

Public Procurement in Bulgaria: The Case of unfair competition

Alexander Boehm, CEU Business School, Budapest, Hungary

Peter Hardi, CEU Business School, Budapest, Hungary

Alexandra Horvathova, CEU, Budapest, Hungary

Rumen Stefanov, New Bulgarian University, Sofia, Bulgaria

Authors:

Alexander Boehm is a researcher at the Center for Integrity in Business and Government (CIBG), CEU Business School.

Peter Hardi is Professor of Business Ethics and CSR, Director of CIBG, CEU Business School.

Alexandra Horvathova is Post-doctoral fellow at CIBG, CEU Business School.

Rumen Stefanov is a Professor at the New Bulgarian University in Sofia.

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Case Summary:

Bulgaria's transition from a communist state with a centrally planned economy to that of a democratic and market-led economy has been fraught with challenges. Despite more than twenty years of democratization, neoliberal economic policies and its 2007 ascension into the European Union, corruption remains pervasive in Bulgaria. This is particularly apparent in the area of public procurement, where the absence of a public procurement process under socialism has made the contemporary processes all the more susceptible to corruption. Consequently, the following case study on public procurement corruption in Bulgaria is designed to provide students with an understanding of how corruption can permeate a country's political, cultural and legal entities.

Learning Objective:

By completing the case study, students will discover that a multidisciplinary approach is needed to determine the culpability of business and public servants in undermining the public procurement process.

Keywords:

Balkan, Bulgaria, Collusion, Corruption, Highway Construction, Public Procurement, Public Tender, Transition Economy, Unfair Competition.

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Economic & Institutional Background

Bulgaria has made considerable strides from its turbulent political and economic transition in the 1990s. Incentivized by its ascension to the European Union in 2007, Bulgaria embraced numerous reforms in all sectors, in an effort to build macroeconomic stability and stimulate growth. Between 2000 and 2010, average annual growth reached 4.7%, whereas the per capita income as a share on the European Union [hereinafter “EU”] average increased dramatically from 28% to 44%. The production of Bulgaria has also expanded and exports have doubled since 2009. Yet despite these advancements, Bulgaria’s economic performance has remained subdued during the post-crisis period of 2009 to present.

Bulgaria has done much to encourage European and international investors who could aid in stimulating its economic growth. However, according to the European Commission, there are still several weaknesses that hinder development in Bulgaria, which governments have been unsuccessful in addressing. These include a low degree of financial intermediation, unreliability of reported financial sector data, weak administrative and judicial systems and pervasive corruption. The judicial system can be characterized as unreliable and does not enforce property rights effectively. Human trafficking, narcotics and contraband smuggling contribute to corruption. In June 2014, in the wake of protests against low standards of living, high-energy costs, and corruption, President Rosen Plevneliev announced that he was dissolving the Bulgarian Parliament. A new election was held on 5 October 2014, and as a result a new government was formed by the GERB (Граждани за европейско развитие на България, “*Citizens for European Development of Bulgaria*”) party at head.

Public Procurement in Bulgaria: *Brief Intro*

The first public procurement law in Bulgaria passed in 1997, when the Law on the Award of State and Municipality Public Contracts was adopted. In 1999 this law was repealed by the Public Procurement Law [hereinafter “PPL”]. The PPL underwent significant changes in 2004 and 2006 as a result of transposition of EU Directives. The legal framework of public procurement is complemented by additional secondary legislation, including the Regulation for Application of the Public Procurement Act, Act on the Liability for Damage Incurred by the States, the Municipalities Ordinance on the Award of Special Public Contracts and several other including the Administrative Procedure Code and Code of Civil Procedure.

Also in 2004, the Bulgarian Public Procurement Agency was established [hereinafter “PPA”], which according to the Decree No. 56 is a self-dependent administrative organ. Yet the PPA is subordinated to the Minister of Economy, Energy and Tourism. The main aim of the PPA is to ensure the efficiency of the public procurement system in compliance with the principles of publicity and transparency, free and fair competition, equality and non-discrimination. The PPA established an e-procurement system in Bulgaria providing a centralized information system, which provides access to all aspects of public procurement.¹

According to the PPL, the following bodies are **subjected** to the public procurement regime: (1) all bodies of state power, (2) the bodies governed by public law,² (3) any medical-treatment facility, which is a commercial corporation and more than 30 percent of the income whereof for the preceding year is for the account of the State budget and/or municipal budget and/or the budget of the National Health Insurance Fund; (4) unions of the above stated bodies, (5) the public enterprises and any combination thereof, where carrying out one or several of the strategic activities³ and (6) the merchants and other persons that are not public enterprises, where carrying out one of several of the activities

¹ Available online at: <http://rop3-app1.aop.bg:7778/portal/page?_pageid=173,1&_dad=portal&_schema=PORTAL>.

