



Public Procurement in 2013-2014: How Taxpayers' Money Got Spent



Public Procurement in 2013-2014:

How Taxpayers' Money Got Spent

July 2015
Tbilisi

Research Supervisor: Levan Natroshvili

Authors: Ana Dabrundashvili, Mikheil Kukava, Giorgi Nasrashvili

Transparency International Georgia

Address: Rustaveli Avenue, 26, Tbilisi 0108

Telephone: (+995 32) 292 14 03

Email: info@transparency.ge

Web site: <http://transparency.ge>



SWEDEN

This report was prepared by Transparency International Georgia under the auspices of the *Business of Government* project funded by the Swedish International Development Cooperation Agency (Sida).

CONTENTS

I. Executive summary.....	4
II. Introduction	7
III. Analysis of the legal framework.....	9
Problem #1: Simplified procurements	9
Problem #2: Misapplication of different forms of public procurement	10
Problem #3: Submission of qualification documents.....	11
Problem #4: Price as the main selection criteria	11
Problem #5: The risk of artificially dividing tenders	12
Problem #6: Changing the conditions of a contract.....	12
Problem #7: The independence of the Public Procurement Appeals Board	13
Problem #8: Access to the public procurement market	13
IV. Simplified Public Procurements	14
1. The largest categories of procurement.....	15
2. The largest procurer organizations	16
2.1 Central government.....	16
2.2. Local government.....	18
3. The largest suppliers	19
3.1. LEPLs in simplified procurements.....	19
3.2. State-owned enterprises in simplified procurements.....	19
3.3. Private companies in simplified procurements	20
3.4. Unfulfilled contracts.....	20
3.5. Public procurements made with the permission of the Government/President.....	20
3.6. Participation of companies of public officials in simplified procurements	22
3.7. Political party donors in simplified procurements.....	24
V. Electronic Tenders	25
1. The largest procurer organizations	25
2. The largest suppliers	26
3. Amendments to contracts	26
3.1. Contracts worth more than a half a million lari to which more than 20 changes were made	27
4. Foreign companies in tenders.....	27
5. Risky procurements.....	28
6. Companies connected to public officials in electronic tenders.....	28
VI. Conclusion and Recommendations.....	31

I. EXECUTIVE SUMMARY

In this report Transparency International (TI) Georgia presents trends and problems related to public procurement in 2013 and 2014 as well as solutions to these problems.

The radical public procurement reforms in the last five years have made the Georgian system one of the most transparent in the world. TI Georgia and a number of international organizations have praised the system, including the World Bank, The United Nations and The European Bank for Reconstruction and Development. Nonetheless, a public procurement system's openness and transparency does not always mean that the system will successfully save resources or ensure an appropriate level of competition.

We believe that the main gaps in the Georgian public procurement legislation are related to the **insufficient regulation of different types of procedures related to procurement**. These problems create a serious risk of corruption. As a rule, detailed regulation minimizes the risk of corruption stemming from, for example, abuse of loopholes in the law by officials. Although insufficient regulation is generally a problem at the level of secondary rather than primary legislation, we have noted a number of gaps in both primary and secondary public procurement legislation.

SIMPLIFIED PROCUREMENT

Simplified procedure can be used for the procurement of goods, services or construction works valued at up to GEL 5 000 or when an entity has the exclusive right to supply the good, service, or construction works and there is not another qualified, alternative supplier. The main concern about simplified procurements is that the law contains a number of exceptions to the above rule, which allow simplified procurement to be used in other circumstances, as discussed below. The following findings are notable in regards to simplified procurement:

- According to the State Procurement Agency's 2014 report, GEL 915.7 million in contracts were awarded using simplified procurements, which is 32% of total procurements. We welcome that the share of simplified procurements as a share of total procurements decreased compared with 2012 (45%) and 2013 (39%). Even so, the share of simplified procurements as a share of total procurements should decrease to a greater extent;
- In 2013-2014, construction works worth GEL 604.5 million were procured through a simplified procedure. Construction works have made up the largest share of simplified procurements in recent years, and their share should clearly decrease. There are a fairly large number of companies in the construction sector in Georgia, and it is unlikely that only a few companies have the specific skills and competences needed for a given project. Hence, it would be difficult for the procuring agency to argue for the use of a simplified procedure on the basis of no alternative supplier being present. Moreover, construction works require an extended period of time, and hence the motivation to save time by using a simplified procurement instead of a competitive tender strains credulity. If the share of competitive tenders in this sector increases, given the high level of competition, the government will be able to direct savings towards more projects;
- In 2013-2014, state owned enterprises and legal entities of public law made the largest procurements. The largest procurer was Gardabani Power plant Ltd. Over the course of two years,

it awarded more than GEL 275 million in simplified procurements. This money was spent almost entirely on one procurement – the construction of Gardabani combined cycle power plant;

- Between 2013 and 2014, legal entities of public law and state owned enterprises were among the largest suppliers. In total, 15% of their income came from simplified procurement;
- Information on simplified procurements issued by the Ministry of Internal Affairs and its agencies is not accessible in the electronic system (CMR). Information on the simplified procurements of the Ministry of Defense and its agencies is also not accessible through the system;
- Over the course of two years, state owned enterprises took in GEL 188.6 million from simplified procurements, with GEL 112.7 million in 2013 and the remainder in 2014. Awarding state-owned companies contracts may hinder competition. It is unclear on what grounds state owned enterprises were awarded the contracts;
- In 2013, approximately 66% of simplified procurements were carried out with the government's or the president's approval. In 2014, approximately 58% of the simplified procurements were carried out with the government's approval (After the 2013 constitutional changes the president was stripped of this right). With the government's approval, a number of procurements were carried out that would have benefited from a competitive tender process, particularly in the construction sector. If a public procurement is necessitated by a truly urgent need (i.e. in instances of natural disasters), then it should be indicated in the *basis of procurement* entry in the procurement system. However, it is apparent that frequently no such need was present in the government approved simplified procurements. As a result, there was not a healthy degree of competition, and hence the state was unable to save public money;
- In 2013-2014, a number of companies connected to officials received a fairly large amount of income from simplified procurement. Notably, companies connected to the majoritarian Member of Parliament representing Khashuri **Valeri Gelashvili** and Kharagauli Municipality *Sakrebulo* Chairman **Akaki Machavariani** received contracts through simplified procurement from agencies which they are directly connected to;
- Companies directly connected to Georgian Dream donors (directors, owners, board members) received GEL 5.6 million in contracts in 2013 and 2014. In the same period, United National Movement donor connected companies received contracts worth approximately GEL 140 000. It should be noted, that the problem was much more severe in 2011-2012. In 2012, the United National movement received GEL 6.6 million in donations from persons connected to companies which received GEL 160 million in contracts. The same companies received GEL 110 million through simplified procurements in 2011.

ELECTRONIC TENDERS

According to Georgian legislation, electronic tenders are used if the value of the procurement is GEL 200 000 or more, while simplified electronic tenders are announced for procurements that are valued at less than GEL 200 000. Regarding electronic tenders, the following findings are notable in 2013-2014:

- In 2013-2014, GEL 3.132 billion was spent on tenders. Of this, GEL 1.428 billion was procured in 2013 and GEL 1.704 billion in 2014. Electronic and simplified electronic tenders made up approximately 60% of total public procurement spending in 2014 and 51% in 2013.
- In 2013-2014, 42 404 contracts were reached through tenders. Of these, 33 984 contracts (80%) were not amended after being signed, 5 753 (13.5%) were amended once, and 1 604 had two amendments. The remaining 1 063 contracts (2.8%) had three or more amendments;

- Of the 42 404 contracts reached through tender, there was a single competitor on 5 644 (13.3%) contracts. After changes were made to 44 of the contracts awarded through electronic tender (0.1%), the final value of the contract was higher than the prices offered by the losing bidders;
- In 2013-2014, some of the companies that won tenders were connected to public officials, as noted in their asset declarations. Among these officials are **Davit Galegashvili** – Deputy Minister of Agriculture; **Nugzar Surmanidze** Minister of Health and Social Affairs of the Autonomous Republic of Adjara; **Giorgi Topadze** – Member of Parliament; Gocha Enukidze – Member of Parliament; **Jemal Putkaradze** – Member of the Supreme Council of Ajara; **Giorgi Zedelashvili** – Former Deputy Minister of Internal Affairs.

II. INTRODUCTION

Approximately 29% (GEL 2.847 billion) of the 2014 consolidated budget¹ was spent on public procurements, which is approximately 10% of Gross Domestic Product (GDP)².

According to Georgian legislation, there are three main types of public procurement: 1) electronic tender, which is used if the value of the procurement is GEL 200 000 or more; 2) simplified electronic tender if the value of the procurement is less than GEL 200 000; 3) simplified procurement which is for a procurement valued at up to GEL 5 000, or when an entity has the exclusive right to supply the good, service, or construction works and there is not another qualified, alternative supplier. In this situation, a procurement contract can be reached with any preferred supplier. This report deals with these three main forms of public procurement, their implementation, and related problems.

Since the radical reforms of 2009 to the Georgian public procurement system, Georgia has had one of the most transparent procurement systems in the world. Transparency International Georgia³ and a number of international organizations have praised the system (e.g. the World Bank⁴, The United Nations⁵, The European Bank for Reconstruction and Development⁶). Even so, a public procurement system's openness and transparency does not always mean that it will ensure resource savings or an appropriate level of competition.

As per the State Procurement Agency's 2014 report,⁷ 32% (GEL 915.7 million) of procurements were carried out via simplified procurement in 2014. This is quite a large share of total procurements. The State Audit Office's 2014 report⁸ also questions the effectiveness of public procurement. The report notes that a number of instances were uncovered where simplified procurement was used based on the justification that it was necessary to urgently procure the items, even though the urgency of the procurement was unsubstantiated. There was a large number of contracts awarded without competition (tender). In total, between 2011 and 2012, more than GEL 2 billion of goods, services, and construction works were procured using simplified procurement, which represents approximately 40% of public procurement during that period.

Despite the transparency of the public procurement system, there remain a number of closely interrelated problems with procurements viz., the system does not help save public monies; provide access to the system for all potential suppliers; or provide equal access to the public procurement market for all bona fide suppliers. As a result, the system does not ensure an appropriate level of competition, a non-discriminatory approach to procurement, or an effective spending of public monies.⁹ Today, these are the most significant problems in the public procurement system. We think there are two significant reasons for these problems, viz., loopholes in the procurement legislation and Georgia's non-use of corresponding

¹The consolidated budget is the state budget and local government budgets combined.

