

# Chapter 1

## Executive summary and main conclusions

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### 1.1 Background

Well-functioning markets are an essential source of economic growth and welfare of society. Among other things, well-functioning markets are characterised by enterprises competing effectively on all parameters and by easy access for customers on the markets to purchase the products that meet their demands at a low price.

In this study, the Danish Competition and Consumer Authority (DCCA) focuses on *public procurement through central framework agreements*. DCCA has as competition authority initiated this competition study in the autumn of 2013.

Central framework agreements can contribute to an effective public procurement system through the use of fewer resources in the procurement process, lower prices and a better match of supply and end user demand. This was addressed e.g. in the Danish government's 2013 strategy for intelligent public procurement as well as by the Danish Productivity Commission. Effective public procurement systems can support well-functioning markets.

One of the reasons why central framework agreements make public procurement systems more effective is that framework agreements remove the procurement obligation from the individual purchaser and consequently reduce procurement costs. And the reason for this is that centralisation creates the basis for a more professional procurement and tendering process, and that the agreements create the basis for a larger volume per product/per supplier. At the same time, framework agreements may reduce the suppliers' costs for selling their products because framework agreements will give more uniform terms and conditions for the actual purchases subsequently made. This may make it more attractive to tender for the contracts and thereby also enhance competition.

If central framework agreements account for a large part of total market revenue, there is a potential risk that this may restrain the ability of effective enterprises which are not parties to a framework agreement to sustain a commercial base and of new enterprises to enter the market. If that is the case, it may impede competition in the long term and result in price increases, a fall in supply and poorer solutions for customers.

If public tenders, including invitations to tenders for central framework agreements, are designed in such a way that they are not attractive for enterprises, or in such a way that the tender requirements, in fact, prevent enterprises from submitting tenders – all things being equal – competition to tender for a contract will weaken. An example could be if the assortment of goods or services to be supplied under the agreement is too wide. Overall, it may have the consequence that customers will pay a higher price or get a poorer solution under the agreement than otherwise.

If central framework agreements prevent enterprises from submitting their own tenders, the enterprises may form consortiums if in compliance with the competition rules. Consortiums can contribute to enhanced competition for contracts under a particular agreement, but may at the same time increase the risk that enterprises will exchange information about crucial competitive factors, such as price. This may weaken competition.

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The current study investigates whether there is effective competition between enterprises when they sell their products to public customers through central framework agreements, and whether it is easy for customers using central framework agreements to purchase good and useful products at a low price. If that is the case, central framework agreements can contribute to effective public procurement and to supporting well-functioning markets.

To form an overall picture of the competitive situation, the DCCA has chosen to analyse all markets with central framework agreements collectively rather than examining individual markets in this study.

The study is based on two questionnaire surveys among enterprises and purchasers about their *experiences and observations* from central framework agreements established by National Procurement Ltd. Denmark (SKI), the Central Procurement Programme, and the inter-municipal joint purchasing bodies as well as on data obtained from the contracting authorities and Statistics Denmark, and, finally, on a number of meetings, etc., with stakeholders, including trade associations, contracting authorities, purchasers and suppliers. For further information on the method used see section 1.13 and Annex 4.

## 1.2 Main conclusions

The DCCA estimates that annual public sector purchasing under the central framework agreements established by the SKI, the Central Procurement Programme and the inter-municipal and inter-regional joint purchasing bodies totals approximately DKK 13.7 billion. The purchases cover everything from standard products, such as ball pens, to complex services, such as construction consultancy services. This estimate is subject to great uncertainty as most purchasers and contracting authorities, in particular the inter-municipal joint purchasing bodies, have only very limited reliable knowledge of the actual revenue generated under central framework agreements.

The DCCA finds no direct indication in the study that central framework agreements will have an impact on market structures in the long term when analysed across the agreements examined. At an overall level, the central framework agreements established by the SKI, the Central Procurement Programme and the inter-regional and inter-municipal joint purchasing bodies account for only a minor portion of total public sector spending. Accordingly, the aggregate purchases made under these central framework agreements account for approximately 7 per cent of the total purchases made by municipalities, regions and the central government of a good DKK 200 billion from private sector suppliers, not including the construction industry, and less than 1 per cent of Denmark's total GDP.

