

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(90) 166 final

Brussels, 7 May 1990

COMMUNICATION FROM THE COMMISSION TO THE COUNCIL

PROMOTING SME PARTICIPATION
IN PUBLIC PROCUREMENT
IN THE COMMUNITY

1. INTRODUCTION

1. The purpose of this communication is to review the role of small and medium sized enterprises (SMEs) in the context of the opening-up of public procurement in the Community and to indicate ways in which this role might be enhanced.
2. The Community's programme for the opening-up of public procurement, now well on the way to completion, should lead to the removal of national, regional and local obstacles to participation in award procedures for public contracts. The legislative provisions have been designed to ensure that, so far as possible, all business, large and small, should have access to public contracts on an equal footing. These provisions, however, can only provide a framework within which the final objective - the building of a Community-wide market - can be pursued. It is here that positive measures to promote SME participation in public procurement have their contribution to make. As was pointed out in the Commission's communication on "Public procurement : regional and social aspects"⁽¹⁾, fuller participation by SMEs will bring the benefits of mobilisation of new resources, increased competition and stimulus to entrepreneurship.
3. Greater participation of SMEs would add both to the quantity and quality of competition in public markets. If SMEs do not participate as fully as possible in public procurement, a significant part of the potential competition is missing. Moreover, smaller enterprises can be particularly flexible in responding to market needs primarily because of their more simple structures and closeness to the market place. Their capacity to provide innovative solutions is also important. At the same time, developed participation would ensure that SMEs play a fuller role in a very significant sector of economic activity which can only help to stimulate enterprise and small business development which are important contributors to economic growth and employment.
4. The Commission's Action Programme for SMEs,⁽²⁾ approved by the Council in November 1986, stressed the importance of providing SMEs with real access to public contracts. In reviewing relevant policies and practices, this communication has made use of an inventory and study of the experience of Member States and also of Japan and North America,⁽³⁾ which was carried out within this programme.

(1) COM (89) 400

(2) COM (86) 445 final

(3) "SMEs and Public Procurement" prepared for the Commission by W. S. Atkins

II. THE CURRENT SITUATION

5. SMEs account for a significant part of the Community economy. Excluding the self-employed some 69.8 % of employment in the manufacturing and service sectors is in enterprises employing less than 500. Such enterprises account for 99.8 % of all enterprises. Enterprises employing less than 100 still account for 51.9 % of employees and 98.7 % of enterprises.
6. There is, however, a long-standing concern that SME participation in public contracts does not reach levels commensurate with the SME share in the economy. Thus even in France which has a developed policy of promoting SME participation, the level has remained at about 30 % of the total value of contracts awarded, a level which is significantly lower than is achieved in Japan and North America.
7. The thrust of the new Community regime is to open a much higher proportion of public procurement to competitive pressures and, potentially, to SME participation. Since, however, such opening-up is affected by new regulation of the procedures by which contracts are awarded, some SME's may perceive the formalities created by those regulations as obstacles rather than as the necessary foundation for new opportunities. At the same time others, who already sell to their public sector, may fear intensified competition from larger, more sophisticated, perhaps non-national enterprises.
8. This communication is, therefore, devoted to reviewing the possibilities for a more active policy to ensure that SMEs participate to the full extent of their potential in the internal market for public procurement.

III. THE SCOPE FOR COMMUNITY ACTION

9. Certain broad criteria can help identify those measures which offer the best prospect of improving SME participation in public procurement without imposing unacceptable costs. Such measures should :
 - increase the volume of work offered to SME's without creating dependency on public contracts or incompatibilities with Community rules on open procurement;
 - improve the quality of SME participation in award procedures by, among other things, improving their technology, and thus improve their competitive position, without discriminating against larger enterprises;
 - not lead to higher cost of goods and services through sacrifice of economies of scale, possibilities of standardization and the requirements of good commercial practice as regards price, quality and performance;

- not add disproportionately to administrative costs, through fragmentation of contracts; additional requirements for specialized technical assessment; monitoring requirements; or the restructuring of procedures which are not balanced by long-term gains.
10. Action at Community level should seek to :
- promote the evolution of law and practice both at Community level and within the Member States;
 - help prepare firms for the achievement of the large internal market in 1992 by making them more aware of the opportunities offered by the single European market and cross-border co-operation;
 - build on existing initiatives and resources, both at the level of the Community and of the Member States.
11. On this basis, certain areas have been identified, as particularly appropriate for policy development and action. These are reviewed in the following section under four main headings.