²GDP in 2014 was GEL 29.2 billion.

³Transparency International Georgia, June, 2013. Georgia's E-procurement platform is one of the most transparent in the world but because of loopholes, too many contracts bypass the system: <http://transparency.ge/en/post/report/georgia-s-e-procurement>

⁴World Bank, February 18, 2015. *Georgia: An E-Procurement Success*: <http://goo.gl/9JkRHZ>

⁵United Nations, 2012. *Public Service Awards Winner* <http://goo.gl/MXrFQb>

⁶European Bank for Reconstruction and Development (EBRD). *On the Way to WTO GPA Accession: Georgia*:

⁷State Procurement Agency, 2015, *2014 Activities Report*. <http://goo.gl/yNytCm>

⁸State Audit Office, March 18, 2014. *Ensuring the effectiveness of the state procurement system*: <http://goo.gl/LNpZFY>

⁹Among them, performing value for money analysis.

international formats (Government Procurement Agreement).¹⁰ These problems, in practice, create a serious risk of corruption (For more about the International Government Procurement Agreement, see Ch. 3, Problem 8).

In December 2013, Transparency International Georgia published a report,¹¹ which presented an analysis of contracts reached through simplified procurement between 2010 and 2013.

The present report highlights trends in public procurement between 2013 and 2014 in connection to the above noted problems. It also presents solutions to the noted problems. The first part of the report presents an analysis of Georgia's legislative framework for procurement – both strengths and weaknesses – as well as recommendations on how to close the existing legislative loopholes. The subsequent chapters discuss research findings and what appear to be cases of corruption involving simplified procurement and electronic tenders. At the end of the report, the main findings are summarized and recommendations are presented on how to close gaps in legislation and to solve current problems related to implementation.

For the research, we looked at the experience of four European countries (Slovenia, the Czech Republic, Slovakia, and Poland). In the report, using these experiences, we examine Georgian public procurement practice against European practice.

¹⁰ World Trade Organization. *Agreement on Public Procurement*: https://www.wto.org/english/tratop_e/gproc_e/memobs_e.htm

¹¹ Transparency International Georgia. December 6, 2013. Simplified procurement: Corruption risks in non-competitive contracts. <http://transparency.ge/simplified-procurement>

III. LEGAL FRAMEWORK ANALYSIS

In this chapter, we analyze the gaps in legislation, which create problems leading to the decreased efficiency and effectiveness of public procurement, decreased predictability of budget spending, and an increase in the risk of corruption.

The main gap in legislation **is the inadequate regulation of procedures for different forms of public procurement, which creates a serious risk of corruption.** Typically, detailed regulation decreases risks such as officials bypassing the law through abuse of office. Inadequate regulation is mainly a problem with secondary¹² rather than primary legislation. Nonetheless there are a number of problems in public procurement law, which we discuss in detail below.

As is well known, in administrative relations only what is regulated is allowed, whereas in civil relations what is not prohibited is allowed. Consequently, it is very important both in secondary and primary legislation that all forms of and procedures related to public procurement are comprehensively regulated.

PROBLEM #1: SIMPLIFIED PROCUREMENTS

Simplified procurement can be used to purchase goods, services or construction works valued at up to GEL 5 000 or when an entity has the exclusive right¹³ to supply the good, service, or construction works and there is not another qualified alternative supplier. The main problem with simplified procurements **is that a number of exceptions in the law allow for the use of simplified procurement in other circumstances.** Simplified procurement is allowed in cases of:

- Urgent need – the length of service provision should not exceed the timeframe needed to solve the urgent problem;
- A procuring entity can decide to procure an item from a supplier to avoid worsening the quality of an object and/or if it is necessary to ensure the procured item is fully used, or if it is necessary that the procurement be carried out with the same contractor as part of a sub-contract, except in cases in which the estimated price of the object to be procured is greater than the original object procured;
- When it is in the state's and the public's interest to take action in a short timeframe instead of conducting a public procurement, the Government of Georgia, an Autonomous Republic or the Board of the National Bank may use simplified procurement. It can be carried out using the budget of an autonomous republic and/or self-governing entities within the borders of an autonomous republic. It can also be carried out with the funds of organizations funded by autonomous republic budgets and other entities funded by the government;
- Other situations¹⁴

¹² Acts of the Chairman of the State Procurement Agency.

¹³ Exclusive right does not apply in situations when a) the estimated value of the good, service, or construction works is over GEL 2 000 000, and outside the country within reasonable territorial boundaries, there are entities which could implement the services; b) The estimated price of goods, service, or construction works does not exceed GEL 2 000 000 and within the country there are entities which can implement the services.

¹⁴

- For public procurement related expenses;
- When purchasing or replacing one or more automobiles, computer equipment, or electronics of the same or better quality, new automobiles, computer equipment, and/or electric appliances, they should be partially paid for using the old automobile, computer equipment, and/or electronic appliance by returning it to the supplier or another physical or legal entity which sells such products as detailed in the law;
- To procure services as detailed in the law;

These exceptions, in practice, enable budget spending entities to bypass the transparent electronic tender process for the purchase of any form of good, service, or construction work.¹⁵

Because state entities award contracts directly to a company when using a simplified procurement, the risk of corruption is significantly higher. It is possible to reach contracts with persons close to office holders or a company which is either loyal to or dependent on the government. Through simplified procurement, the state cannot save money as can be achieved through tenders.

Simplified procurement is used in many countries, although the main difference between the Georgian practice, as detailed in the legislation, and European practice (in Slovenia, the Czech Republic, Slovakia, and Poland) is that simplified procurement is only allowed in *force majeure* situations or in case of emergency. Changes¹⁶ to the regulations for simplified procurements, simplified electronic tenders and electronic tenders which prohibit increasing the volume procured in an emergency in order to solve a problem in a given time frame are absolutely inadequate to solve the problem. This change will lead to procuring organizations delaying purchases in order to artificially create the need to carry out a simplified procurement on the basis of urgent need.

Recommendations:

In order to reduce the risks associated with simplified procurement, we think that the government should introduce two key terms into state procurement legislation: 1. *force majeure situation*; and 2. *urgent need*, which will include every situation, when shortened time frames for procurement will be allowed on the basis of European practices:

- **Urgent need** should be interpreted as a situation in which it is not possible to foresee the need, and/or the reason for the procurement was not caused by the procuring organization's actions, or which, by not procuring, would significantly harm the public's or the state's interests or property;
- **Force majeure situations** should include wars or national emergencies, strikes, sabotage, industrial unrest, civil unrest, blockade, insurrection, ecological catastrophe, natural disasters, epidemics, dangerous situations related to disease among the animal population, or other *force majeure* situations in which by not procuring an item, human life, health, public welfare, or state security will be endangered.

PROBLEM #2: MISAPPLICATION OF DIFFERENT FORMS OF PUBLIC PROCUREMENT

According to Georgian legislation, simplified electronic tender is used if the value of the tender is less than GEL 200 000, while electronic tender is used for the procurements over GEL 200 000.

-
- To carry out annual and/or maintenance works on vehicles under warranty and/or servicing of spare parts and/or the purchase of lubricants;
 - Legal Entities of Public Law – higher education institutions purchasing literature (printed, electronic, or audiovisual media), reagents, computer programs, pharmaceutical products (health products), laboratory equipment and data sets;
 - A state established higher education institution non-commercial legal entity – Higher education entities and the higher education development fund can make purchases with the permission of the Board of Regents. In such cases, the Board of Regents will grant well founded requests.

¹⁵ Transparency International Georgia. 6 December, 2013. Simplified procurement: Corruption risks in non-competitive contracts.

<http://transparency.ge/simplified-procurement>

¹⁶ Order №9 of the State Procurement Agency Chairman, 7 April, 2011, Article 3, Point 1, Sub-point B (Changed on 23 January, 2015)

The procurement law recognizes a specific case in which simplified electronic tender can be announced, including when it is in the state and/or public interest to carry out the procurement within a short period of time. A legal act of the Georgian President and/or Georgian Government may allow the use of simplified electronic tender when within a single budget year, the same type of items worth GEL 200 000 or more are to be procured.¹⁷

The EU legislation studied does not allow the use of two essentially different means of procurement in such situations, which is not only a problem with the legal technique, but rather blurs the boundaries between two different kinds of procurement – simplified electronic tender and electronic tender.

Recommendations:

- Simplified electronic tenders valued at GEL 200 000 or more should not be used in instances where it is in the public or state interests to carry out the procurement in a shorter timeframe, but rather should only be used in instances of urgent need or *force majeure* situations, as defined in this section.

PROBLEM #3: SUBMISSION OF QUALIFICATION DOCUMENTS

For bidders on electronic tenders, it is usually required to submit qualification documents,¹⁸ although for specific procurements, the bidder can be allowed not to submit qualification documents. For simplified procurements, however, qualification documents are required only in certain situations. If a bidder is required to provide qualification documents, the procuring entity must substantiate the necessity in tender documentation. The fact that bidders do not need to submit qualification documents represents a clear risk of corruption.

Recommendations:

- As with electronic tenders, simplified electronic tenders should require bidders to present qualification documents (the organization's registration number, legal restrictions, and existing financial and other commitments). Demanding qualification documents from a supplier does not represent an extra barrier, but rather it is an additional guarantee for the procuring entity that the supplier is qualified to implement the given work.

PROBLEM #4: PRICE AS THE MAIN SELECTION CRITERIA

In the EU countries we studied, price is not the only legislative criteria for selection, because such an approach can seriously damage the quality of the procured goods, services, or construction works.

Even though the rules for simplified procurement, simplified electronic tender, and electronic tender were amended on 6 April, 2015,¹⁹ price remains the main selection criteria in Georgia. According to the amendments, upon a procuring entity's request, a bidder is required to substantiate the adequacy of the price given in the tender if it is 20% or more below the procuring entity's estimated price. At present, bidders have the right to lower the price of their proposal in order to win the contract, within a given timeframe.²⁰

¹⁷ Georgian Law on State Procurement, Article 10, Point 3

¹⁸ Qualification documents include registration data, legal restrictions, financial and other commitments, according to the Georgian Law on State Procurement, Article 10, Point 3

¹⁹ Order №9 of the State Procurement Agency Chairman, 7 April, 2011.