² Any legal person which, regardless of its commercial or industrial character, is established for the specific purpose of meeting needs in the public interest and which fulfills any of the following conditions (a) it is more than 50 per cent financed by the State budget, by the budgets of public social insurance or of the National Health Insurance Fund, by the municipal budget, or by any contracting authorities; (b) more than half of the members of the management or supervisory body thereof are appointed by any contracting authorities; (c) which is subject to management supervision by side of any contracting authorities.

³ These activities relate to: (a) natural gas, heat or electricity; (b) drinking water; (c) provision or operation of networks providing a service to the public in the field of transport by railway, tramway, trolley bus or bus, as well as of automated transport systems or cableway; (d) provision of a universal postal service and (e) exploitation of a geographical area

covered by above stated bodies and enterprises on the basis of special or exclusive rights.

Yet despite the regulation in force, conflicts of interests, kickbacks and bribery are frequent in Bulgaria's public procurement process.⁴ More than a half of all companies participating in public procurement in Bulgaria report that corruption prevents them from winning public tenders.⁵ Nevertheless, only very few corruption cases are investigated and prosecuted.⁶

Case Study introduction

Bulgaria's transition from a communist state with a centrally planned economy to that of a democratic and market-led economy has been fraught with challenges. Despite more than twenty years of democratization, neoliberal economic policies and its 2007 ascension into the European Union, corruption remains pervasive in Bulgaria. This is particularly apparent in the area of public procurement, where the absence of a public procurement process under socialism has made the contemporary processes all the more susceptible to corruption. Consequently, the following case study on public procurement corruption in Bulgaria is designed to provide students with an understanding of how corruption can permeate a country's political, cultural and legal entities. The case study showcases how unfair competition in the public procurement process, which often manifests itself in the form of collusion and conflict of interest between business and government, can have a corrosive effect on ethical norms and free market principles. By completing the case study, students will discover that a multidisciplinary approach is needed to determine the culpability of business and public servants in undermining the public procurement process.

⁴ See BTI 2014, Bulgaria Country Report, *available online at*: < <http://www.bti-project.org/reports/country-reports/ecse/bgr/index.nc>>.

⁵ See Report from the Commission to the Council and the European Parliament: EU Anti-Corruption Report, Feb. 3rd, 2014, COM(2014) 38 final, *available online at*: < http://ec.europa.eu/dgs/home-affairs/e-library/documents/policies/organized-crime-and-human-trafficking/corruption/docs/acr_2014_en.pdf>.

⁶ See the 2014 review of the Investment Climate Statement of Bulgaria.

Key Actors

National Government Actors and Entities:

- Ministry of Regional Development (MoRD)
- Inspectorate Department of the MoRD
- Tsvety Ivanova, Inspectorate Department of the MoRD
- Lubomir Tanev, Deputy Minister of MoRD
- Kiril Tanev, Bulgarian Consul-General Thessaloniki
- Public Procurement Agency (PPA)
- Bulgarian Ministry of Foreign Affairs
- Commission for the Protection of Competition (CPP)
- Public Financial Inspection Agency of the Ministry of Finance
- Public Procurement Commission
- Elefteria Stamatakis, a Deputy Minister of Ecology
- Nikolai Valov, Public Procurement Agency Director

International Actors and Entities:

- General Community Directorate of the European Commission
- Official Journal of European Communities
- BIBA – Bank Interests Balkan Analysis

Private Sector Actors and Entities:

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- **Baum**
- **Midos**
- **Tetovostroy**
- **Barge**
- **Firststroy**

- Dragan Vassilev, President of Vassilev LLC and former Pelagos employee
- Ekrem Rama, Majority owner of Tetovostroy
- Georgios Stamatakis, Management Director of Pelagos
- Georgios Fotos, Experienced Greek Journalist
- Petar Dobrev, Young Journalist