Even though, at an aggregate level, central framework agreements account for only a minor portion of the economy, such purchases may account for a major portion in individual markets. No in-depth analyses have been made of the individual agreements to analyse the potential impact on the market structures of individual markets. However, to shed light on the impact on individual markets, the DCCA has obtained revenue data from Statistics Denmark on the suppliers under the central framework agreements established by the SKI and the Central Procurement Programme. The analysis of this data shows that, in almost 90 per cent of the 49 agreements on which the DCCA has revenue data, the *expected* average revenue from the framework agreements constitutes less than 20 per cent of the average *aggregate* revenue generated by the enterprises which are suppliers under the agreements. This means that at least 80 per cent of the revenue generated by the suppliers under the agreements is generated *outside* the central framework agreements in competition with other enterprises. With respect to the vast majority of the agreements analysed, there is consequently no direct indication that the expected revenue from the agreements is of such an order of magnitude that it prevents effective enterprises from competing on markets in which central framework agreements are used.

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In the long term the market structures can suffer if effective enterprises are forced out of the market due to the magnitude of the agreements today. However the study indicates that the volume of centralised public procurement under these agreements is not of such magnitude as to force out of the market effective enterprises which are not parties to the agreements, which would have a negative impact on market structures in the long term. It should be noted that the suppliers included in the study may supply to several markets. The data do not allow for a breakdown of supplier revenue on individual markets. Nor do the data allow for an analysis of the percentage of the revenue generated by the suppliers included in the study that derives from sales under central framework agreements.

Furthermore, 75 per cent of the enterprises responding to the questionnaire survey conducted by the DCCA which are not suppliers under a central framework agreement have not indicated that, in their experience, not being supplier under a central framework agreement has material consequences. However, approximately one fourth of the enterprises have indicated that they *have* experienced material consequences. In connection with the study, the DCCA has also been given examples by enterprises and trade associations of enterprises which experience that the revenue from central framework agreements constitutes such a large percentage of the revenue generated on that market that they find it difficult to sustain their commercial base if they do not have a contract under the framework agreement. It is therefore important to maintain focus on whether and how central framework agreements affect market structures, including how a potential increase in the centralisation of public procurement will affect market structures.

Furthermore, the study indicates that for the major part of the central framework agreements analysed there have been basis for effective *competition for contracts under the agreements*. At the same time, the study shows that there may have been only limited competition for contracts under some of the agreements. In 16 per cent of the 162 agreements analysed, all tenderers eventually were awarded a contract.

An analysis of the data on tenders for 162 framework agreements and lots established by the SKI and the Central Procurement Programme shows that five or more enterprises had tendered for a contract under 79 per cent of the agreements. Under 17 per cent of the agreements, three or less tenders were received (after any pre-qualification). The study further shows that three or more of the tenderers were *not* awarded a contract under 71 per cent of the framework agreements (after any pre-qualification). Under one of every five agreements (21 per cent), only one or none of the tenderers were *not* awarded a contract under the agreement. It is not possible to conclude on the basis of the current data whether the low number of tenders for some of the framework agreements is attributable to circumstances relating to the framework agreement itself, or whether they are owing to a limited number of enterprises operating in the particular markets.

Furthermore, the number of tenders received and the number of enterprises which were not awarded a contract have been determined subsequent to any pre-qualifying exercise, during which a number of tenderers were deselected. In a pre-qualification process, enterprises demonstrate that they have the ability to perform the contract, but they do not submit a tender proposal or a quotation. In a pre-qualification process, several factors are weighed, e.g. to ensure effective competition and to reduce total transactions costs for tenders.

The study shows that *certainty of revenue* from central framework agreements is essential for making it attractive for enterprises to tender for a contract (not a certain amount of revenue). Thus, the lack of certainty of revenue is the factor mentioned by most enterprises as being the most significant reason why they do *not* wish to tender for a contract under a central framework agreement (45 per cent). This may weaken competition. The study further shows that one of the most important factors for the tenderer's *pricing* is that the agreements provide certainty of revenue. To 40 per cent of the enterprises, certainty of revenue had an impact on their decision to offer or not to offer a lower price.