²⁰ State Procurement Law, Article 3, Point 1, sub-point T

Recommendations:

- Bidders should keep the right to lower the price of their proposal in order to win a tender, although it is important that the final price and the difference between the estimated value of the procurement and the final price be substantiated. Structured substantiation requires the creation of a questionnaire in which procuring entities ask suppliers specific questions, when the proposed price is lower than the estimated value of the item to be procured by 20% or more. When the substantiation is not structured, the supplier will be unable to respond to the questions, which are essential for the procuring agency to know the answers to in order to guarantee that the bidder will be able to provide the good, service, or construction works of the same quality at a lower price.

PROBLEM #5: THE RISK OF ARTIFICIALLY DIVIDING TENDERS

According to the public procurement law, a procuring entity is prohibited from artificially dividing tenders to avoid monetary thresholds or other related requirements with the goal of evading regulation (monetary thresholds are defined in the public procurement law).²¹ As per the law, artificial division of a procurement means decreasing or dividing the amount or quantity of a single object, when the procuring organization knows in advance that during the same budget year it will be necessary to make another procurement of the same object.

Recommendations:

- It is important that the methodology for preventing the artificial division of tenders be developed in consultation with experts and civil society organizations.

PROBLEM #6: CHANGING THE CONDITIONS OF A CONTRACT

According to public procurement legislation, it is impermissible to change the conditions given by the supplier on the agreement, if as a result of those changes, the price of the procurement increases or the conditions of the agreement worsen, except in situations which are set out in Article 398 of the Civil Code.

Article 398 of the Civil Code 1. deals with conditions on the basis of which the contract was awarded, which have clearly changed after the contract has been awarded and how the parties would have acted had they known what they knew after they reached the agreement, 2. notes that changes to circumstances are tantamount to a situation when the performance on which the award was made was found to be misrepresented 3. notes that the sides must first attempt to adjust to the changed circumstances. If it is impossible to adjust the agreement to the changed circumstances, or the second party does not agree to it, then the side whose interests are violated can withdraw from the agreement.

A first step towards improving legislation related to changing the conditions of agreements came on April 29, 2015 in the rules²² for carrying out a simplified procurement, simplified electronic tender, and electronic tender. Changes are now allowed due to problems created by changes in the price of the

²¹ According to Georgia's Law on Procurement, Article 3, division of state procurement means decreasing or dividing the amount or quantity of a single object or through another action, when the procuring organization knows in advance that during the same budget year it will be necessary to make another procurement of the same object, with the goal of avoiding a monetary threshold as prescribed by law .

²² Order №9 of the Chairman of the State Procurement Agency, dated 9 April, 2011

national currency, and/or as a result of recent events in the region which resulted in increased costs for the supplier. Due to these circumstances it is possible that the value of the contract increases if 1. the price of the contract increases by up to 10% of the original value, and it causes the total price of the contract to increase by more than GEL 100 000; 2. the total value of the contract increases by more than 10%. No comparable regulation was in force in 2013-2014.

Recommendations:

- It is necessary that the public procurement law or the State Procurement Agency Chairman's order specify what worsening the conditions of the contract means, including when conditions require releasing the supplier fully or partially from responsibility for incomplete fulfillment of obligations, and specifically when obligations are not met due to unforeseen factors, such as the devaluation of the national currency or other situations which create a number of problems for suppliers. Apart from this, procurement law should define the misrepresentation on the basis of which a contract was awarded.

PROBLEM #7: THE INDEPENDENCE OF THE PUBLIC PROCUREMENT APPEALS BOARD

The Public Procurement Appeals Board should settle appeals quickly and justly, respecting the equality of the parties. Clear conflicts of interest are the largest problem connected to the Public Procurement Appeals Board. These conflicts have been present from the Board's establishment. Specifically, the Public Procurement Appeals Board is chaired by the Chairman of the State Procurement Agency. Of the six board members, the chairman nominates two board members annually. Even though there are three representatives of non-governmental organizations on the board, the fact that the chairman nominates two board members yearly poses a risk to the Board's independence. Hence, the Appeals Board cannot be considered an independent entity at the moment.

Recommendations:

- The Public Procurement Appeals Board should be established as a completely independent entity. The Chairman of the Appeals Board should no longer be the Chairman of the State Procurement Agency, nor should the chairman nominate members. The Board of Appeals should be established as an independent entity, which means that the Board should have its own staff who do not work for the Public Procurement Agency.

PROBLEM #8: ACCESS TO THE PUBLIC PROCUREMENT MARKET

Despite the transparency of public procurement system, there remain a number of closely interrelated problems with public procurement, viz, the system does not help save public money, provide access to the country's public procurement market to all potential suppliers as well as to all bona fide suppliers. As a result, the system does not ensure an appropriate level of competition, a non-discriminatory approach to procurement, or an effective spending of public money.²³ Solving these problems will allow the government to save resources.

To achieve the effective spending of public resources, the procuring organization should consider options which they are not at present. For example, instead of constructing a building, would it be better to lease one?

²³ Among them, performing value for money analysis.

The efficacy of state spending, including the saving of public money, should be fundamental to all public procurement systems. In order to accomplish this, it is necessary for all potential suppliers to have access to the system. According to the 2014 State Procurement Agency's report, 58 contracts, valued GEL 82 254 335,²⁴ were awarded to non-resident suppliers in 2014. While this is about 5.2 times the level of 2013, it is still below 5% of the total value of all tenders awarded.

Recommendations:

- To solve these as well as similar problems, Georgia needs to accede to the Government Procurement Agreement, which the country has been an observer to since 1999. Although the legislation in force is neither discriminatory towards foreign suppliers nor protectionist towards local suppliers, the public procurement market has still not been liberalized. The procurement market can only be liberalized through changes to Georgian legislation;
- As the conclusion of the State Audit Office's 2014 report²⁵ has it, **unified procurement should be used more actively in instances where centralization is expedient**. Public procurement is still carried out in a decentralized manner, which in turn prevents the state from saving public money;
- The State Audit Office's recommendation that a supplier assessment system should be developed should be implemented in a timely manner. This will ease procurement planning as well as the process of selecting suppliers. Suppliers could be rated by a "star" system based on objective criteria.

IV. SIMPLIFIED PUBLIC PROCUREMENTS

Simplified procurement is a form of public procurement which public institutions resort to in the case of procurement with a value below GEL 5,000 or when the provision of construction works is the exclusive right of a single economic agent. Other exceptions in which simplified procurement is used are determined in the Law of Georgia on Public Procurement. In the case of simplified procurement, the procurer concludes a contract with any desirable supplier.

In this chapter, we will discuss and analyze the noteworthy trends that were revealed in the simplified procurements made from January 1, 2013, up to December 31, 2014.²⁶

According to the 2014 report on the activities of the State Procurement Agency, the volume of simplified procurements in 2014 amounted to GEL 915.7 million, which constitutes 32% of the total procurements. It is a welcome fact that the share of simplified procurements within the total procurements has been decreasing in the recent years; in 2013, the share was 39%, while in 2012 it was 45%.

Simplified public procurement involves a high risk of wasteful spending, making it impossible to decrease the price. This would be ensured by the participation of a competing company in a tender. At the same time, concluding contracts bypassing the transparent Electronic Procurement System increases the risks of corruption because it permits settling of contracts with companies aligned with the authorities.

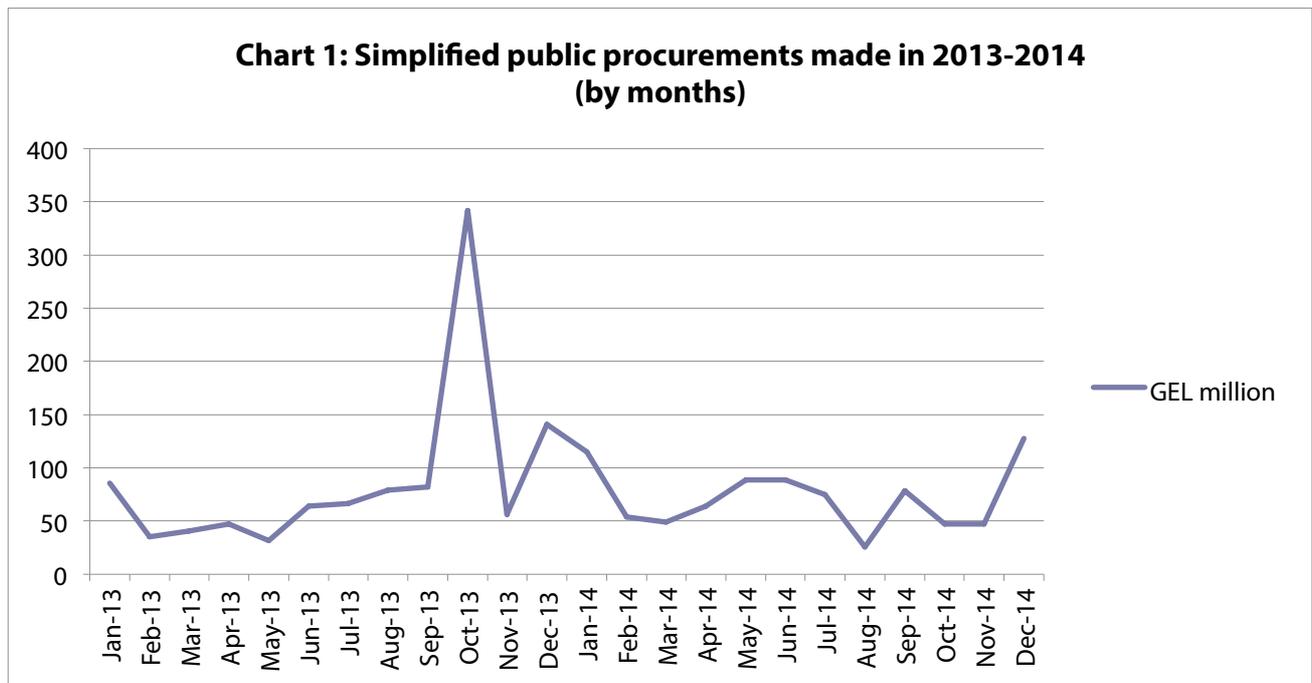
Of the sums spent on simplified procurements in 2013-14, almost GEL 1 billion was spent from the state budget, and GEL 648.6 million came from the revenues of various agencies and state-owned enterprises; GEL 174.8 million was spent from the local self-government budgets, and GEL 28.2 million was spent from the budgets of autonomous republics. The remaining sums were spent from grants and credits.