Banks

- Pelagos
- Cristalbank
- Rila Bank
- Balkan Bank

Narrative

Stage I:

As **Tsvety Ivanova** turns the corner from Vasil Levski Boulevard onto Cyril and Methodius Street in downtown Sofia, she figures she must be close. Her mind begins to race as her pace quickens. She's suddenly filled with discouraging thoughts, "what if this isn't for me? What if my boss is some kind of ogre determined to run me out of the ministry?" She momentarily hesitates as she approaches the Ministry of Regional Development (MoRD), a greyish socialist era building that while not in a state of total disrepair, has undoubtedly seen better days. It is mid-July in Sofia and the sweltering summer heat makes the city's humidity almost unbearable. As Tsvety raises her eyes, taking in the enormity of the building she notices all the individual air conditioning units lining the windows of the ministry, glinting in the sunlight and struggling to keep their human patrons comfortable indoors. There's no turning back now.

Tsvety is a recent law graduate from Sofia University, Bulgaria's oldest and perhaps most prestigious institution for higher education. She was recruited by the MoRD's Inspectorate Department and while she competed and was subsequently offered the position based on merit, her uncle's close ties with the director of human resources might have helped.

As part of the ministry's inspectorate unit, Tsvety and her colleagues are tasked with investigating any irregularities in the public procurement process and are responsible for ensuring that the public procurement law is being upheld. This includes overseeing the work carried out by the Public Procurement Agency. Months go by and Tsvety begins to realize that there is little in the way to investigate. This is a reality that doesn't mesh well with her understanding of how the Bulgarian government works. With little to do, Tsvety retreats to the ministry's basement and into the archives. Wandering around the ministry's archives proves to be an eerie experience. It's a space seemingly devoid of any life, it's as though the archive has been completely forgotten by the rest of the ministry. There are rows and rows of grey filing cabinets, one just as nondescript as the next. Tsvety stops at one marked 2012, pulls the drawer open and sees a folder haphazardly heaped on top of the rest of the files. Picking up the folder it is labeled "Dunav Highway Tender." She opens the folder and is immediately met with an article written by **Petar Dobrev**, a young up-and-coming journalist known to Tsvety for being particularly critical of the centre-right GERB party.

The article, published in the Vratza regional newspaper "Utro" or "Morning" is dated March 7, 2012 and is entitled "Corruption Milestones on the Dunav Highway" – the stretch of highway linking Vratza and Vidin. Years ago, a public tender had been issued for its construction. The article alleges that the MoRD, along with a Greek construction company called **Midos** were complicit in bid rigging and corrupt practices. The article goes on to state that although the public tender procedure was formally observed, the terms of the contract were so utterly disadvantageous to the Bulgarian tender that the awarding of the tender must have been vitiated. The article also suggests that there were misappropriations of EU funding, therefore indicating that kickbacks, or other benefits, were given to public officials. Given the allocation of EU funding, Dobrev also assumes that corrupt practices took place with international participation. Supporting Dobrev's claims is the fact that a similar stretch of highway between the Greek cities of Komotini and Thessaloniki had been built two years earlier by the same company at an average price per kilometer of about 60% of the price contracted by the Bulgarian tenderer. Compounding matters more is the fact that labour and building materials are 30-50%

cheaper in Bulgaria than in Greece, thus raising additional doubts as to the actual cost of the highway's construction.

The article also discloses an interesting connection between the procurement commission which was nominated by the MoRD and its decision to hire the company **Vassilev LLC** as a consultant. Its owner, Dragan Vassilev, had worked for five years as an expert on road construction projects financed by the Greek bank **Pelagos**. Pelagos was the mediator and guarantor of EU payments on the project. The bank has a few branches in Bulgaria and had reportedly bought assets in some Bulgarian banks. At the beginning of 2010, Vassilev left the bank for undisclosed reasons and registered a separate LLC for consulting services in the field of road construction financing. Vassilev is well known for his expertise and is often contracted by national and foreign public offices and credit institutions. Construction of the Vratza – Vidin stretch of highway is co-funded by the EU operational program “Transport” while the Bulgarian MoRD is to co-finance 20% of the project's expenses.