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This result must be seen in light of the fact that 54 per cent of the enterprises experience that the actual revenue generated from the framework agreement does *not* live up to the expected revenue specified in the procurement documents. The SKI and the Agency for the Modernisation of Public Administration have stated that it is their experience that the contract value specified in the procurement document often exceeds the actual revenue. This may be owing to several circumstances, including uncertain revenue estimates, competing framework agreements, low compliance, phase-in and/or implementation challenges, changes in the demand for the assortment of goods or services to be supplied under the agreement during the term of the agreement (e.g. in connection with general cuts in public spending) or lower prices in connection with the tender (which will generally result in lower revenue even if the volume is as expected). The SKI and the Agency for the Modernisation of Public Administration have also stated that it appears from the procurement documents that the contract value specified in the procurement documents does not imply a guaranteed volume, but an expected contract value, which may turn out to be higher or lower than specified.

Moreover, the questionnaire survey conducted by the DCCA indicates that the *assortment of goods or services to be supplied under several agreements has been so extensive* that this has resulted in fewer tenders for a contract: Forty (40) per cent of the 59 enterprises which were eligible to tender for a contract, but which decided not to, indicated that they strongly agree/agree that they opted *not* to tender for reasons related to assortment width. Most of the enterprises which would have liked to tender for a contract, but which were unable to meet requirements, reported that they were unable to supply the full assortment required (note: few respondents).

The study further shows that there are consortiums among the suppliers under four of the 25 framework agreements established by the Central Procurement Programme and under 14 of the SKI's 41 voluntary framework agreements. The consortiums seem to be predominantly found among the suppliers under framework agreements for consultancy services, e.g. IT services and engineering and architect services. The most common reason for tendering as a consortium mentioned by the enterprises which responded to the DCCA's questionnaire survey is that enterprises are unable to supply the full assortment on their own (35 per cent). However, approximately one of every four respondents indicated that the enterprise would have been able to submit a tender on its own, but that it was financially most advantageous to tender as a consortium. It may be in violation of the Danish Competition Act to tender as a consortium for contracts which the enterprise would be able to perform on its own, and consortiums risk aiding the (implicit) coordination of tasks and prices outside the framework agreement and in future.

In summary, the study findings seem not to give a direct indication that central framework agreements will have an impact on market structures in the long term when analysed across the agreements examined. No in-depth analyses have been made of the individual agreements to analyse the potential impact on the market structures of individual markets. In order to shed light on the impact on individual markets, the DCCA has obtained revenue data from Statistics Denmark for the suppliers under the central framework agreements established by the SKI and the Central Procurement Programme. Furthermore, the study indicates that, in most cases, there was a basis for effective competition for contracts under the central framework agreements analysed. However, the study shows that competition for some agreements may have been weakened. The DCCA believes that the framework agreements would contribute to supporting well-functioning markets to a much higher extent if competition for contracts under the framework agreements became more effective, e.g. by providing a greater certainty of revenue.

The questionnaire survey conducted by the DCCA also shows that purchasers find that the central framework agreements established by the SKI, the Central Procurement Programme and the inter-municipal joint purchasing bodies often make it easy to purchase products that meet end user demands at a low price. More than half of the purchasers of the survey have

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experienced that procurement through framework agreements *either* ensures a low price (60 per cent), a less resource-intensive procurement process (60 per cent) *or* a good match of supply and end user demands (50 per cent). One of every four purchasers experience a low price, a less resource-intensive procurement process, and a good match of supply and end user demands when making purchases under central framework agreements. By contrast, a minor part of purchasers experience that the procurement under framework agreements does not result in a low price (6 per cent), a less resource-intensive procurement process (13 per cent) or a good match of supply and end user demands (8 per cent).