²⁴ State Procurement Agency, 2015, *2014 Activities Report*. <http://goo.gl/yNytCm>

²⁵ State Audit Office, March 18, 2014. *Ensuring the effectiveness of the public procurement system*: <http://goo.gl/LNpZFY>

²⁶ The report includes the simplified procurement contracts that entered into force in the period between January 1, 2013, and December 31, 2014.

Simplified procurements are distributed evenly over the year, although expenditures increase in December in comparison with other months. This trend may be caused by agencies' desire to fully spend their budgets at the end of the year. During the years 2013-14, the only exception was October 2013, the month of the presidential elections, when simplified procurements reached a record level (GEL 341.8 million). In general, monthly expenditures in other months did not exceed GEL 150 million. No similar trend of growth was observed at the time of the local self-government elections in 2014, which is a welcome fact.



1. THE LARGEST CATEGORIES OF PROCUREMENT

In 2013-14, **construction works** of GEL 604.5 million were carried out through simplified procurements; of these, more than two-thirds of the public procurement (GEL 435.9 million) were made in 2013, while the remaining procurements were made in 2014. The category of construction works also ranked first in terms of spending in the previous years.

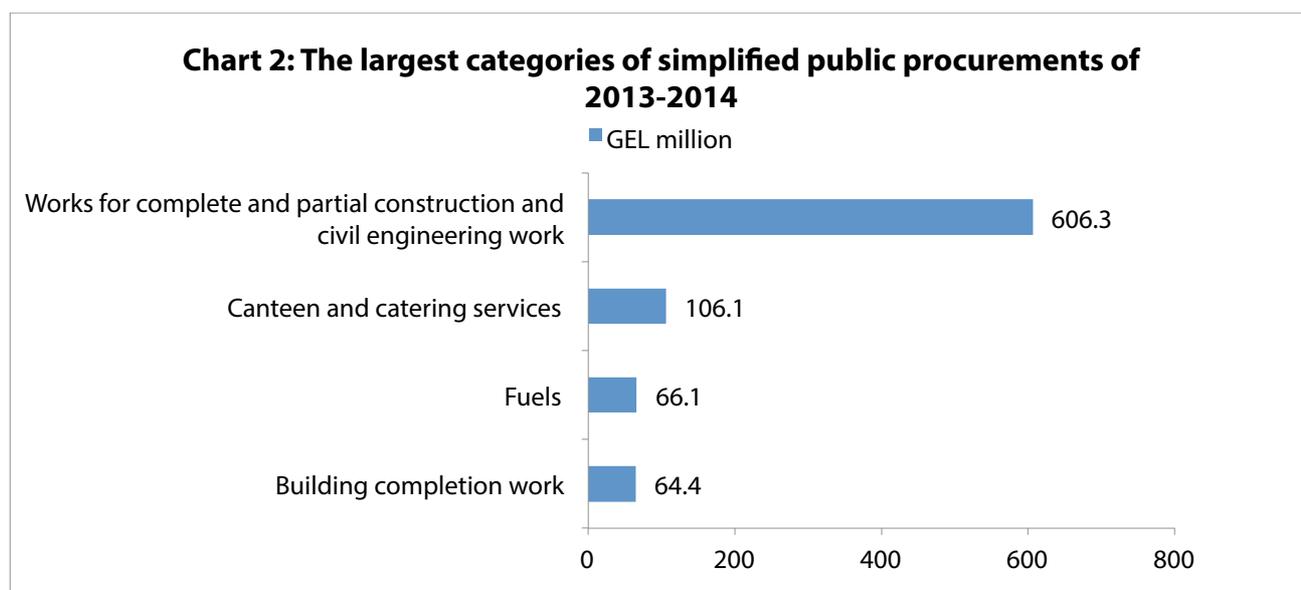
Recommendation:

- Construction works belong to the very categories where the **share of simplified procurements should decrease**, because:
 - There are an abundance of of companies operating in this sector in Georgia and, under high competition, the State will be able to save more funds when carrying out expensive projects if the share of competitive tenders increases further;
 - Construction works are always long term ventures and it is ineffective to avoid a competitive tender for the purpose of saving time.

According to the combined data of the two years, the category of construction works is followed by **healthcare services** (GEL 173.7 million) and **canteen and catering services** (GEL 106.1 million). As for the

other large categories, a total of GEL 38.5 million was spent on **administrative services**, and GEL 38.3 million and GEL 35.5 million was spent on **services related to motor vehicles** and **motor vehicles**, respectively.

The largest categories of 2013 and 2014 differ slightly. In 2014, spending on healthcare services increased by GEL 40 million. Expenditures on computer equipment and accessories were also significantly higher. In 2013, relatively large procurements (GEL 79.9 million) were made in the category of catering services in comparison with 2014.



2. THE LARGEST PROCURER ORGANIZATIONS

2.1 Central government

In 2013-14, state-owned companies and legal entities of public law are predominant among the largest procurers. The largest procurer is Gardabani Powerplant LLC, which made simplified procurements of more than GEL 275 million during the two years. This sum was almost entirely spent on only one procurement – the construction of the combined cycle power plant in Gardabani.

Other large procurers include:

- The Ministry of Defense of Georgia (GEL 149.3 million);
- The Social Service Agency (GEL 148.4 million);
- JSC Georgian State Electrosystem (GEL 57.7 million);
- The Educational and Scientific Infrastructure Development Agency (GEL 56.5 million).

Table 1. The largest simplified public procurements made in the years 2013-2014 (over GEL 15 million)

Registration number	Procurer	Supplier	Value (GEL)	Object or category of procurement	Date
CMR130327893	Gardabani Powerplant LLC	ÇALIK ENERJİ SANAYİ VE	271,757,721	Construction of Gardabani Combined	31/10/2013

Public Procurement in 2013-2014:
How Taxpayers' Money Got Spent

		TİCARET A.Ş		Cycle Power Plant	
CMR130359846	Ministry of Defense of Georgia	Georgian Food Company	24,844,440	Canteen and catering services	31/12//2013
CMR140117854	Ministry of Defense of Georgia	Georgian Food Company	18,150,000	Canteen and catering services	30/06/2014
CMR140017486	Social Service Agency	LEPL Emergency Medical Service Center	16,401,000	Emergency medical services for public healthcare program	22/01/2014 (This contract was terminated on August 5, 2014)
CMR140083893	Tetnuldi Development LLC	State Construction Company	15,500,000	Works of development of ski trails and mountain infrastructure of Tetnuldi	22/04/2014

Simplified procurements made by the Ministry of Internal Affairs and its agencies are not accessible for users of the Electronic Procurement System (CMR module). Simplified procurements by the Ministry of Defense and its agencies were also inaccessible in the system, though during the several months while we were working on the report some procurements appeared on the website. We asked the Ministries of Internal Affairs and of Defense, as well as the State Procurement Agency why it was not possible to find the procurements of these agencies. The Ministry of Internal Affairs failed to respond to the freedom of information request, while the Ministry of Defense wrote to us that they uploaded all contracts in compliance with law. In a conversation with an employee of Transparency International Georgia, a representative of the State Procurement Agency explained that this may have been caused by a technical failure. As the problem was not eliminated while we were working on the report, after some time, we contacted the Agency again. In a second conversation, the Agency's representative stated that the Electronic Procurement System was in order and they had not impeded access in any manner. For reasons unknown to us, a part of simplified procurements of the Ministry of Defense and simplified procurements of the Ministry of Internal Affairs are still impossible to find in the CMR section of the Electronic Procurement System.

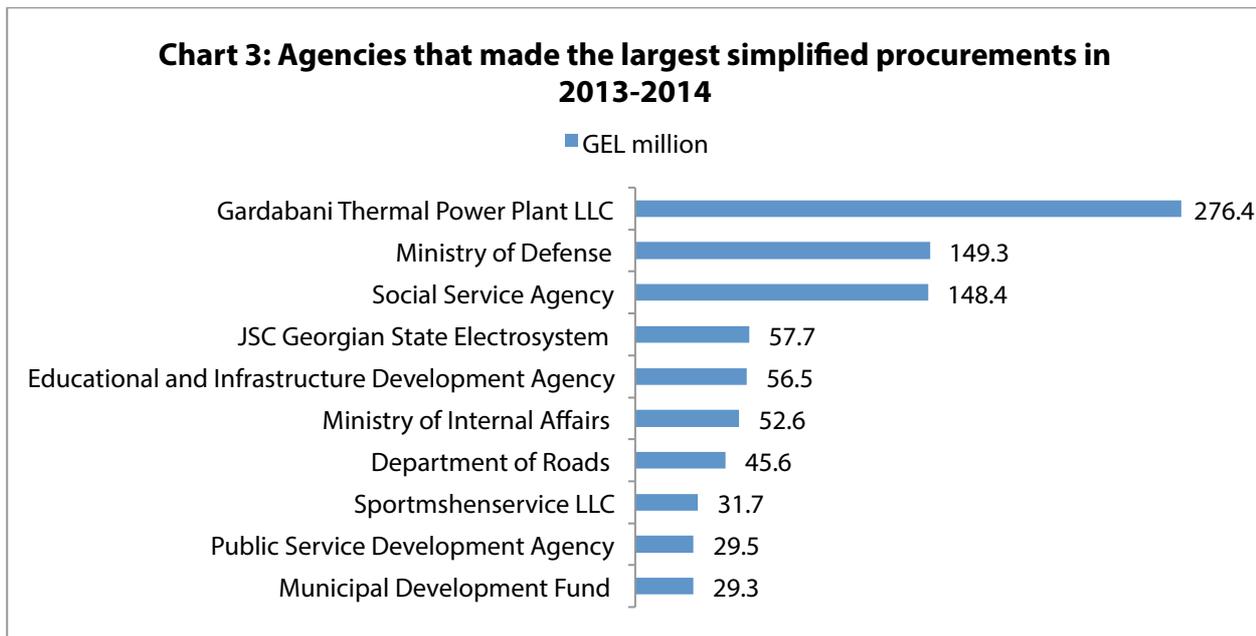
Recommendation:

- The State Procurement Agency, as well as the Ministries of Internal Affairs and of Defense, should explain officially why the simplified procurements of these ministries, which do not constitute state or commercial secrets, are not visible on the corresponding website. These agencies should eliminate the technical fault as soon as possible and make their procurements accessible.

