DRAFT BILL ON THE STATE PURCHASING ACT

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The Federal Government has concluded the elaboration of a new draft bill on the State Purchasing Act (or Bidding Act). The new proposed text was published in the Official Gazette *[Diário Oficial da União]* of February 19, 1997. Suggestions for possible improvements are welcome and can also be sent through e-mail. The legislation currently in force - Act 8666 - is very recent. Nevertheless, nearly everybody tends to agree that it ought to be substantially amended, if not entirely replaced by a new law.

Why has Act 8666 failed? For the following two basic reasons: (1) because its strict regulatory and bureaucratic provisions limited the public manager's authority to a minimum, thus making purchases by the government and the state-owned companies much more expensive and time-consuming, while on the other hand providing poor control on fraud; (2) because when President Itamar Franco vetoed an article requiring contractors to provide exaggerated technical guaranties (which was in conformity with the law's bureaucratic nature), the state was left with no guaranty at all as to the actual delivery of the works and services contracted. This gave firms with no technical or financial capacity a way into major biddings. The new legislation corrects these two errors.

By striving to prevent corruption through strict written bureaucratic provisions, Act 8666 expressed no concern for bringing purchase prices down for the state. At the same time it made it impossible for the public manager to make decisions. It took for granted that every public servant was corrupt and that, as such, should be given no authority to handle negotiations. The law was to be coldly enforced. It did certainly

limit the corrupt manager's room for action. At very high cost, though: honest public managers - the overwhelming majority - were tied up in their ability to work out the most advantageous deal for the state.

Nonetheless, the door to price-setting arrangements among bidders was left open, for it is impossible to prevent such occurrences by the enforcement of mere administrative provisions. Only by penal action can the formation of cartels be discouraged, but the penal aspect was surprisingly underprivileged in Act 8666.

The second mistake was to take engineering works as the standard for reference and definitions. Engineering works present bidding situations, which are complicated by definition. They call for projects and the assessment of the contractor's technical and financial capacity. They should not provide the yardstick for a number of other ready-made goods and services, which are purchased or contracted out by the state rather frequently. The new project substantially simplifies the minor purchases, not only by raising the threshold beyond which a bidding must take place, but by simplifying the procedures themselves.

The third mistake was not to have given the state more guaranties to contract out. The Congress had passed a bill that posed excessive demands on the technical-operational capacity of bidders, in which was vetoed by the Federal Government in an attempt to protect small and medium-sized companies. The consequence was that no actual demand for guaranty was kept in the law.

As a result of all these errors, the procurement process was made slow and expensive. Early estimates indicate a price markup in state purchases between 10% and 20% of the actual price. The proceeds are costly to the state, as it has to pay close attention to every formal provision of the law and specify in advance every screw deemed necessary in the works to be contracted out, or the amount of polishing wax or the number of brooms to be bought. Costly also for the bidders, who are demanded to present unnecessary documentation and are faced with lengthy deadlines. In addition, there is great easiness, or rather encouragement, to file appeals, which have become an industry built around the flaws in the legislation. The complex legal formality makes it impossible to produce a perfect Call for Tenders and invariably yields numerous allegations and claims, the aim of which is but to procrastinate. Any unsuccessful bidder may go to court at nearly no cost at all, since the burden of proof falls on the Administration, not on the bidder.

There seems to be a consensus in the government and in the public sector as a whole about the need to reform this legislation. The only exception comes from insensitive bureaucrats and a handful of

minor bidders who benefited from the President's veto on the need for technical capacity certification. They argue that it is important to control the public manager's deeds and fight corruption, and that this can be achieved through the establishment of detailed regulatory provisions to reduce subjectivism to a minimum in public bidding processes, taking decision-making away from the public manager. This way, bribing one public servant would prove useless and he or she would become as incorruptible as a robot. This preaching, however, is outmoded and bureaucratic, and should not be expected from a modern entrepreneur. It comes from the assumption that the public manager should never make any decision and blindly follow a clear set of regulations. It is understood that public management calls for caution. The state should not purchase goods and hire services as freely as a private company. But this is not to say that the Union and the state-owned companies are doomed to inefficient and irrational buys. Not at all.