#### Box 1.1

#### Overall main conclusions and focus points

##### **Overall main conclusions of the study:**

- » There is no direct indication that central framework agreements will have an impact on market structures in the long term when analysed across the agreements examined.
- » No in-depth analyses have been made of the individual agreements to analyse the potential impact on the market structures of individual markets. Based on revenue data from Statistics Denmark on the suppliers under the 49 central framework agreements established by the SKI and the Central Procurement Programme there seems to be no direct indication that central framework agreements will have an impact on market structures in the long term for the vast majority of agreements analysed.
- » Data on the number of tenders received and the number of contracts awarded indicate that, in most cases, there was a basis for effective competition to be awarded a contract under a central framework agreement. However, the study shows that competition for some agreements may have been weakened. In 16 per cent of the 162 analysed agreements, all tenderers were eventually awarded contracts.
- » The ability to (also) sell products outside the framework agreement to customers under the framework agreement was important to almost 40 per cent of the enterprises which tendered for a contract under a framework agreement.
- » In the experience of the enterprises, certainty of revenue from the agreements seems to be essential for competition and price.
- » The standardisation of the framework agreements may pose challenges for effective public procurement where end users have different demands.
- » In the experience of the purchasers, central framework agreements often contribute to effective public procurement, i.e. they can easily purchase products that meet end user demands at a low price
- » In the experience of the enterprises, central framework agreements contribute to some degree to effective public procurement, but not in every case.
- » The purchasers find that mini-competitions do not ensure a good match of supply and demand. In the opinion of the suppliers, customers rarely pay a lower price at the time of purchase than the market price where contracts are awarded following a mini-competition instead of on a direct award basis.

##### **Focus points**

To increase the probability that central framework agreements contribute to effective public procurement and support well-functioning markets, the DCCA recommends that decision makers and contracting authorities should in future (continue to) have focus on the following points:

- 1) Ensure that suppliers will generate a certain revenue from the contract under the agreement.
- 2) Create standardisation at the level which creates volume-based economies of scale and makes it attractive to tender for a contract and at the same time with an assortment width and volume which do not prevent enterprises from submitting tenders (on their own). This may lead to the use of lots. And make standardisation across a group of end users with uniform demands, e.g. a sector-specific or an institution-specific group of end users.
- 3) Use mini-competitions with prudence and make it easier for purchasers to purchase through mini-competitions.

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The overall main conclusions of the study and focus points are set out in detail below. Box 1.2 gives a short introduction to framework agreements.

Box 1.2  
**About framework agreements**

The public sector may organise its procurement activities in different ways. The Productivity Commission and the Council on Public-Private Collaboration (*Rådet for Offentligt-Privat Samarbejde*) recommend that public authorities "... take a strategic approach to identifying where procurement and tendering processes are conducted most effectively, including whether they should be conducted locally, in cooperation with other public authorities or through centralised agreements.

One way of purchasing is through framework agreements. The Public Procurement Directive defines a framework agreement as an agreement between one or more contracting authorities and one or more economic operators (suppliers). The purpose of a framework agreement is to establish the terms governing the contracts to be awarded on the basis of the framework agreement during a given period, in particular prices and the quantity of goods or services to be procured.

When a public authority uses a framework agreement for which tenders have been properly invited in compliance with the Public Procurement Directive, the public authority may place orders with a supplier under the framework agreement without conducting a new EU tender.

Framework agreements comprise agreements entered into by one public authority with one or more suppliers as well as agreements entered into by a central or joint purchasing body on behalf of several public authorities with several suppliers.

As a general rule, a framework agreement does not entail an obligation for the public authority to actually make use of the framework agreement. However, the users of framework agreements may commit themselves to using a framework agreement. During the entire contract period, the supplier is obliged to meet any orders placed by the contracting authority on the terms set out in the agreement.

It may be useful for public authorities to use framework agreements if it is uncertain how large a quantity of a given product or a given service the authority will require and when the authority's need for supplies will arise. For instance, many public authorities use framework agreements for purchases of photocopy paper because the authority does not know in advance how much photocopy paper it will need to purchase over a period of several months or years. The Productivity Commission recommends that central framework agreements should be used where it is possible to standardise goods and services or to standardise the procurement processes.

*Source: The Danish Public Procurement Council (Udbudsrådet), Analysis of best practice in the use of framework agreements, 2011. The Danish Productivity Commission, Public-Private Collaboration, Analysis Report 6, 2014*

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