It should be noted that the volumes of simplified procurements of other ministries fall behind those of the Ministries of Defense and of Internal Affairs to a significant extent:

- The Ministry of Corrections and Probation (GEL 8.7 million);
- The Ministry of Finance (GEL 8.5 million);
- The Ministry of Internally Displaced Persons from the Occupied Territories, Accommodation and Refugees (GEL 5.4 million).

Despite the fact that some ministries have not made large simplified public procurements, legal entities of public law (LEPL) subordinated to the ministries have spent large sums. For example, two LEPLs of the Ministry of Infrastructure – the **Department of Roads** and the **Municipal Development Fund** – concluded simplified procurement contracts with a total value of almost GEL 75 million.



2.2. Local government

In 2013-14, the following agencies were distinguished by making the largest simplified procurements at the local government level:

- **The Tbilisi City Hall** (GEL 21.9 million)

During these two years, the capital's City Hall spent more than GEL 12 million on construction works with a simplified procedure. Fuel and motor vehicles turned out to be the most expensive sectors for Tbilisi City Hall after construction works – the fuel expenses of the City Hall reached GEL 2.4 million. The City Hall spent GEL 746,592 on motor vehicles in 2013 (in 2014, the agency did not purchase vehicles through simplified procurement). With this money, the City Hall purchased 21 vehicles. Of these, one was a truck (designed for transportation of goods), and the remaining 20 vehicles were sedans. The entire sum spent on the vehicles went to only two companies – Kia Motors Georgia and Auto Trade In. During the two years, the agency spent an additional GEL 695,000 on technical service of motor vehicles and GEL 176,815 on parts and accessories of motor vehicles.

- **The Ozurgeti Municipality** (GEL 10.7 million)

The Ozurgeti Municipality (after the 2014 self-government elections, the City Hall of the Town of Ozurgeti and Gamgeoba of the Ozurgeti Municipality) spent almost GEL 8 million on services related to

construction works. In addition, almost a million lari was spent on construction materials. The expenditures of the municipality in other sectors are much smaller.

With Order No. 98 of December 19, 2014, the Sakrebulo of the Ozurgeti Municipality gave permission to purchase motor vehicles worth GEL 90,000 through simplified procurement. With the consent of this order the Gamgeoba of the Ozurgeti Municipality purchased two SUVs that December: one priced at GEL 43,700 and another priced at GEL 40,000.

Recommendation:

- It is unjustifiable to purchase expensive vehicles with the motive of urgent necessity and it raises doubts as to whether it was necessary to make these procurements in this form. At this stage, there is no independent mechanism of monitoring and enforcement for cases of conflict of interest. It is necessary that the Parliament of Georgia takes interest in this issue and develops an independent mechanism by which cases of conflict of interest in public procurements will be disclosed and corresponding persons will be held accountable.

- **The Batumi City Hall** (GEL 8.2 million)

Expenditures on construction works were also the largest segment (GEL 3.9 million) for the Batumi City Hall. This agency paid GEL 1.6 million to purchase the services of city transport by which it provided groups of beneficiaries (students, pensioners, etc.) with municipal transport. The services of *LEPL Security Police Department* cost Batumi GEL 1.4 million.

- **The Lanchkhuti Municipality** (GEL 7.2 million)

The Lanchkhuti Municipality also spent most of its procurements (GEL 6.4 million) on services related to construction works. Suppliers of the municipality are often physical persons rather than companies.

- **The Dusheti Municipality** (GEL 7.2 million)

The Dusheti Municipality carried out construction works with a value of GEL 4.5 million. Unlike other municipalities, in this case expenditures on air transportation were larger (GEL 153,789), which was typically caused by urgent necessity in settlements in the mountains. During the two years, the municipality purchased tractors with a total value of more than GEL 200,000.

3. THE LARGEST SUPPLIERS

In the years 2013-14, legal entities of public law and state-owned companies were also predominant among the largest suppliers. In total, the income they received during the two years equals about 15% of the total volume of simplified procurements.

3.1. LEPLs in simplified procurements

In 2013-14, up to 40 Legal Entities of Public Law (LEPL) provided services worth GEL 110 million for various public agencies. These were mostly services related to investigation and security, as well as administrative services. Due to this, GEL 90 million from the total sum was distributed to only two LEPLs – the Security Police Department of the MIA (GEL 54.6 million) and the Public Service Hall (GEL 34.4 million).

3.2. State-owned enterprises in simplified procurements

In 2013-14, state-owned enterprises received an income of about GEL 188.6 million from simplified procurements: of this, GEL 112.7 million was received in 2013 and the remainder – in 2014.

The largest supplier among the state-owned companies is Georgian Food Company, an enterprise owned by the Ministry of Defense, which provided the Ministry of Defense and its subordinate agencies with

catering services worth GEL 90.4 million. The State Construction Company, which is subordinated to the Ministry of Regional Development and Infrastructure, received an income of GEL 51.4 million during the two years for various construction works. The third largest supplier is Construction Company – Builder 2011 which provided services with a total value of GEL 3.5 million.

In the case of state-owned enterprises, too, simplified procurements were mainly made with the Government's permission. Secured simplified procurement contracts with state-owned companies puts the private sector in an uncompetitive position. It is uncertain by what criteria the state-owned companies were given priority.

3.3. Private companies in simplified procurements

In 2013-14, the largest simplified procurement contracts were awarded to the following private companies:

- ÇALIK ENERJİ (GEL 271.7 million);
- UGT (GEL 30 million);
- MagtiCom (GEL 19.8 million);
- Zimo (GEL 19.6 million);
- Sun Petroleum Georgia (GEL 17.4 million).

3.4. Unfulfilled contracts

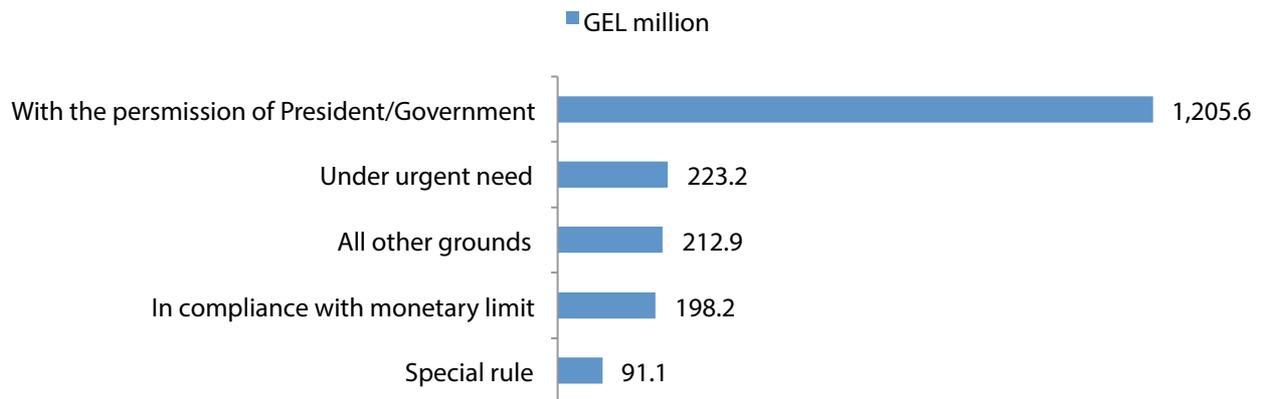
In 2013-14, 1,002 contracts with a total value of about GEL 40 million (0.23% of all the contracts) were not fulfilled. The largest unfulfilled contract (worth GEL 21.1 million) had been signed with the Artes construction company for renovations on a building located at 25 Atoneli Street, Tbilisi. Due to the company's failure to fulfill the contractual obligations, the procurer – Infrastructure Development Company LLC – canceled the contract with Artes.

One more procurer, the TV and Radio Center of Georgia, terminated a contract worth about GEL 10 million with G & T Service LLC due to the latter's failure to submit a bank guarantee. This company was supposed to supply the TV and Radio Center with communications systems in the process of transition to digital broadcasting and perform works related to their introduction. Transition to digital broadcasting is a very important development for Georgia's broadcasting sector, but it was interrupted due to agreement to a simplified procurement contract with an unsuitable company.

3.5. Public procurements made with the permission of the Government/President

In the overview of the legislation, it was noted that state agencies can make simplified procurements on quite a lot of grounds, including when there is permission for this procurement in the form of a normative act issued by the Government. Before the constitutional changes that became effective in 2013, the President was also authorized to issue such an act. Accordingly, this sub-chapter discusses simplified procurements made with the permission of both the Government and the President.

Chart 4: Grounds for simplified public procurements in 2013-2014



In 2013, about 66% of simplified procurements were made with the permission of the Government/President, while in 2014 about 58% of such procurements were made with the Government's permission. In 2013, the value of simplified procurements amounted to GEL 703.9 million, and in 2014 it equaled GEL 501.7 million, which means a decrease by 29%. During the two years, about GEL 636 million was spent from the state budget on the basis of this procedure, GEL 64.8 million was spent from the budgets of local self-government bodies, and GEL 14.9 million – from the budgets of the autonomous republics. The agencies made procurements of about GEL 461 million from their own revenues; accordingly, a larger part of the expenditures on public procurements which were made with the permission of the Government/President involve state funds, not the revenues of LEPLs and state-owned enterprises.

These sums were distributed to the following categories: construction services (GEL 618 million), healthcare services (GEL 170.3 million), canteen and catering services (GEL 75 million), administrative services (GEL 35.1 million), etc.

Procurement of construction works of the Gardabani Combined Cycle Power Plant, as well as procurement of catering services from the state-owned Georgian Food Company by the Ministry of Defense, was made with the Government's permission.

As already noted in the analysis of the legislation on public procurements, the permission of the Government/President is used "with the purpose of unhindered conduct of measures of state and public importance within limited time frames". This entry is quite vague and can be applied in relation to a broad spectrum of goods and services, which enables public agencies to avoid competitive tenders.

Recommendation:

- It is important to ensure that some procurements made with the Government's permission, especially the procurements of construction works, are carried out through competitive tenders. If a procurement is indeed made necessary by a force majeure situation (e.g. a natural disaster), the procurement basis should contain a corresponding entry. The simplified procurements made with the Government's permission often show, however, that there was no such need. As a result, healthy competition is not created and the State cannot manage to save funds.

