Ruslan Dzhabrailov
Doctor of Legal Science, Senior Lecturer
Deputy Head of the Department on
Commercial Law and Legislation Modernization
Institute of Economic and Legal Research
of the National Academy of Sciences of Ukraine

Vesta Malolitneva
PhD in Law, Research Fellow
Institute of Economic and Legal Research
of the National Academy of Sciences of Ukraine

HARMONIZATION OF UKRAINE'S PUBLIC PROCUREMENT SYSTEM WITH THE EU STANDARDS: THE CONCEPT OF SPECIAL AND EXCLUSIVE RIGHTS

Over the last few years Ukrainian legislation has been substantially updated which was stipulated by different reasons and aims, in particular to prevent corruption, to simplify public procurement rules, to promote competition and transparency, etc. With ratification of the EU-Ukraine Association Agreement [1] Ukraine assumed obligations to harmonize national legislation with the basic requirements of the EU Treaty and the detailed provisions of the EU Directives on public procurement according to the Chapter 8 of Section IV and Appendix XXI of the Association Agreement which address the relationships in the public procurement field, providing for the public procurement market liberalisation. Currently, the main amendments to the Ukraine's legislation on public procurement are based on the need to harmonize national laws with the EU requirements. One of the recent and most essential amendments envisages that not only contracting authorities and public undertakings but also private entities may fall within the scope of public procurement legislation because they carry on the activities in utilities sector on the basis of exclusive or special rights. Since the notion of special and exclusive rights in Ukraine in the context of public procurement is new it is important to define its concept.

Since there are a lot of scientific papers and articles on Ukraine's

public procurement system reform in the context of euro-integration processes [2, c. 12-18; 3, c. 197-214; 4, c. 263-265; 5], there is still lack of literature and research on the concept of special or exclusive rights as well as problems of legal status of private undertakings which pursue an activity covered by the utilities sector under special/ exclusive rights. This makes the study on special/exclusive rights more relevant and defines the main aim of research.

For the purpose of the harmonization with the EU legal acts in the sphere of public procurement Ukrainian Parliament has already entered a considerable number of amendments into the Laws. One of the most significant step towards the European standards was the enactment of an important Law on 'The peculiarities of Public Procurement in Certain Spheres of Economic Activity' (Law on peculiarities) [6]. This Law aims at establishing the legal and economic principles of conducting public procurement in certain sectors of economic activity, namely, in the so-called "utilities", which, in the EU, are regulated by the Utilities Directive. Thanks to this Law the European approach when the legislation on public procurement covers not only public but also private undertakings, which carry on one of the activities referred to in the Law on peculiarites (e.g. production, transportation and supply of heat, electric energy and drinking water), was introduced. However, private entities fall within the scope only subject to the supplementary condition that they carry on the activity on the basis of exclusive or special rights. According to the Ukrainian Law 'On Public Procurement' [7] special and exclusive rights are rights granted within the powers of public authorities or a local self-governing authorities on the basis of a legal act and/or individual act, which restrict the performance of the activities in the areas defined by this Law to one or more persons, which significantly affects the ability of others to carry out such activities.

The notion of special and exclusive rights was introduced in the Ukrainian legislation in compliance with the EU Utilities Directive. According to the Green paper of the European Commission on the modernization of EU public procurement policy the main reason for introducing public procurement rules for the utilities sector was the closed nature of the markets in which undertakings operate, owing to the existence of special or exclusive rights granted by the Member

States [8, p. 11]. Generally special and exclusive rights exist where a license is required to carry out an activity. Undertakings engaged in the activities covered by the Utilities directives have traditionally depended on state licenses: it has almost not possible for anyone to set themselves up, for example, as an water supplier or electricity producer [9, p. 223]. The main reason for regulating procurement of private undertakings was that it was considered that state can influence these entities, because of the power that state has over their operating licenses. In the absence of sufficient competitive pressure, the mandatory public procurement rules were considered to be necessary in oder to ensure that procurement in the utilities sector would be carried out in a transparent and non-discriminatory manner. Otherwise, it was feared that procurement decisions by utility undertaking could be influenced by favoritism, local preferences and other factors [8].