IV. AREAS FOR POLICY DEVELOPMENT AND ACTION

A. Measures discriminating in favour of SMEs

12. Such measures may discriminate in favour of SMEs and against larger undertakings, either directly or indirectly. Indirect discrimination could arise where SMEs predominate among the enterprises of a region or locality which is itself the subject of preference. Such measures have generally taken one of the two forms :
- the reservation or set-aside of certain contracts;
 - discrimination in the evaluation of bids through the acceptance of bids from qualifying enterprises exceeding bids from other enterprises by a given price percentage.
13. While elaborate systems of preference continue to exist in the USA, they have been rejected in most other developed countries, including Member States, as being administratively costly and protecting economic inefficiency, distorting competition and discouraging modernisation and improvements in productivity. The Commission, in its Communication on "Public Procurement : Regional and Social Aspects"⁽¹⁾ has expressed similar concerns, also underlining the incompatibility between certain preference regimes and Community law. The requirements of Community law in this context have recently been reaffirmed by the Court of Justice of the European Communities (Case C-21-88 : Du Pont de Nemours Italiana Spa and Unità Sanitaria Locale no. 2 di Carrara 20 March 1990).

Steps are now being taken to bring to an end the infringements of Community law which result from their operation. Such measures are not, therefore, discussed further in this communication.

B. Measures which facilitate access of SMEs to award procedures for public contracts

14. The first contribution Member States must make is to ensure full observance by contracting authorities of the principles and disciplines of the Community's public procurement regime. It is SME's seeking to penetrate new markets which are the first victims of resort to negotiated or restricted procedures, where these are used to favour secure relationships with known enterprises or to cope with programmes delayed until the end of the budgetary year, rather than justified by urgency arising from genuinely unforeseeable circumstances or from the need for specific technical qualifications.
15. It is also open to contracting authorities to apply certain provisions, particularly that on publication of tenders free of charge in the Official Journal of the European Communities for contracts below the threshold at which this is made obligatory under the public procurement directives. Although smaller contracts might be expected to be generally appropriate for smaller enterprises, it has been estimated in one Member State with an active policy of promoting SMEs, that at least one third of such contracts are being awarded to larger enterprises.
16. Contracting authorities may themselves go beyond the minimum advertising requirements under national legislation, for example by introducing a simplified form for contracts below obligatory national thresholds. They may also co-operate in the diffusion of tender information in parallel with published tender notices through the use of contact points, established at regional or departmental level, perhaps in association with Chambers of Commerce or other bodies representing enterprises. Further development of services adapted to the needs of SMEs, based on tender information supplied by contracting authorities, is dealt with in paras. 33 - 35.
17. Adapting the scale of individual public procurements to the productive capacity of SMEs is incontestably favourable to their participation in public contracts. The break up of larger contracts, however, carries the risks of adding to administrative costs, losing the benefit of potential economies of scale and offering a pretext for evasion of the thresholds of application of the public procurement directives. Division of larger contracts into lots may by contrast, enable the objectives of open and efficient public procurement and accessibility to SMEs to be simultaneously attained. The contracts for the lots would be fully publicised, while firms which bid for a lot would have to match the price offered by larger enterprises for the full contract.

