contractor is also of supreme importance, i.e. the protection of its interest in not being discriminated against and being able to take part in a competitive process. In practice, Italian law has had to adjust to the new meaning of the principle of competition by providing for more guarantees of transparency and advertising, more opportunities to take part in tender processes and by neutralising any discrimination arising from the demand for exclusionary technical services.

Thus, for example, as a result *inter alia* of judicial rulings inspired by the new principles of European origin in the 1980s, special rules (which were often contained in regional laws) that only allowed undertakings registered in the relevant territory to take part in tender processes were repealed as they not only

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[7] An analysis about the effects of public award on competition is made by Office of Fair Trading, *Assessing the Impact of Public Sector Procurement on Competition*, vol. I, London 2004.

discriminated between Italian and European undertakings, but also between undertakings operating in different parts of Italy.

Another indicator of the different foundation upon which the European law on public contracts is built is the broad scope of application of the provisions that regulate tender processes. Unlike the laws on public accounts, the Code also applies to bodies governed by public law entities and, in the special sectors, to public enterprises and to private operators with special or exclusive rights, which are not public administrations in the traditional meaning of the term and not necessarily even public economic entities.

In particular, while the pro-competitive objective in the ordinary sectors goes hand in hand with the traditional objectives of the procedural rules (selection of the most efficient operator to which to assign public resources and the fight against corruption), in the special sectors identified by European law (gas, electricity, post, ports, etc.) such objective emerges even more clearly.

Indeed, operators engaged in the special sectors may be purely entrepreneurs and, therefore, the issue of the efficient assignment of public resources does not arise. Nor is there an issue with corruption, since these operators do not exercise a public function and do not manage public services. The issue of prevention and repression of corruption in relationships between private parties has long been ignored by the Italian legislator and only recently has Parliament addressed the problem (Law no. 190 of 6 November 2012).

Moreover, as in practice the special sectors gradually become more open to competition, there is less need to apply the rules on tender processes. In fact, the special sectors have been traditionally run as monopolies by the winning entities, which, without the mechanism of the public tender process, could distort competition. Therefore, in the event that these sectors are liberalised and are no longer run as monopolies, the role of the tender process in promoting competition is superfluous as the market dynamics themselves will neutralise the winning bidder's potential power to distort the market.

The protection of competition as the most important fundamental principle of the rules on public contracts, which has also been reiterated on several occasions by the European Court of Justice, has emerged as a primary public interest which is

expressed by numerous provisions in the Code. Indeed, the Italian Constitutional Court emphasised the pro-competitive approach of the Code when it rejected a series of petitions submitted by the Regions which claimed that the Code was detrimental to their legislative competence (judgement no. 401/2007). The *Consiglio di Stato* was even more peremptory, when it stated that the pro-competitive approach has "*resulted in the end of the conception that the procedure for the selection of contractors should be exclusively dictated by the administration's interests* " (see Cons. St. Plenary Session, judgement no. 1 of 3 March 2008).

3. The impact of European Law.

At a national level, this change of perspective has also had an impact on the methodological approach to the regulation of public contracts in the Code.

On the one hand, the traditional conception of the rules on public contracts relied on a complex system of strict rules that ruled out any discretion (for example, in the identification of anomalous bids). Instead, the pro-competitive vision of European law grants the contracting authorities more flexibility by introducing opportunities for cooperation, i.e. interaction with the private entities with the aim of rectifying the one-sidedness of the information available. In fact, the administration is often not in the best position to know in advance the actual conformation of the goods or the services that it wishes to procure. This occurs when such goods or services are complex and the administration is not able to assess all the features. The most obvious case is that of the "competitive dialogue"[8], which is permitted under European law, but is disliked by the Italian legislator and the courts as it is deemed to be too flexible and to jeopardise the principle of equal treatment of the undertakings.

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[8] Competitive dialogue is an important new kind of procedure characterized by a flexible structure. About competitive dialogue see C. Kennedy-Loest, *What Can be Done at the Preferred Bidder stage in Competitive Dialogue?*, in Public Procurement Law Review, 15, 317, 2006; A. Rubach-Larsen, *Competitive Dialogue*, in R. Nielsen and S. Treumer (eds), *The New EU Public Procurement Directives*, Djøf, 2005; S. Treumer, *The Field of Application of Competitive Dialogue*, in *Public Procurement Law Review*, 15, 307, 2006.

Moreover, according to the traditional approach, which is based on strict rules and inspired *inter alia* by a lack of confidence in the moral integrity of the contracting authorities and the undertakings, formal compliance with the *lex specialis*, which comprises detailed rules that guarantee the *par condicio,* was more important than the need to allow the administration to assess the best-value choice on the basis of more substantive criteria. Frequently, bids submitted in breach of formal provisions of little importance envisaged by the *lex specialis* (for example, regarding the manner in which certain requisites are certified) were excluded from the procedure with the bidders being denied any chance to correct them. As a result, the contracting authority was deprived of the opportunity to compare the contents of a greater number of bids.