Aware of this need for a change, the Government has concluded the first phase of the law's revision. The project drafted intends to prevent, or at least reduce, the five following costs: (1) the cost of kickback arrangements between seller and buyer (corruption); (2) the cost of price-setting arrangements among bidders (cartel); (3) the cost of receiving a good or service of inferior quality than what was promised (fraud); (4) the cost of simply not being delivered the goods or services at all, due to the incapacity of the successful bidder; and (5) the cost of delayed purchasing owing to bureaucratic red tape and the possibility to file empty appeals for procrastination purposes.

Act 8666 concerns itself with the first of such costs only, and does so by taking any decision-making away from the procurement committees. It certainly did not solve the problem of the second cost outlined and did poorly in addressing the other three.

The occurrence of fraud upon delivery of the service or work contracted is a function of the lowest-price principle. The cost of not receiving the actual goods or services contracted derives from the lack of minimum guaranty demands on suppliers. The cost of more expensive purchases is a consequence of manifold demands for documents and deadline compliance, plus the possibility to appeal and postpone. Finally, and in addition to all that, there is the Government's inability to pay on time. These costs are eventually incurred by the state, as suppliers have no alternative but to incorporate them to the final price.

The Bill

The new draft bill is the result of a broad survey carried out by the Ministry of Federal Administration and State Reform. It is also the result of the efforts by a work group coordinated by the State Department. The focus of the new legislation is to avoid those five costs. To achieve this goal, several strategies were devised.

As provided by the Constitution, Title I of the new law will be devoted to the principles and general norms governing the bidding process and the penal dispositions derived thereof, to be enforced nationwide. The remaining sections of the law, of specific character, shall only bind on direct federal administration, public foundations and autonomous entities. They shall however be mandatory for the autonomous agencies at state and local level, as well as state and local Judicial and Legislative Branch agencies for as long as they do not issue their own provisions and regulations.

Penal dispositions have been aggravated from the text currently in force. For example, the penalty for price-setting arrangements among bidders or the bribing of competitors has grown from detention to up to three year-term imprisonments.

The bill classifies the object of bidding into seven categories: (1) tailor-made works and services; (2) standardized goods; (3) goods in general; (4) engineering services; (5) specialized technical services; (6) brokerage services, as in advertising and tourism; and (7) other services. This classification goes from minor to major complexity. This way, it can be further detailed and differentiated in specific legislation or Call for Tenders documentation, into degrees of complexity and value and as to documentation, guaranty and deadline requirements deemed necessary in each particular case.

Title I determines that documents shall be required of the bidder in certification of (a) judicial capacity; (b) fiscal compliance; (c) technical qualification; and (d) financial-economic capacity. No reference is made to specific documents, though. Under Title II, however, applicable to direct federal administration agencies, foundations and autonomous entities, documents are specifically identified, thus presenting the parameters for use by the indirect administration, state and local government agencies.

The proceeds for minor purchases have been simplified. The competition known as Invitation to Bid was eliminated. The limit beyond which a bidding is required has been raised to R$ 30 thousand. Up to this limit, the public manager takes full responsibility for the process, which must be justified in writing. In the Invitation to Bid, the choice was backed by the higher prices of other companies (sometimes in price-

setting arrangements). Those Invitations were not necessarily published in the Official Gazette. This has changed, now. In 30 days' time all purchases by the Federal Government in Brasilia will be available on the Internet, for absolute transparency.

The limit beyond which a bidding becomes necessary is R$ 3 million. Between R$ 30 thousand and R$ 3 million, a simplified form of competition shall be established - the so-called price-quoting. Here, bidders are required to register in advance, thus eliminating the qualifying rounds that used to make biddings much more complex and time-consuming.

The industry of appeals has been struck through an inversion in the burden of proof. It is now up to the accuser to objectively substantiate the illicit practice in his or her appeal. Any sign of bad faith on the part of an accusing bidder may be reported to the Public Prosecution.

The aim of the law is to permit the state to purchase or contract at market price, not at the lowest possible price any longer, especially when this price proves unfeasible. Objective criteria will be defined to allow the elimination of unfeasible prices. In cases of low competitiveness, explicit authority will be given to set maximum prices.