18. The alternative approach, adapting the productive capacity of SMEs, to the economically justified scale of public procurement may be achieved through various forms of association or co-operation, such as joint ventures, cooperatives, economic interest grouping or public companies with SME's as their shareholders.
19. The Community has long actively promoted the development of such co-operation between enterprises, adapting its competition rules to exempt small-scale co-operation agreements, promoting transnational co-operation within Community programmes, such as ESPRIT BRITE and COMETT and providing, through the Business Co-operation Network (BC-Net) developed by the Commission's Business co-operation Centre, a service to SME's seeking potential partners in bidding for public contracts. The Community has, also, in the provision for the European Economic Interest Grouping (E.E.I.G.) provided a clear legal framework within which such co-operation can take place. The Europarteneriat programme aims at helping selected SMEs in regions being assisted by the Structural Funds to form cooperative business agreements with SMEs throughout the rest of the Community and thus mutually strengthen their respective abilities to compete in the market.
20. Member States have a positive role to play in removing legal and fiscal uncertainty which may continue to inhibit the use of such forms of association, and in fostering the development of new forms, where appropriate and necessary. The Community may reasonably expect their support in helping the E.E.I.G. to become fully operational. Member States can also assist these developments by reviewing their public procurement rules which govern the assessment of financial and technical capacity on a joint basis.
21. SME's have complained of their exclusion from selection by contracting authorities, which impose on them unreasonable or unnecessarily specific requirements as regards qualification. Contracting authorities should review the need for such requirements and the form in which they should be met. Further reflection and study is needed on the underlying issue of how the quality of enterprises is to be assessed, certified, compared and, where necessary, improved.
22. SMEs increasingly gain access to larger public contracts through the sub-contracting of work from large contracts. The public procurement directives leave Member States a wide freedom to pursue an active policy of encouraging local sub-contracting. Following the logic of the decision of the Court of Justice in Case 31/87 (Gebroeders Beentjes v. the Netherlands), it is open to them to use contract conditions to promote sub-contracting, providing this is not done in a way which has the effect of discriminating against enterprises from other Member States.

23. The Commission has set out its approach to the promotion of sub-contracting in a Communication to the Council⁽⁴⁾ on the development of sub-contracting in the Community. In particular, sub-contracting could be encouraged in appropriate circumstances, larger contractors being required to indicate their sub-contracting intentions in their offers, such intentions being published in contract award notices to give SME's adequate opportunities to present offers related to the execution of each sub-contract. Sub-contractors could also be given assistance by main contractors in meeting their qualification and certification requirements.
 24. A clear and balanced legal framework would make it easier to tender for sub-contracts in other Community countries. The review of procedures referred to below (Para. 26) should pay particular attention to the specific issues involved in sub-contracting, such as : the recognition given by public authorities to sub-contractors; the principle that a main contractor should offer to his sub-contractors conditions identical to those to which he is subject; the payment terms granted to sub-contractors; and questions of redress in cases of non-payment or of insolvency of the main contractor. Sub-contracting is thus to be promoted and protected in a balanced way. Measures are also required to eliminate evasion of tax and social security regulations.
- C. Measures which reduce the costs incurred by SMEs in public procurement
25. The administrative and financial costs, imposed by complex public procurement procedures can be such as to discourage SME's with little experience of working with public authorities from bidding even for smaller contracts.
 26. Simplification of procedures would benefit firms of all sizes and, in the medium term, the purchasing authorities themselves. Member States should review : the cost and actual utility of the documentation required of SMEs in submitting tenders; the difficulty caused to SMEs by allowing insufficient time for bid preparation on the one hand and costly delays between receiving and adjudicating upon bids on the other; the possibility of harmonising and simplifying the contract documents themselves. Particular attention should be given to ensuring that the procedures for small contracts, which are of relatively greater interest to SMEs, should be as straightforward and transparent as possible.

(4) COM (89) 402 of 7 August 1989

27. Contracting authorities should be aware of the potential contribution of electronic bidding information services in reducing costs and delays. Such services are being developed by suppliers of business information and related services on the basis of tender information sourced from the Official Journal of the European Communities and from contracting authorities. A fully developed electronic mailbox network embracing contracting authorities and interested SMEs would allow speedy communication requesting bid packages and the placing of queries between contracting authorities displaying contracts and potential bidders.
28. Delays in payment to contractors for work done vary greatly within the Community, depending on legal obligations, the requirements of audit and financial control and acceptable national or local practice. They can be such as to impose unsustainable losses on SMEs which depend on public contracts. Problems are multiplied where SMEs are sub-contractors dependent for payment on main contractors, themselves awaiting payment from contracting authorities.
29. Many improvements could be introduced by contracting authorities to ensure that contractors are kept in funds, through payments on account or higher percentage advance payment; measures to speed up accounting procedures, including reduction in the documentation required; and devices to minimise, or to minimise the inconvenience of, delays in payment, for example through the practice of issuing irrevocable letters of credit, which remove the threat of insolvency to SME's dependent on substantial, but delayed payments. The Commission has carried out a study of the general problem of late payment as it affects SMEs, including late payments by public authorities and will consider how best it can contribute to its alleviation in the light of consultations on the study's findings.
30. Guarantees to ensure that enterprises do not withdraw offers once made and perform contracts to time and specification are a feature of most, but not all, national public procurement systems. Where they are lacking, or ineffective in protecting contracting authorities against the risk of major costs and inconvenience when a contractor defaults, contracting authorities are less likely to accept as contractors SMEs which pose a greater risk than larger enterprises. When there are functioning systems, on the other hand, SMEs can experience difficulty in obtaining the necessary guarantees at a cost which is not prohibitive.