According to the first European Utilities Directive 93/38/EEC coordinating the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors [10], namely the article 2, special and exclusive rights meant rights deriving from authorizations granted by a competent authority of the Member State concerned, by law, regulation or administrative action, having as their result the reservation for one or more entities of the exploitation of an activity defined in the Utilities Directive. The aforementioned Directive clearly defined when the contracting entity should be considered to enjoy special or exclusive rights, in particular where: 1) for the purpose of constructing the networks or the facilities referred to in Directive, it may take advantage of a procedure for the expropriation or use of property or may place network equipment on, under or over the public highway; 2) the entity supplies with drinking water, electricity, gas or heat a network which is itself operated by an entity enjoying special or exclusive rights granted by a competent authority of the Member State concerned. Such concept of special and exclusive rights did not cause problems and provided for an understanding of the necessity for private operators to follow public procurement rules.

However, on 15 September 2015 the Ukrainian Parliament adopted the Law 'On Amendments to Some Legislative Acts on Public Procurement in Order to Ensure the Compliance with

International Standards and to Combat Corruption' [11], which altered the notion of special and exclusive rights. According to this Law the rights, which were granted within the open procedure (tendering) on the basis of objective criteria with adequate publicity before the procedure, do not constitute exclusive or special rights. The substantiation of the need to adopt the mentioned amendment is missing. However, the Ukraine's Strategy of reforming the public procurement system ("Roadmap") [12] defines stages of the harmonization process of Ukrainian legislation with the requirements of the EU where special and exclusive rights play an important role. Thus, the introduction of the new provisions is based on on the need to harmonize Ukrainian legislation with the requirements of the EU Directives on public procurement. In order to determine the aim of making the procedure for acquiring exclusive and special rights as the main criteria which defines whether special or exclusive rights exist or not, it is rational to appeal to the EU law on public procurement.

Since the adoption of the first European Utilities Directive the gradual liberalization processes have been pursued either at EU level or at the national level for many sectors (e.g. electricity supply, postal services, etc.), which essentially influenced the concept of special and exclusive rights. Now within the EU the need for an operating license granted by government will not necessarily constitute a special or exclusive right. In 1996 the European Court of Justice (the Court) in the *Telecommunications* case [13] substantially updated the notion of special and exclusive rights. The Court stated "that the exclusive or special rights in question must generally be taken to be rights which are granted by the authorities of a Member State to an undertaking or a limited number of undertakings **otherwise than according to objective, proportional and non-discriminatory criteria** (Emphasis added), and which substantially affect the ability of other undertakings to provide or operate telecommunications networks or to provide telecommunications services in the same geographical area under substantially equivalent conditions". The Court pointed out that exclusive or special rights for the provision of a public telecommunications network cannot be characterized by the possibility for the authorized telecommunications organizations to enjoy certain prerogatives, in

particular the right to acquire land compulsorily, to enter land for exploratory purposes and to acquire land by agreement or to place network equipment in, over or under the public highway and to place apparatus on private land with the consent of the persons having an interest in that land, which consent can be dispensed with by the Court, inasmuch as such rights, "which are merely intended to facilitate the provision of networks by the operators concerned and are or may be conferred upon all those operators, do not give their holders any substantial advantage over their potential competitors".