The Administration shall be given greater flexibility for deliberation. For large works, where the best-price-and-best-technique criterion may prevail over the best price criterion, the Procurement Committee is free to negotiate with the technically best bidder who will eventually have a chance to bring its prices down to the best price bid. This cannot be done at present, for the best-price-and-best-technique criterion can only be applied to biddings on "predominantly intellectual" services. The law currently in force has in fact a provision allowing for such procedure under very exceptional circumstances, but the requirements and conditions are so many that it becomes virtually unfeasible. The concern behind so much formality and inflexibility in the current legislation stems from the understanding that biddings on the basis of "best technique" could eventually privilege this or that contractor, given the subjectivism of technical assessment procedures. This risk is eliminated in the new legal text. The technically best bidder will simply be given the chance to lower the price later.

Electronic registration systems made public through the Internet will continue to be implemented. The registration of suppliers (already implemented over the last year by the government), will be completed by the goods and market prices registration. The suppliers registration shall eliminate the demand to disclose documents at the time

of competition and will set a standard for a growing number of products. The definition of standard goods and services and the knowledge of fair prices will also become readily available. Bidders will be able to automatically register themselves. The validity of documents and the bidder's compliance to particular requirements will be checked electronically. This system of registration, along with other features provided for in the new legislation, shall make purchases a lot quicker and more inexpensive, as much as they will simplify the bidding processes. The chance for judicial appeals will be reduced, as will the need to disclose qualifying documents in price-quoting and other forms of competition.

For the qualifying phase the general provisions of the law shall specify the need for judicial capacity and fiscal soundness, as well as technical and financial-economic certification on the part of bidders. With respect to their technical skills, a more specific section of the law shall demand bidders to attest the previous performance of works and services that are similar to the object of the competition, up to five contracts being possibly considered here. This requirement is halfway between what is currently demanded (nothing) and what was provided for in the original, vetoed text.

The consortium of companies shall be expressly accepted.

With regard to guaranties, the bidder will be able to choose from the following possibilities: deposit, financial bail, warranty insurance (which may be partial) and performance bond (which guarantees the delivery of the complete work). The bidder will be able to replace all guaranties, as well as the whole documentation regarding technical and financial-economic qualification. These forms of insurance privilege the companies' quality and reliability, much more than their size or financial capacity. Small and medium-sized companies therefore shall not be harmed, as long as they are able to prove their quality. The insurer shall not be uncomfortable backing up a company that although relatively small has the technical competence to win the competition. The form of insurance that privileges big companies, the so-called bid bond, was not considered in the new legislation.

The inclusion of financing arrangements shall be permitted in competitions involving state-owned companies or joint-stock companies of mixed capital that generate income enough to amortize such financing, provided their cost is clearly known.

The case of travel agencies and advertising companies will deserve special attention, as their system of standard commissions invariably increases prices for the state. Here, the technique-and-price

criterion shall be applied so a maximum discount or a minimum commission can be settled that will avoid predatory competitions. In the event of a draw, the technique will provide the tiebreak parameter.

All these provisions are combined in a new legislation that shall be up-to-date and more easily manageable, in conformity with the modern and effective public sector that we all look forward to building in compliance to the guidelines contained in the *Master Plan for State Reform* [*Plano Diretor da Reforma do Estado*] prepared by the Ministry of Federal Administration and Reform of the State approved by the President in September 1995.[1] This plan advocates a reform of the state based on the ideas of privatization of state-owned enterprises, "publicization" or "corporativization" the social, scientific and environmental services of the sate (i.e., its transference to competitive non-governmental organizations), and outsourcing of the auxiliary (non-core) government activities. And a reform of the civil service so that will substitute a bureaucratic for a managerial public administration - an administration outcome oriented and citizen oriented.

In this vein, procurement committees shall be granted greater authority and responsibility. The complexity of the bidding process will mirror the nature of the object being purchased or contracted. Biddings will become more agile and less costly. The state, as well as those state-owned companies that fail to be privatized, will be able to purchase goods and hire services at lower costs and higher speed, with no loss of the required controls in the management of the *res publica* (the public patrimony), which will actually be greatly safeguarded inasmuch as the taxpayer's money is more wisely spent.

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1 - There is a printed English version of this paper and it is also available at the Ministry's home page (http://www.bresserpereira.org. br).