On the contrary, the approach adopted by the European directives envisages a different balance between discretion and formal rigour, with the administration having greater room for assessment and flexibility. It also permits dialogue with the undertakings for the purposes of acquiring information (as is the case with the competitive dialogue procedure). From this perspective, discretion is a value that should be cultivated as it permits the administration to make the best choice in relation to the actual individual circumstances. Moreover, the formalistic application of the rules contained in the *lex specialis* is discouraged.

The Code expresses this new balance in several central institutions: the criterion of the economically most advantageous bid as opposed to that of the lowest price; the gradual specification of the bid assessment criteria; the discretionary assessment, including consultation with the tenderer, of the verification of anomalous bids. In these and in other cases, the contracting authorities have considerable room for discretion, which the administrative courts normally tend to respect.

Another defect of the traditional Italian approach to the rules on public contracts is, as mentioned, the formalistic application of the rules. This type of approach favours the exclusion of bids with even minimal formal errors and may lead to the annulment of entire procedures which are vitiated by errors that are, in reality, not fundamental.

A more substantive vision, based on the new European approach, is emerging in some rulings by the *Consiglio di Stato* and

the Regional Administrative Courts with regard to exclusionary clauses, which are envisaged by many calls to tender and which provide that any failure to comply with any clause of the *lex specialis* will automatically result in exclusion from the process.

Indeed, a recent tendency by the courts is to restrict this type of "*error hunt*". According to the most recent ruling, formal irregularity does not imply the exclusion from the tender process of operators which essentially meet the envisaged requirements (according to the "innocuous falsehood theory").

The European law has conditioned two further aspects of the Italian rules on public contracts.

In the first place, the civil liability of the public administration for unlawfully awarding public contracts is greater than that envisaged by the Italian Civil Code and applied by the administrative courts with regard to the issue of unlawful measures. The latter is construed as a case of tortious liability of the public administration pursuant to article 2043 of the Italian Civil Code for which wilful intent or negligence is required on the part of the agent. However, in the public contract sector, a contracting authority may be held liable even if the administration has not been shown to have been negligent, precisely to ensure the effectiveness of the protection envisaged by the European directives. Recently, the *Consiglio di Stato*[9] expressly upheld, exclusively with regard to the public contract sector, the concept of objective liability, in accordance with the indications of the European Courts. As a consequence, any undertaking that has been unlawfully excluded from a tender process and is unable to obtain judicial assignment of the contract (specific performance) will automatically receive compensation, which is an important incentive for the administration to manage the process properly.

In second place, from a procedural standpoint, Directive 2007/66/EC (the New Remedies Directive)[10] made the Italian legislator introduce a special proceeding for public contracts,

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[9] *Consiglio di Stato*, Sect. V, judgement no. 5686 of 8 November 2012.

[10] An analysis about the New Remedies Directive is given by J. Golding and P. Henty, *The new Remedies Directive of the EC: standstill and Ineffectiveness*, in *Public Procurement Law Review* 17, 146, 2008; P. Henty, *Is the standstill a step forward?: The proposed revision to the EC Remedies Directive*, in *Public Procurement Law Review* 15, 253, 2006.

which envisages very different procedural rules and powers of the administrative courts (now contained in articles 120-124 of the Code of Administrative Procedure). As mentioned, the proceeding is particularly rapid (with procedural deadlines reduced to a minimum) and is intended to guarantee the effectiveness of the remedy either through correction of the infringement that caused injury to the interests or through full compensation. Moreover, administrative courts may issue rulings with a range of contents, such as, for example, annulling the contract and establishing that the annulment is not retroactive.

Under Italian law, undertakings in the public contract sector and, more generally, the application of the competitive principles contained in the Code enjoy an additional level of organisational and institutional protection, which is not required by European law. The first few articles of the Code regulate the organisation and the tasks of the Public Contract Regulator, which was set up to monitor contracting authorities' activities, to disseminate best practices and to resolve certain disputes between undertakings and contracting authorities out of court. The Code has extended the Regulator's field of action, which was originally limited to public works, to include the entire public contract market. The very recent anti-corruption law (Law no. 190 of 6 November 20120) provides that the Regulator has to collect and compare on its website a large amount of data regarding contracts awarded by the contracting authorities (winning economic bids, number of participants, etc.), so as to allow more effective supervision of the public contract market. The regulator's action is accompanied by the prerogatives of the Italian Antitrust Authority which has on several occasions used its power to report anti-competitive legislation and practices to the Government and Parliament and to request amendments.