The unacceptable situation appeared when the concept of special and exclusive rights had two different meanings both in the Court's Judgment and the Utilities Directive 93/39/EEC. In 2004 the new Utilities Directive 2004/17/EU coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors [14] accepted the notion of special and exclusive rights which was elaborated by the Court. According to this Directive special and exclusive rights were determined as a rights granted by a competent authority of a Member State by way of any legislative, regulatory or administrative provision the effect of which was to limit the exercise of activities defined in the Directive to one or more entities, and which substantially affected the ability of other entities to carry out such activity. Additionally the Preamble of the Directive 2004/17/EU emphasized on the need to have an appropriate definition of the concept of special and exclusive rights. The consequence of the definition is depicted in three ways: firstly, the availability of a procedure for the expropriation or use of property and the ability of an entity to place network equipment on, under or over a public highway for the purpose of constructing networks, port or airport facilities, do not automatically constitute exclusive or special rights within the meaning of the Directive; secondly a special or exclusive right does not exist merely due to the fact that an entity supplies drinking water, electricity, gas or heat to a network which is itself operated by an entity enjoying special or exclusive rights granted by a competent authority of a Member State; and thirdly, rights granted by Member State through acts of concession, to a limited number of undertakings **on the basis of objective, proportionate and non-discriminatory criteria that allow any interested party fulfilling those criteria** (Emphasis

added) to enjoy those rights are not considered special or exclusive rights.

The practical implication of the definition of special or exclusive rights under the new Utilities Directive 2004/17/EU is the non-applicability of the regime to the entities that do not meet the conditions but are still covered under the existing regime solely because they are considered to benefit from exclusive or special rights. With adoption of the Directive 2004/17/EU it will therefore no longer be possible to conclude the existence of exclusive or special rights solely on the basis of the activity pursued. As stated the European Commission in the explanatory note concerning the special and exclusive rights under the Directive 2004/17/EU, it is in effect unthinkable in practice that an entity might for example distribute electricity without having at least the right to install its pylons on public land. Thus, according to the conclusion of the European Commission it is necessary to analyze on a case-by-case basis whether the entity in question does or does not possess exclusive or special rights [15].

In 2014 the new Utilities Directive 2014/25/EU on procurement by entities operating in the water, energy, transport and postal services [16] was adopted. The definition of the concept of special and exclusive rights in this Directive was altered under the influence of the aforementioned Court's Judgment and the Preamble of the Utilities Directive 2004/17/EU. Currently, the analysis of presence or absence of special or exclusive rights must also include the analysis of the way or procedure how this rights were gained by the private undertaking. According to the new Directive 2014/25/EU the definition of special and exclusive rights was supplemented with the following provision 'rights which have been granted by means of a procedure in which adequate publicity has been ensured and where the granting of those rights was based on objective criteria shall not constitute special or exclusive rights'. The European Commission emphasizes that if private undertaking gained rights to exercise one of the activities covered by the Utilities Directive on the base of objective and non-discriminatory criteria it is not subject to the provision of Directive. However, it is necessary that the procedure used to grant the rights in question should take place after adequate publicity has been guaranteed – in effect, without such publicity it

cannot be guaranteed that the criteria effectively open up to any interested party which fulfills them the possibility of obtaining the right in question [15]. The new Directive 2014/25/EU lists the procedures of granting the rights and when such rights do not constitute special or exclusive rights. This list includes all procedures under the Directive on public procurement with the exception of the negotiated procedure without prior publication. The list also includes procedures established by a number of Directives on liberalization of the EU utilities sector in oder to provide system of competitive distribution of licenses/permits, which aims at providing equal access to all interested entities [17].

One of the justifications for implementation of aforementioned provision to legislation is the following. If any undertaking, which meets certain criteria, can obtain the license and the process of its obtaining is transparent, state can not detrimentally influence the procurement behavior of the recipient of such rights, for example to buy only from local producers. Thus, there is no need to apply utilities procurement regime [18, p. 9].