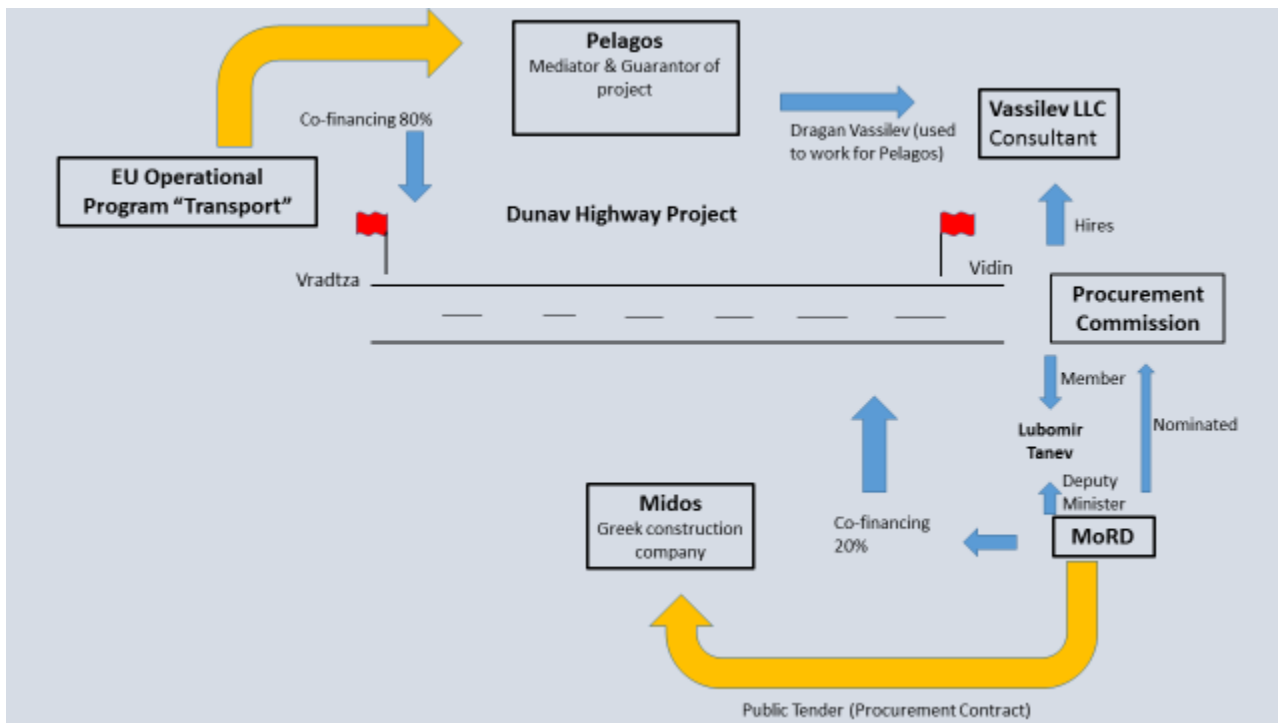
As part of Dobrev's final salvo aimed at the current government, he paints a bigger picture of the alleged transgressions. The project is of a considerable value, with the largest contribution of funding being allocated by the EU. As a result, Dobrev finds it disconcerting that the management of the procurement commission took the decision to include the MoRD Deputy Minister, Lubomir Tanev in the commission, particularly as the Deputy Minister's brother, Kiril Tanev, has been the country's Consul-General in Thessaloniki since 2006. To Dobrev, this suggests a conflict of interest. Incidentally, Kiril Tanev's children are undergraduate university students in the United States and are also recipients of Pelagos scholarships.

Stage II:

Aghast by the contents of Petar Dobrev's article and the absence of any formal investigation into the alleged transgressions, Tsvety removes the folder from the archives and heads to the copier room. Fearing possible reprisals and as a means to protect herself, she decides to make copies of the documents she has uncovered and take them home with her. This is an investigation that will have to be handled delicately and discreetly. Spending time on it in earnest would require conducting the investigation outside of the office and from her home. Tsvety could easily let this go and choose not to dig deeper on this case but she feels morally compelled to investigate the matter further.

Upon arriving home, Tsvety begins assembling the facts of the case on a bulletin board. The diagram below (Figure 1) shows what connections she has made given the information currently available.