3.6. Participation of companies of public officials in simplified procurements

During the research we also studied the participation of those companies owned by public officials and their families in simplified procurements that public officials had indicated in their asset declarations.

As it turned out, in 2013-14, companies connected to several officials received quite large incomes by means of simplified procurements. Particularly noteworthy are the instances where the companies were contracted by agencies with which the officials have direct links.

Valeri Gelashvili – member of the Parliament

A son of the Majoritarian MP of Khashuri, Valeri Gelashvili, whose name is also Valeri Gelashvili, is the director of Evra-Construction LLC (currently Lit Geo Invest LLC). In 2013, the company signed a construction works contract worth GEL 151,726 with the Khashuri Municipality.

At the same time, the MP's Bureau of Valeri Gelashvili himself made two contracts with a total value of GEL 14,000 with Evra-Construction LLC.

According to Subparagraph 1 (e), Article 8 of the Law of Georgia on Public Procurement, the conditions for avoiding a conflict of interest apply to selection of a supplier in case of a simplified procurement. A physical person making a simplified procurement will be in a conflict of interest with a supplier if they are related as envisaged by Article 19 of the Tax Code of Georgia.

According to Article 19 of the Tax Code, special relations include those relations in which persons are first branch relatives (spouse, parent, child, sister, brother) or second branch relatives (spouse, parent, child, sister, brother of each of the relatives under the first branch, with the exception of an individual that has already been ascribed to the first branch). Judging from this, a conflict of interest is present.

The Law on Public Procurement establishes the following rule to avoid such cases: *"If a person performing activities stipulated in Paragraph 1 of this Article [in our case, such activity is simplified procurement] turns out to be in a conflict of interest, he/she must immediately declare about the aforementioned and cease any involvement in the implementation of this procurement."* According to Article 195 of the Criminal Code of Georgia, a prior agreement or other deal by subjects taking part in public procurements for obtaining a material benefit or advantage for themselves or other persons which has caused an essential violation of the procuring organization's lawful interest is punishable by a fine or by deprivation of liberty for up to two years.

Akaki Machavariani – Chairman of Sakrebulo of the Kharagauli Municipality

Akaki Machavariani has been the Chairman of the Sakrebulo of the Kharagauli Municipality since 2010. According to his asset declarations of 2013 and 2014, he is a shareholder of JSC Autotrans. In the years 2013-14, JSC Autotrans was awarded simplified procurement contracts with a total value of GEL 45,735, most of which the company of the Chairman of the Sakrebulo concluded with the Kharagauli Municipality. In this case, too, a conflict of interest is present.

Recommendation:

- Law enforcement bodies should take interest in government contracts that reveal an obvious conflict of interest and a possible criminal offence.

Sergo Khabuliani – member of the Parliament

In 2013-14, Tsekuri LLC, 62% of which is owned by MP Sergo Khabuliani, obtained five simplified procurement contracts with a total value of GEL 8.9 million. The Majoritarian MP of Tsageri was awarded the largest of these contracts (with a value of GEL 6.8 million) by the Department of Roads of the Ministry of Infrastructure for the performance of works of rehabilitation of the Kutaisi-Tskaltubo-Tsageri-Lentekhi-Lasdili highway, while the remaining contracts were awarded to the company by the Tbilisi City Hall.

Kakhaber Okriashvili – member of the Parliament

During the two years, two companies owned by Kakhaber Okriashvili (PSP Pharma and PSP Insurance) obtained more than 400 simplified procurement contracts with a value of about GEL 8.9 million. The largest of these – a contract with a value of GEL 6.3 million – was awarded to PSP Insurance by the Ministry of Internal Affairs.

Gocha Eukidze – member of the Parliament

MP Gocha Eukidze sold his stakes in most companies in July 2013. His former and current companies received revenues of about GEL 8.2 million through simplified procurement contracts while under Eukidze’s ownership.

Revenues of Gocha Eukidze’s former companies received through simplified public procurements before July 15, 2013	Revenues of Gocha Eukidze’s current companies received through simplified public procurements in the years 2013-14
Iberia Service LLC – GEL 3.69 million	Iberia Petroleum LLC – GEL 164,814
Kia Motors Georgia LLC – GEL 1.9 million	City Sport LLC – GEL 8,425
Caucasus Motors LLC – GEL 1.4 million	
Iberia Autohouse LLC – GEL 490,198	
Iberia Auto Land LLC – GEL 313,179	
Iberia Auto LLC – GEL 142,800	
Iberia Tech Automotive LLC – GEL 56,274	
Auto Style LLC – GEL 62,651	

Irakli Gegeshidze – Gamgebeli of the Bagdati Municipality

Irakli Gegeshidze has been the Gamgebeli of the Bagdati Municipality since the local self-government elections of 2014. According to his asset declaration of 2014, Gegeshidze is a shareholder of JSC Bagrationi

– 1882. In 2013-14, this company received almost half a million lari in total through simplified procurements, and from July 2014 to the end of the year, it received about GEL 205,000.

3.7. Political party donors in simplified procurements

The Financial Monitoring Service of the State Audit Office regularly releases information about donors of political parties. During the past two years, the parties comprising the Georgian Dream coalition received a total of GEL 9.4 million in contributions, while the United National Movement received about GEL 729,000. One of the important risks of corruption in the case of financing of political parties is usually related to contributions. Receiving government contracts in return for financial assistance to political parties is considered a problematic issue in many countries.

In June 2014, Transparency International Georgia released data on the participation of companies connected to political party donors in public procurements. In the publication, it was noted that companies with direct links with donors of Georgian Dream (through the director, an owner, or a member of the supervisory board) were awarded contracts worth GEL 5.6 million through simplified procurements from January 2013 up to May 2014, while, in the case of the United National Movement, this sum amounted to about GEL 140,000.²⁷ No simplified procurement contract of a significant volume has been made with companies connected to donors of either Georgian Dream or the United National Movement since May 2014.

It should also be noted that this problem was far more severe in the years 2011-12. Specifically, in 2012 the United National Movement received GEL 6.6 million in contributions from the very persons whose companies received GEL 160 million from the State through simplified procurement contracts (in 2011, the same companies were awarded contracts of GEL 110 million with the same method).²⁸

²⁷ Transparency International Georgia, June 25, 2014, *Connections among political parties, their donors, and companies contracted for state acquisitions*: <http://transparency.ge/en/blog/connections-among-political-parties-their-donors-and-companies-contracted-state-acquisitions>

²⁸ transparency International Georgia, December 6, 2013. *Simplified procurement: Corruption risks in non-competitive government contracts*: <http://transparency.ge/en/simplified-procurement>

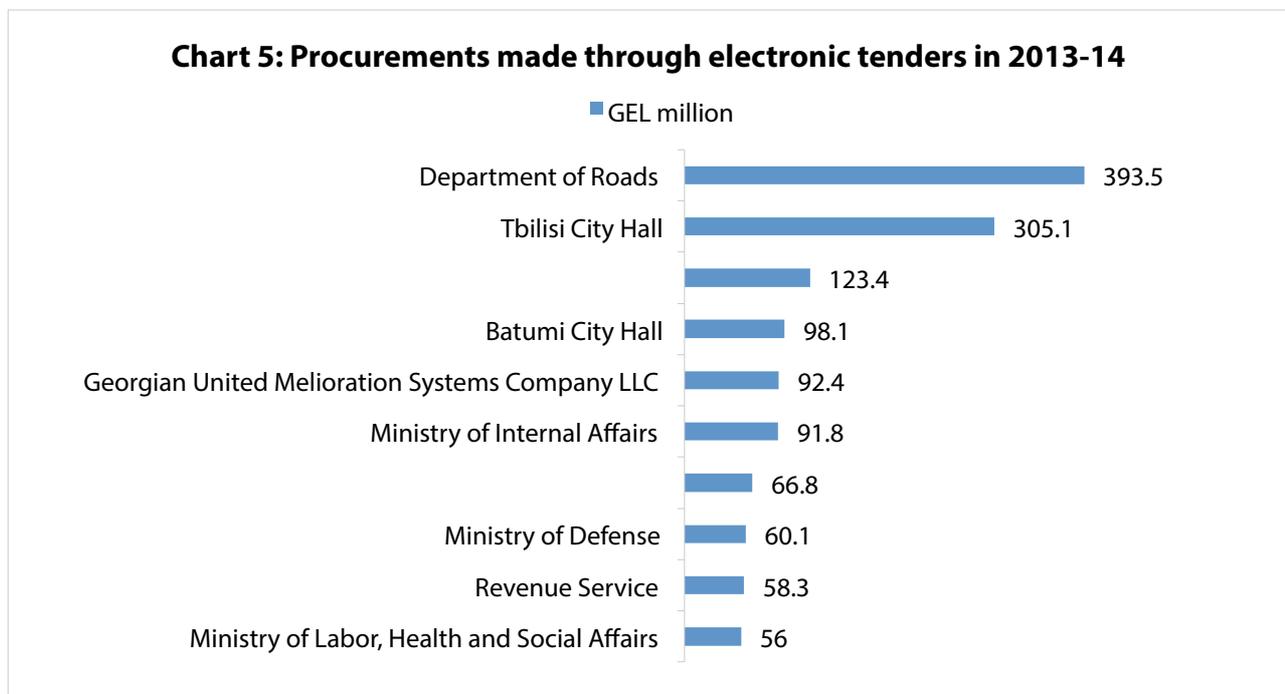
V. ELECTRONIC TENDERS

An electronic tender is the most common means of procurement which is characterized by a high degree of transparency and competition. According to the Georgian legislation, a simplified electronic tender, which is held within tight time frames, is used for procurements with a value below GEL 200,000, while an electronic tender is to be held for procurements worth more than GEL 200,000. The process of simplified electronic tenders and tenders is regulated by the Law of Georgia on Public Procurement.