In this context it is worth specifying another position of the EU on special and exclusive rights the effect of which is to limit the exercise of activities defined in the Utilities Directive to one or more entities, and which substantially affects the ability of other entities to carry out such activity and place the private companies in a monopoly or oligopoly situation. The entities which operates in the utilities sector usually hold a monopoly position. This means in turn that these entities do not have to worry about making good and economical purchases, they can simply transfer their extra costs onto public who has no alternative source of supply available [19, p. 6]. Thus, in order to meet the requirements for quality, price etc., the entity has to comply with the rules on public procurement in the utilities sector, since the activity of such undertaking aims at rendering of public services. According to the European Commission where an entity has the right to operate utilities as a result of an open and advertised procurement procedure there is enough competitive pressure in that market so as to negate the need for the extra protection for consumers which would exist otherwise had these rights been designated “special and exclusive” [20]. Because everyone can obtain the right to carry on the activities in the utilities

sector, competitive pressure on those who already have licenses exists. Such companies therefore must minimize their costs and procure goods on the best commercial conditions but not on the terms of favoritism. Otherwise there is a risk of being eliminated from the market and going bankrupt [19, p. 6]. Thus, according to the European Commission if any company has the right to obtain the license without limitations in their number special and exclusive rights do not exist. Back in 1977 the European Court in the Case 13/77, Inno v ATB, which does not directly concern activities in the utilities sector, ruled that no special or exclusive rights exist where, they have been conferred upon the undertaking as a member of a class carrying on the activity which is open to everyone [21].

The same position is set out in the recommendations on the concept of exclusive and special rights, which should be applied in the Ukraine's legislation on public procurement. These recommendations were elaborated by the project funded by the EU 'Harmonization of Public Procurement System of Ukraine with EU Standards'. According to the mentioned recommendations the risk that procurement decisions by utilities operators could be influenced by state, which resulted in local preferences and favoritism, exists only in those cases where the utilities operators have received the right in a non-transparent manner and is managed at the discretion of state [17].

The experts of mentioned project arrives at the conclusion that special/exclusive right does not exist in case when: 1) relevant activities may be carried out by any economic operator and the right is aimed only at facilitating such activities (land access right, the right to store equipment on, under or over public highway and even the right to mandatory land acquisition), provided that everyone has a de facto equal opportunity to obtain such rights; 2) the right constitutes a condition for carrying out certain activities, but it is automatically granted to everyone willing to obtain it as a kind of a formality (most cases of licensing, for instance, licenses for different construction works, for rendering taxi services, etc.); 3) the right constitutes a condition for carrying out certain activities, but is granted pursuant to the method that includes: open acceptance of applications accessible to all interested undertakings; the right is granted based on objective criteria, thus leaving less possibility for

the states' discretion. In particular, it may be the case when local authorities select local suppliers of transport services, apart from municipal transport (for instance, buses and minibuses for short and medium distance carriage), by means of the competitive procedure or select suppliers of certain utilities (for instance, garbage removal services). However, when the State or local authorities grant by their decision rights to carry out certain activities directly and solely to one or several economic operators, eliminating or significantly restricting the possibility to carry out such activities for other entities, it shall be considered as granting special or exclusive rights. The relevant examples for Ukraine are: formal licensing of electricity distributors and suppliers possessing a technical (natural) monopoly as confirmed by the license; operation of a telecommunication network for rendering general access services (Ukrtelecom's private natural monopoly) [17].

Thus, special or exclusive rights exist where rights: 1) are limited in number; 2) are granted otherwise than in accordance with objective and non-discriminatory criteria and are granted by a competent authority by way of any legislative, regulatory or administrative provision; 3) limit the exercise of activities in utilities sector to one or more entities, and which substantially affects the ability of other entities to carry out such activity. Special or exclusive rights do not exist where: 1) there is no limit to the number of such rights; 2) such rights are granted on the basis of objective and non-discriminatory criteria; 3) do not limit the exercise of activities in the utilities sector to one or more entities.

However, the EU Directive, the Court as well as Ukrainian legislation on public procurement do not solve, as the C. Bovis emphasizes [18, p. 9], the complicated situation when private entity compete for special or exclusive rights such as concessions on the basis of objective criteria but these rights substantially restrict market access to other undertakings and limit the number of interested parties. For example, a private undertaking received a service concession, for instance was entrusted to provide and manage of municipal tramway system for 10 years. Although this entity will be the only concession-holder for such a long period of time, it competed in an open procedure to win this concession.