4. The most recent legislation.

As mentioned, the economic crisis has led to numerous legislative interventions on the framework outlined above, which have amended various provisions of the Code of Public Contracts, especially since May 2011 (up to the aforementioned very recent anticorruption law).

Some of the amendments are of a structural nature in that they have an impact on aspects of public tender processes in accordance with the four guiding principles that are destined to condition the subject for a long time to come: the reduction of the costs of public works; the reduction of the time taken to execute public works and the simplification of procedures; a more effective supervisory system; the reduction of disputes.

Thus, for example, restrictions have been introduced on the objections that an undertaking that has been awarded a public works contract may raise during the execution of the works (which may give rise to an increase in the costs for the contracting authority) and an expenditure ceiling has been envisaged for "variations" during the execution of the works, which often make the execution of the works more costly; the threshold amounts envisaged for the award of contracts through the negotiated procedure have been raised; there is a strict list of causes of possible exclusion from the award procedure and the contracting authorities are prohibited from adding others in the calls for tender; there are sanctions for parties that start "reckless" disputes, i.e. which bring manifestly unfounded legal actions.

Particular consideration has been given to small and medium-sized enterprises in the legislation that has been issued to address the economic crisis. In particular, the legislator has issued provisions with the force of general principles on the subject that require contracting authorities to subdivide, where possible and economically advantageous, the contracts into functional lots so as to encourage small and medium-sized enterprises to take part in the tender processes. Moreover, the execution of large infrastructure works, and the associated supplementary or compensatory works, must guarantee procedures for the involvement of small and medium-sized enterprises (article 2, paragraphs 1-*bis* and 1-*ter* of the Code, introduced by article 44, paragraph 7, Law no. 214 of 2011).

Various criticisms may be made with regard to these last provisions.

Firstly, provisions of this type appear to go against the original plan on which the European law on public contracts is based, i.e. the need to create "European champions" that are increasingly able to compete on a worldwide scale. Secondly, although the fragmentation of public contracts may have a

positive impact on competition as it increases the number of participants and reduces entry barriers and risks of collusion between undertakings, it could also produce side effects with regard to competition. The creation of contracts with a low economic value makes such contracts less attractive, with the consequence that increasingly fewer operators will be willing to take part in tender processes outside their traditional field of action. Therefore, if it is always the same small and medium-sized enterprises that take part in the processes, this will have potentially negative effects on relations between contracting authorities and contractors, in terms of quality and efficiency of the performance of contracts[11] and also on the efficiency of the undertakings themselves, which will have no incentive to develop their organisation or to expand.

Indeed, according to the Italian Antitrust Authority, subdividing contracts into lots is not always compatible with the pro-competitive principle. In particular, there are two restrictions which would have a beneficial effect on the subdivision of contracts: the number of lots should always be lower than the number of undertakings that may be expected to take part in the tender process; there must be no limit on the number of lots that each participant may be awarded as "*a limit such as this could encourage forms of coordination between the participants of the tender process with the objective of dividing up the lots for which the bids will be submitted* ".

Therefore, the introduction of the new provisions raises certain doubts, In fact, if interpreted too strictly in favour of small and medium-sized enterprises, it could distort competition.

5. Brief conclusions.

In conclusion, the approval of the Code of Public Contracts, in implementation of the European Directives, has changed the traditional approach of the Italian legislator to the regulation of public contracts as the Code is less inspired by need to protect

[11] In this brief article there is no time for discussing about an important subject such as the performance of public contracts. For a good analysis focused on this theme, see A. Giannelli, *Performance and Renegotiation of Public Contracts*, 2013, on www.ius-publicum.com.

competition and more favourable to undertakings. Moreover, there is still a tendency to interpret the provisions on the tender processes in a formalistic manner and, where possible, contracting authorities prefer tender processes with a low level of discretion, as is demonstrated by the fact that institutions such as the competitive dialogue are almost never used in practice. Finally, the legislator continues to introduce amendments to the Code, sometimes with objectives that are inconsistent with the general framework of the latter.

In essence, the public contracts sector is still unstable from a legislative perspective and the application of the rules is characterised by uncertainty and variations. All this has negative repercussions on the activities of the contracting authorities, the undertakings and, more generally, legal operators. Despite the attempts to discourage judicial disputes, even through remedies of dubious appropriateness (such as the increase in the taxes and costs of filing applications), the level of litigation is still extremely high.

At this point, it would be best to impose a legislative "moratorium" in order to allow the rules to stabilise. Instead, there is much that should be done at a sub-legislative level to maximise the spread of best practices and to improve the professionalism and technical expertise of the contracting authorities. The Public Contracts Regulator has a fundamental role to play in all of this and it has now been given sufficient powers to monitor the public contracts market.