In 2013-14, the total volume of public procurements made through electronic tenders amounted to GEL 3.132 billion. Of this, procurements with a value of GEL 1.428 billion were made in 2013, and those with a value of GEL 1.704 billion were made in 2014. In 2014, the sum spent through electronic tenders and simplified electronic tenders amounted to about 60% of the total sum spent on public procurements, and in 2013 it amounted to 51% of the total figure.^{29 30}

1. THE LARGEST PROCURER ORGANIZATIONS

The largest procurer in 2013-14 was the *Department of Roads* of the Ministry of Regional Development and Infrastructure whose procurements made through electronic tenders amounted to GEL 393.5 million. In the same period, the second largest procuring agency with GEL 305.1 million was the *Tbilisi City Hall* followed by the *Educational and Scientific Infrastructure Development Agency* with GEL 123.4 million. The fourth largest procuring agency in terms of procurements made through electronic tenders was the *Batumi City Hall* with GEL 98.1 million, while the fifth largest one was *Georgian United Melioration Systems Company LLC*, which made procurements of GEL 92.4 million.

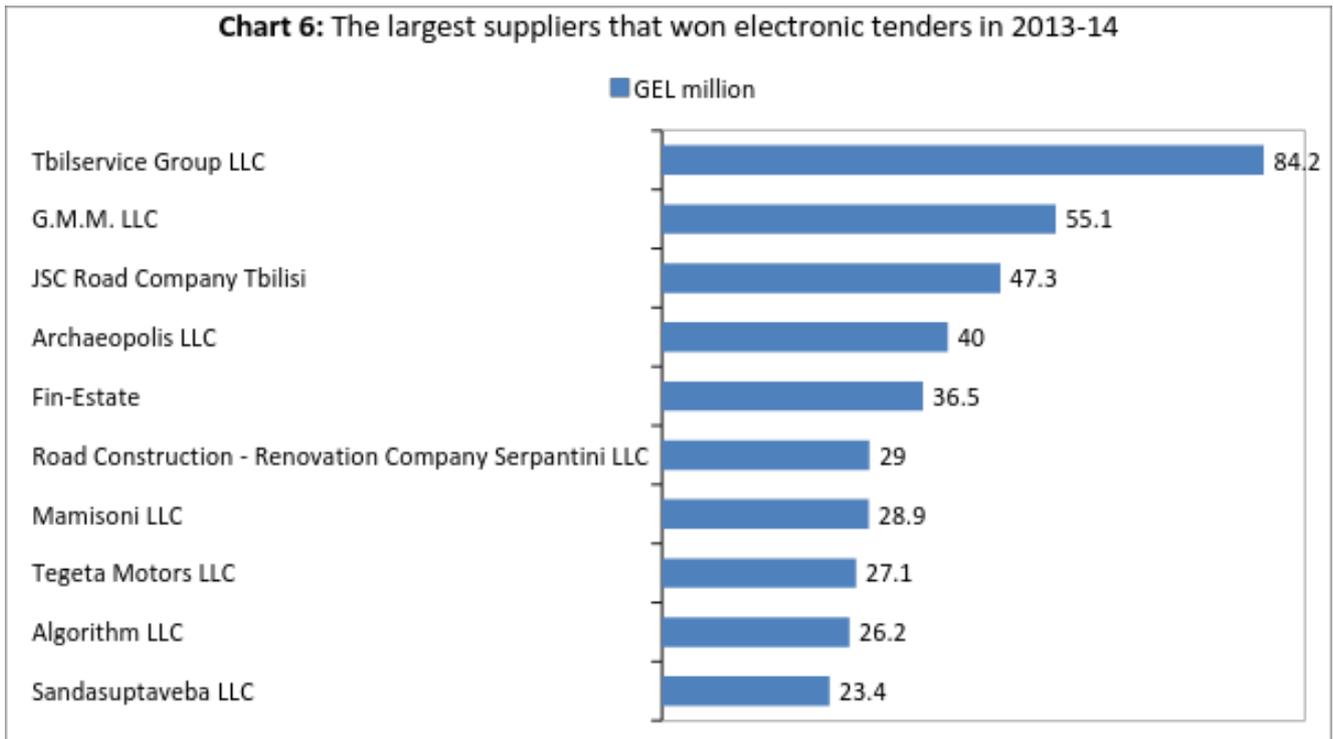


²⁹ The Public Procurement Agency. Activity reports of 2013 and 2014: <http://goo.gl/OKK35M>, <http://goo.gl/Lacq0p>

³⁰ The data presented in the sub-chapter are rounded figures of the sums spent as a result of procurements.

2. THE LARGEST SUPPLIERS

In 2013-14, the largest supplier of goods and services procured through electronic tenders was Tbilservice Group LLC, 100% of whose stake is owned by the Tbilisi City Hall. In this period, the company was awarded contracts with a total value of GEL 84.2 million. The second largest supplier during this two-year period was G.M.M. LLC with GEL 55.1 million. JSC Road Company Tbilisi, Archaeopolis LLC, and Fin-Estate LLC were the third, fourth, and fifth largest suppliers with GEL 47.3 million, GEL 39.9 million, and GEL 36.5 million, respectively. And Road Construction – Renovation Company Serpantini LLC took the sixth place among the largest suppliers with contracts worth GEL 29 million.



3. AMENDMENTS TO THE CONTRACTS

In 2013-14, 42,404 contracts were formed through electronic tenders. Of these, no changes have been made to 33,984 contracts (80%) since their enactment, one change was made to 5,753 contracts (13.5%), two changes were made to 1,604 contracts (3.7%), and three or more changes were made to the remaining 1,063 contracts (2.8%).

During 2013-14, the most changes (124) were made to the contract with a value of GEL 250,000 between a sub-agency institution of the MIA, the Border Police, and Autoservicecenter+ LLC (SPA130003939) which was concluded on April 4, 2013. However, the changes did not apply to the contract value.

On March 12, 2013, 93 changes were made to the contract worth GEL 120,000 between the Penitentiary Department of the Ministry of Corrections and Probation and Center House LLC (SPA130002888). The contract value was not changed in this case either. The object of both contracts was the purchase of technical services of vehicles owned by the agencies.

On February 27, 2013, 48 changes were made to the contract with a value of GEL 755,994 between the Patrol Police Department of the MIA and Insurance Company Ardi Group LLC (SPA130002267). As a result of

the changes, the final value of the contract was set as GEL 781,100. This time, the subject of the contract was the insurance of motor vehicles.

3.1. Contracts worth more than a half a million lari to which more than 20 changes were made

On March 7, 2013, 44 changes were made to the contract between the Ministry of Internal Affairs and the GPI Holding insurance company (SPA130003090). The initial contract sum amounted to GEL 2,826,501, although, as a result of the changes, it was decreased to GEL 2,767,152. The object of the contract was the purchase of insurance of motor vehicles.

On February 27, 2014, the Border Police, a sub-agency institution of the Ministry of Internal Affairs, and the Mate Motors company signed a contract with a value of GEL 510,000 (SPA140000694), although, after 31 changes that were made to it, the contract sum was set as GEL 560,000. The object of the contract was the repair, maintenance and associated services of vehicles and related equipment.

On January 31, 2014, the Patrol Police Department of the MIA and JSC Aldagi Insurance Company signed a contract with a value of GEL 1,084,837 (SPA130028925), although, after 26 changes were made to it, the contract sum was decreased to GEL 1,053,117. The object of the contract was the insurance of motor vehicles.

4. FOREIGN COMPANIES IN TENDERS

A total of 85 companies took part in electronic tenders announced in the years 2013-14. Of these, 60 companies were able to win. In this period, 87 contracts with a total value of GEL 102 million were established with foreign companies. Specifically, in electronic tenders announced in 2013, 33 contracts with a value of GEL 29 million were made with 27 foreign companies, while in 2014, 40 foreign companies won in 54 electronic tenders with a total value of GEL 73 million.

In 2013-14, JSC Georgian Oil and Gas Corporation signed three contracts with the largest total volume – GEL 21 million – with foreign companies. The state-owned Tetnuldi Development LLC ranks the second in this regard with GEL 15.38 million. The third largest procurer of goods/services from foreign companies through electronic tenders is LEPL Service Agency of the MIA with GEL 10.5 million.

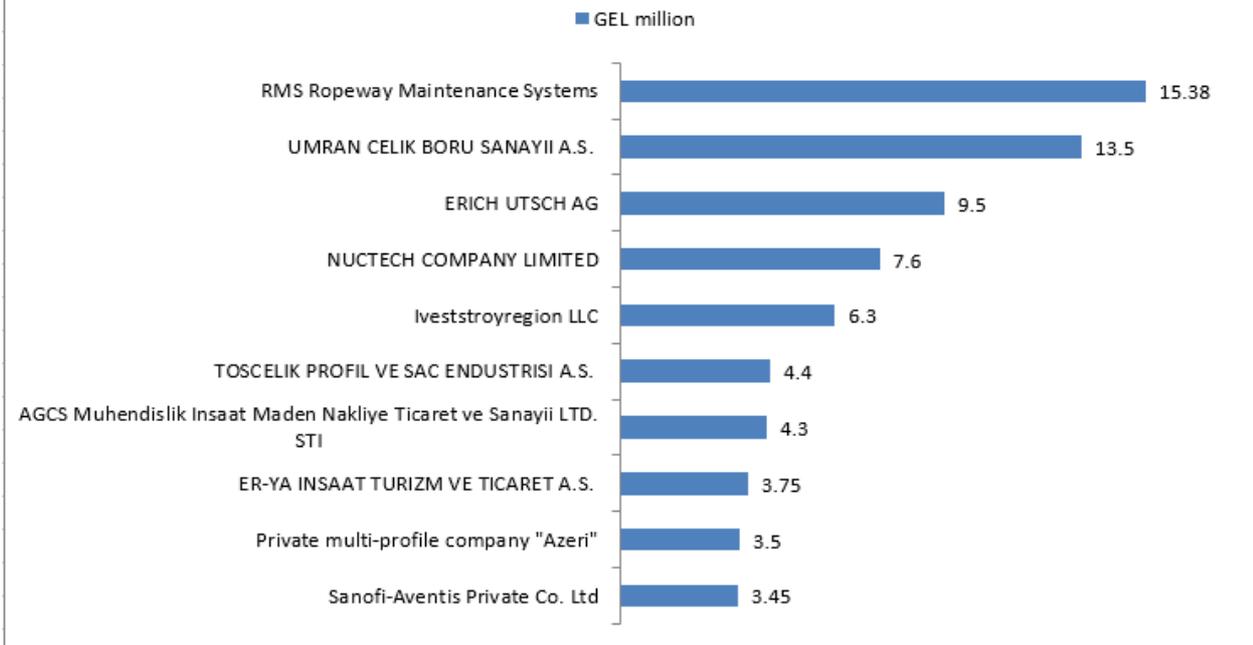
In 2013-14, the largest contract (worth GEL 15.38 million) through an electronic tender was made by the state-owned Tetnuldi Development LLC with an Austrian company RMS Ropeway Maintenance Systems. The contract was formulated with the aim of purchasing works for complete or partial construction and civil engineering work.