31. Developments in this field are under way in a number of Member States. In Italy, for example, the introduction of performance bonds is being considered as an alternative to the present system, which, based as it is on a simple listing of all enterprises deemed to have sufficient financial and technical capacity, does not provide either contracting authorities or bidders, particularly SME's, with a solid basis for a contractual relationship. In Portugal, a sub-programme of the Commission's PEDIP programme is concerned with the development of a system of financial guarantees which will reduce the burden of the present system which requires borrowing at high interest rates to finance deposits by contractors. In certain other Member States, there is a movement away from exclusively financial guarantees backed by the banks to insurance systems or other arrangements, guaranteeing replacement of defaulting contractors, funded in some cases by the trades concerned. The Commission, in building-up an open public procurement market, will contribute to the search for technical solutions adapted to the particular situation of Member States. It will in the near future begin consultations on possible action in this field with interested parties, including the Advisory Committees on public procurement.
- D. Measures which prepare SMEs for effective participation in contract award procedures
32. The need for more comprehensive publication of information on tender opportunities has already been discussed in para. 21 in relation to the standard method of publication of notices through the Official Journal of the European Communities. An opportunity now exists to simplify these notices, which must in any case be adapted to meet the requirements of the new public procurement directives, through greater standardisation of descriptions of the tenderer, of the object of the procurement and of the essential procedural requirements of the purchasing authority. This development, taken along with that of electronic public procurement databases (see para. 33 below) and electronic bidding information services (see para. 27 above) should greatly facilitate access to basic market information.
33. The Commission has also developed the "Tenders Electronic Daily" (TED) database, to which all information on tenders published in the Official Journal is transferred. The system can be accessed either directly through the "Echo" Customer Service or by agreement with the Commission through a "Host" or Licencee, who can sell information from the database to other users. The "Host" is at liberty to enhance the database, for example, by adding information on unpublished contracts below the obligatory thresholds for publication and supplied to it by contracting authorities. A number of systems are currently being developed.

34. The Community has supported the development of localised projects, based on such host agreements, for example the POINT (Public Orders Information Network), a consultancy service provided by the Chambers of Commerce for North West Rhine-Westphalia. The value added by POINT consists in the selection of information from TED which is relevant to the needs and capacities of the enterprises using the service and also in the arrangement for co-operation now established with similar organisations concerned with tender information in other parts of the Community. The market building potential of such projects is illustrated by the dramatic rise of 96 % in the first year of operation of the number of enterprises being drawn to the attention of the purchasing services of the Land concerned.
35. The network of Euro Info Centres developed by the Commission, which is being extended to provide a service to SMEs throughout the Community, provides access to information on tenders published in the Official Journal. The centres can help SMEs to respond to tenders of interest to them, in particular to tenders issued in other Member States. For example, the Bilbao EIC scans the TED data-base daily and notifies enterprises and Chambers of Commerce in Spain of contracts throughout the Community. The Diemen and Helmond EIC in the Netherlands jointly produced a guide to public procurement in the Community. The Bordeaux EIC is actively involved with the support of the regional authorities in Aquitaine with those responsible for procurement in the public works domain.
36. Other activities which can be supported in the field of general information on the implications of open public procurement include :
- support for public procurement fairs designed to bring SMEs into contact with purchasing authorities in their own and in other Member States;
 - support for seminars and conferences for SME managers to encourage participation in public procurement by explaining procedures and describing opportunities;