In addition, the new provision on special and exclusive rights in

Ukrainian legislation on public procurement arises questions on difference between the legal status of private undertaking which obtained special or exclusive right within the competitive procedure on the base of objective criteria, for example according to procedure envisaged in the Law of Ukraine 'On concessions' [22] it received the right to carry on the activities in the water sector for 30 years, and the private entity which obtained such right directly on the base of regulatory provisions of competent authority.

In the first case the entity does not have to follow the requirements of public procurement legislation and in the second case it falls within the scope of such legislation. The European Commission and some authors say that even if only a limited number of undertakings can enjoy the rights, they are open to all to enjoy, as anyone can compete for them and, if the awarding process is transparent there is no possibility for state to influence the concessionaire [9, p. 224]. Moreover, if private companies operating in the utilities sector, won a contract in a public procurement process they are not subjected to the provisions of the Utilities Directive, even if they end up in a monopolistic or oligopolistic position. Such companies are considered to already have had to streamline their procurement in order to submit a competitive offer [19, p. 6]. Furthermore, the Preamble of the Utilities Directive 2014/25/EU states that an entity, which has won the exclusive right to provide a given service in a given geographic area following a procedure based on objective criteria for which adequate transparency has been ensured would not, if a private body, be a contracting entity itself, but would, nevertheless, be the only entity that could provide the service concerned in that area.

Still, the actual situation of undertakings in the first and the second cases is the same, because in both cases the entities are the only companies that carry on activities in the certain markets. In other words they both have monopolistic position. However, the determinative criteria of defining whether the undertaking is subject to the legislation on public procurement or not is only the procedure of acquiring special or exclusive rights.

In the first case the undertaking as a single entity that carries on certain activities in the utilities sector may not fall within the state's influence on purchase decision-making in favor of certain economic

operators, since it was selected in accordance with the open procedure based on objective criteria, but with the course of time this undertaking can start to use money ineffectively transferring extra costs onto the population who has no alternative source to buy goods, services and works from. If there is no incentives for the undertaking in the utilities sector to keep their costs down it could affect the competitiveness of other industries which in turn have to raise their prices. The purchasing power of the population would then be affected, to the detriment of a nation's whole economy [19, p. 8].

In summary the research revealed the following:

1. Currently, according to the novels in the Ukrainian legislation on public procurement in order to define whether a private undertaking in the utilities sector has special and exclusive rights or not, one must analyze the way of obtaining such rights, that is to say, the way of granting rights plays a decisive role.

2. In the case when a private undertaking obtained the right to carry on the activity in the utilities sector within the open procedure based on the objective criteria but this right substantially affects the ability of other entities to carry on such activity, which is examined on a case-by-case basis, it is proposed to establish the duty for such undertaking to observe the basic public procurement principles set out in the Law of Ukraine 'On public procurement', namely the fair competition, economy and efficiency, transparency, non-discrimination, equal treatment, preventing corruption and objective assessment of proposals. Such private undertakings are not required to follow the procurement procedures set out in the Law 'On public procurement', however they have to ensure the level of transparency which allow all interested economic operators who meet certain criteria to participate in the procurement of relevant goods, services and works. For these purposes and with the aim to select a supplier of commodities the private undertakings in the utilities sector may use e-procurement system according to the Law of Ukraine 'On public procurement'. By analogy with the article 2 of the Law 'On public procurement' concerning the coverage of legislation, in case of procurement of goods, works and services without using e-procurement system provided that the value of procurement is equal or more than UAH 50 000 (approximately USD 20 000), the private undertakings in the utilities sector have to publish a report on

concluded contracts in the e-procurement system according to the Law of Ukraine 'On public procurement'. It helps to ensure the compliance of legislation with the Ukraine's obligations within the EU-Ukraine Association Agreement, to be more specific, with the principle of transparency in procurement which is not covered by the EU Directives.

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