In the same period, JSC Georgian Oil and Gas Corporation signed the second largest contract with a foreign company. The value of the contract made with a Turkish company UMRAN CELIK BORU SANAYII A.S. is GEL 13.5 million, and its purpose was to purchase construction materials and auxiliary construction materials.

The third largest procurement with the participation of a foreign company - ERICH UTSCHE AG. - was made by LEPL Service Agency of the MIA. The value of the contract is GEL 9.5 million, and it was made with the German company with the aim of purchasing miscellaneous transport equipment and spare parts.

In 2013-14, foreign companies most often took part in electronic tenders announced with the aim of purchasing pharmaceutical products. Thirteen of the 87 contracts (15%) that were concluded with foreign companies in the reporting period were intended to purchase pharmaceutical products.

Chart 7: Foreign companies that won the largest electronic tenders



5. RISKY PROCUREMENTS

In 5,644 cases (13.3%) out of 42,404 contracts that were concluded through electronic tenders in 2013-14, the competition was low (only one participant). In addition, after changes were made to 44 contracts (0.1%) concluded through an electronic tender, the final contract value exceeded the price offered by the losing bidder in the tender.

6. COMPANIES CONNECTED TO PUBLIC OFFICIALS IN ELECTRONIC TENDERS

Among the winners of electronic tenders in 2013-14, particularly noteworthy are the companies connected to various public officials. Such companies are those that were mentioned in the officials' asset declarations. However, unlike simplified procurements, electronic tenders involve much less risk that the winning company will be selected unfairly, on the basis of private interests.

Davit Gelegashvili – Deputy Minister of Agriculture

In 2013-14, the Herio company, 100% of whose stake is owned by the Deputy Minister of Agriculture Davit Gelegashvili, won eight electronic tenders. The total value of the contracts amounted to GEL 9.5 million. In all the cases, the object of the contract was the performance of works for complete or partial construction and civil engineering work. Of these, Herio signed five contracts with the Tbilisi City Hall, two contracts – with the Gamgeoba of the Mtatsminda District, and one contract – with the Department of Roads of the Ministry of Regional Development and Infrastructure.

Nugzar Surmanidze – Minister of Health and Social Affairs of the Autonomous Republic of Adjara

In 2013-14, the Vitapharm company, 10% of whose stake is owned by Nugzar Surmanidze, won 19 electronic tenders. The total value of the contracts amounted to GEL 928,000. The contracts were mainly

made with the aim of purchasing pharmaceutical products and medical equipment. Among the procurers are Tbilisi State Medical University, Batumi Republican Clinical Hospital LLC, Batumi Regional Center of Infectious Pathology, AIDS, and Tuberculosis LLC, and other organizations.

Giorgi Topadze – member of the Parliament

In 2013-14, the Kazbegi 1881 company, 24% of whose stake is owned by MP Giorgi Topadze, signed a contract worth GEL 877,000 with Georgian Food Company LLC through an electronic tender. A 100% stake in Georgian Food Company is owned by *LEPL State Military Scientific-Technical Center "Delta"*. The object of the contract was the purchase of refreshment drinks.

Gocha Enukidze – member of the Parliament

Gocha Enukidze sold his stakes in most companies in July 2013. But before July 2013, his companies Iberia Autohouse LLC, Caucasus Motors LLC, Kia Motors Georgia LLC, Iberia Auto LLC, and Iberia Tech Automotive LLC made contracts with a total value of GEL 1.6 million with various state agencies through electronic tenders.

Gocha Enukidze's former companies that have won electronic tenders	The value of contracts awarded before July 15, 2013 (GEL)
Kia Motors Georgia LLC	381,500
Caucasus Motors LLC	409,800
Iberia Autohouse LLC	524,000
Iberia Auto LLC	208,800
Iberia Tech Automotive LLC	106,000

Jemal Putkaradze – member of the Supreme Council of the Autonomous Republic of Adjara

In 2013-14, Neopharm LLC, 12.9% of whose stake is owned by Jemal Putkaradze, signed a contract with a value of GEL 24,460 with the Social Service Agency. The object of the contract was the purchase of pharmaceutical products.

Giorgi Zedelashvili – former Deputy Minister of Internal Affairs

Serpantini LLC was registered on May 19, 2000. Its director is Zurab Peikrishvili, while most part of the stake in the company (51%) is owned by Tamar Jankarashvili. According to news reports, Serpantini has links with several high-ranking officials. Specifically, according to news reports, Tamar Janrakashvili is the mother of the former Deputy Minister of Internal Affairs, currently the Deputy Head of the Council on the Management of Crises and State Security, Giorgi Zedelashvili. The total value of the contracts that the company won in 2011-12 through electronic tenders amounts to GEL 6,191,375. Serpantini is operating in

the field of construction works, and its services are mainly used by the Department of Roads of the Ministry of Regional Development and Infrastructure, Georgian United Melioration Systems Company LLC, and various municipalities.

VI. CONCLUSION AND RECOMMENDATIONS

The fundamental reforms that were implemented after 2009 made Georgia's public procurement system one of the most transparent in the world, which was given high evaluation by Transparency International Georgia and a number of international organizations. However, the openness and transparency of the public procurement system does not always mean that the system ensures saving of funds, adequate competition, etc. just as successfully.

The research into the public procurements of 2013-14 has revealed a number of problems in terms of both legal regulation and practice. The main deficiency of the legislation regulating public procurements in Georgia is the insufficient regulation of various means and procedures of procurement, which creates a significant risk of corruption. In order to resolve the legal and practical problems that were discussed extensively in the report, we believe, the following recommendations should be taken into consideration:

- In order to reduce the risks associated with simplified procurements, we believe the government should introduce two key terms into public procurement legislation: 1. *Force majeure situation* and 2. *Urgent need*, which will include every situation, when shortened time frames for procurement will be allowed on the basis of European practices:
 - **Urgent need** should be interpreted as a situation in which it is not possible to foresee the need, and/or the reason for the procurement was not caused by the procuring organization's actions, or which, by not procuring, would significantly harm the public's or the state's interests or property;
 - **Force majeure situations** should include wars or national emergencies, strikes, sabotage, industrial unrest, civil unrest, blockade, insurrection, ecological catastrophe, natural disasters, epidemics, dangerous situations related to disease among the animal population, or other *force majeure* situations in which by not procuring an item, human life, health, public welfare, or state security will be endangered.
- Simplified electronic tenders valued at GEL 200 000 or more should not be used in instances where it is in the public or state interests to carry out the procurement in a shorter timeframe, but rather should only be used in instances of urgent need or force majeure situations, as defined in this section.
- As with electronic tenders, simplified electronic tenders should require bidders to present qualification documents (the organization's registration number, legal restrictions, and existing financial and other commitments). Demanding qualification documents from a supplier does not represent an extra barrier, but rather it is an additional guarantee for the procuring entity that the supplier is qualified to implement the given work.
- Bidders should keep the right to lower the price of their proposal in order to win a tender, although it is important that the final price and the difference between the estimated value of the procurement and the final price be substantiated. Structured substantiation requires the creation of a questionnaire in which procuring entities ask suppliers specific questions, when the proposed price is lower than the estimated value of the item to be procured by 20% or more. When the substantiation is not structured, the supplier will be unable to respond to the questions, which are essential for the procuring agency to know the answers to in order to guarantee that the bidder will be able to provide the good, service, or construction works of the same quality at a lower price.
- It is important that the methodology for preventing the artificial division of tenders be developed in consultation with experts and civil society organizations.

- It is necessary that the public procurement law or the State Procurement Agency Chairman's order specify what worsening the conditions of the contract means, including when conditions require releasing the supplier fully or partially from responsibility for incomplete fulfillment of obligations, and specifically when obligations are not met due to unforeseen factors, such as the devaluation of the national currency or other situations which create a number of problems for suppliers. Apart from this, procurement law should define the misrepresentation on the basis of which a contract was awarded.
- The Public Procurement Appeals Board should be established as a completely independent entity. The Chairman of the Appeals Board should no longer be the Chairman of the State Procurement Agency, nor should the chairman nominate members. The Board of Appeals should be established as an independent entity, which means that the Board should have its own staff who do not work for the Public Procurement Agency.
- To solve these as well as similar problems, Georgia needs to accede to the Government Procurement Agreement, which the country has been an observer to since 1999. Although the legislation in force is neither discriminatory towards foreign suppliers nor protectionist towards local suppliers, the public procurement market has still not been liberalized. The procurement market can only be liberalized through changes to Georgian legislation;

As the conclusion of the State Audit Office's 2014 report³¹ has it, **unified procurement should be used more actively in instances where centralization is expedient.** Public procurement is still carried out in a decentralized manner, which in turn prevents the state from saving public money;

The State Audit Office's recommendation that a supplier assessment system should be developed should be implemented in a timely manner. This will ease procurement planning as well as the process of selecting suppliers. Suppliers could be rated by a "star" system based on objective criteria.

- Construction works belong to the very categories where the **share of simplified procurements should decrease**, because:
 - There are an abundance of companies operating in this sector in Georgia and, under high competition, the government will be able to save more funds when carrying out expensive projects if the share of competitive tenders increases further;
 - Construction works are always long term ventures and it is ineffective to avoid a competitive tender for the purpose of saving time.
- Expensive vehicles should not be procured with the motive of urgent necessity. At this stage, there is no independent mechanism of monitoring and enforcement for cases of conflict of interest. It is necessary that the Parliament of Georgia takes interest in this issue and develops an independent mechanism by which cases of conflict of interest in public procurements will be disclosed and corresponding persons will be held accountable;
- It is important to ensure that some procurements made with the Government's permission, especially the procurements of construction works, are carried out through competitive tenders. If a procurement is indeed necessary because of a force majeure situation (e.g. a natural disaster), a corresponding entry should be made in the procurement basis entry in the system.

³¹ State Audit Office, March 18, 2014. *Ensuring the effectiveness of the public procurement system*: <http://goo.gl/LNpZFY>



JULY 2015
TBILISI