For example in this area the Commission has recently supported participation from SMEs from throughout the Community in a major European conference in London in April 1990 on new opportunities for business in the light of the opening-up of public procurement; the necessity for measures to enable SMEs to participate fully in the opening up of public contracts throughout the community emerged as one of the most important conclusions of this conference;

- the preparation of practical manuals explaining procurement procedures and legal aspects of public contracts, as in the Commission's brochures available in the Community languages and the recent guides to public procurement prepared by Córas Tráchtála, the Irish Export Board, which provide essential information on procedural and legal requirements of the systems of other Member States.

37. Access to information is the logical means of overcoming market imperfections. It does not, however, of itself guarantee a mutual understanding by contracting authorities and SME's in search of market opportunities, if their relationship remains bureaucratic, without the effective development of communication or managed dialogue beyond the point of initial contact. There is also a need to communicate to public purchasers that the involvement of smaller firms in public procurement is very much in the public interest and is also of benefit to the purchasing organisation because it widens the range of potential suppliers and develops their competence. The content of training courses for purchasing officers of contracting authorities could be adapted to assist in meeting these requirements.
38. As regards the development of the SME side of the dialogue with public purchasers, training in the necessary management skills is an essential element of strategic management, both for firms already selling to the public sector in their Member State and those wishing to equip themselves to enter the market or to operate across the Community. The pilot series of seminars for managers which the Commission has initiated within the programme "Preparing SME's for the Europe of 1992", launched in the second half of 1989, can make a useful contribution.
39. The activities discussed in para. 36-38 can be regarded as elements in an outreach programme, answering to certain general needs. They are not, however, designed to provide a sufficient response to the specific and perhaps pressing needs of individual firms for assistance with such matters as arrangements for certification, drawing up of market plans, preparation of bids or simple translation. In certain Member States, national or regional organisations, normally with a strong commercial and technological basis, are able to provide consultancy services to firms, which could include advice on the critical choice of specialisation within a changing public procurement market. Conscious of the vital role which SMEs can play in generating local economic development, the Community is supporting the establishment of EC Business and Innovation Centres, linked in an international network (European Business and Innovation Centre Network - EBN). These Centres provide, in an easily accessible and cost-effective way, services which assist firms entering the public procurement market.

40. Such services are particularly important in the peripheral regions of the Community, where SME's are heavily preponderant within the economy, and where the opening-up of public procurement brings particular challenges and opportunities. Local enterprises may have to face new competitors, better informed and with more sophisticated marketing skills. On the other hand, greatly increased investment in infrastructure with structural funds support and the potential for technology transfer from larger incoming enterprise can create the stimulus for radical improvement of the quality of enterprises supplying the public sector. The Commission has encouraged the inclusion of relevant services to enterprises within regional development plans submitted for Structural Fund support. In this context, it will study the different measures which are appropriate to resolve any serious problems directly associated with the implementation of open public procurement and in promoting its application at regional level.

V. CONCLUSION

41. Failure to achieve the best possible participation of SMEs in public procurement reduces the dynamism of the internal market at the same time as holding back regional economic development. It is therefore in the interests of the Community to ensure that any cost-effective measures which could promote their participation are actively pursued at the appropriate level.
42. This communication has reviewed a large number of measures. With the exception of discriminatory measures mentioned in section A which are contrary to the Treaty, these measures could, together, give substantial help to SMEs to participate more effectively.
43. At the same time, this review is only a first step. Much work remains to be done so that the ideas set out in the communication can be further developed and can be put into effect at the appropriate level, whether that be Community, Member State, region or locality.
44. The Commission, in close contact with the Member States and other interested parties, will therefore continue its work on measures which facilitate the access of SMEs to award procedures for public contracts, or the reduction of the costs incurred by SMEs on measures which prepare SMEs for effective participation in contract award procedures.

To this end, it will :

- encourage appropriate experiments and pilot-projects;
- critically study and evaluate the results achieved where measures have been put into effect;
- facilitate the exchange of information and ideas within the Community;
- report as appropriate to the European Parliament, the Economic and Social Committee and the Council, making where necessary, proposals.