Figure 1: Connections among the participants in the Dunav Highway project



Looking for answers, she begins by going back and reviewing the documentation related to the procurement procedure for the Vratza-Vidin section of highway.

The earliest documentation on the file comes in the form of two press releases. One was issued by the MoRD while the other was posted by the Public Procurement Agency's website on January 30th, 2010. Both press releases state the intention of the public tender entity (MoRD) in initiating a procurement procedure.

Sifting through the various documents in the folder, Tsvety learns that the decision to open the public procurement procedure was taken on September 2nd, 2010. The MoRD deemed a "Restricted Procedure" classification (section six of the Public Procurement Law) as the most appropriate means to conduct the tender. As a result, only five candidates would be invited and nominated according to a pre-disclosed selection criteria provided by the commission. The invitation to tender noted that bids would be assessed against the criterion of the economically most advantageous bid and on the basis of four awarding criteria with equal relative weighing:

- (1) price,
- (2) utilization of Bulgarian building materials and labour,
- (3) period for project completion, and
- (4) period of warranty for the surface layer of asphalt pavement.

The latter, should not be for a period of less than 10 years. The project is to be completed within a maximum time frame of **three years**.

Among the other documents provided in the invitation to tender, Tsvety finds a draft of the award contract. In it, a requirement imposed by the MoRD asks for candidates to submit proof of their economic, financial, technical equipment, personnel capabilities and official annual financial statements (balance sheet and/or profit and loss account) for the last two years. Additionally, the procurement entity requested references that indicated experience in the construction of roadbeds and road facilities. Candidates were also required to have not been subject to a judicial ruling that had established non-compliance of a public tender contract and had not been sanctioned for the illegal hire of immigrants. Proof of registration in some of the professional or trade registers in the residual state, or in its absence, a signed declaration would also be required by candidates. The financial guarantee for participation was fixed at 500,000 Euro and 1.3 million Euro for contract completion. The bid validity would last for a period of no less than three months.

Following the invitation to tender and award contract draft, Tsvety comes across two newspaper clippings announcing the procurement call, one national and one local. Accompanying the press clippings is an email that was sent to the Official Journal of the European Communities informing the journal of the procurement call. In a separate email addressed to the Public Procurement Agency, the tendering entity defends its use of a “Restricted Procedure” as opposed to an “Open Procedure”, along with the approved methodology it used for the bid assessment and the call draft. A subsequent email sent by the PPA to the MoRD did not contest the procedure or the approach used in the tendering procedure, nor did it offer any recommendations. This letter simply agreed with the deadline for candidates’ submission of documents, which was consistent with the Public Procurement Law provisions and stated that the option to shorten the deadline period was deemed unnecessary by the PPA. There was no record of anyone, candidates or government departments, contesting the requirements or the awarding criteria. Contenders were not obligated to sign a “Declaration of Fair Competition” in where they could declare non-collusion amongst them, as it does not exist in Bulgarian legislation and were never mentioned in the tenderer’s call as a requirement.

A separate document by the MoRD detailed the **five** construction companies nominated during the pre-selection stage. Two were Bulgarian companies; **Barge (A)**, with residual registration in the city of Pleven and **Firststroy (B)**, with residual registration in Vidin. These national companies were complemented by **Baum (C)**, an Austrian company based in Graz, a Macedonian **Tetovostroy (D)**, with residual registration in the offshore zone of Cyprus and a Greek company, **Midos (E)**, with its headquarters in Thessaloniki, Greece. Other companies not nominated for final consideration were notified by the tendering commission's decision by way of letter. Only one company issued a claim against the selection decision before the Commission for Protection of Competition.. The subsequent ruling by the Commission for Protection of Competition stated that the company's demands and arguments **were unfounded**. Consequently, its decision was not appealed before the Administrative Court.

In its final invitation to submit bids, the MoRD's tendering commission requested, along with price quotes, receipt of certified photocopies of contracts for road work projects carried out over the last five years. Construction work on these projects should have been completed within the last ten years. These documents were to be signed, notarized and should include no fewer than three references.

Early on in the bid selection stage, Tsvety learns that the Commission **had rejected** two candidates as non-responsive – **Firststroy** and **Tetovostroy**. In the case of **Firststroy**, this conclusion was reached after a formal request had been issued for the company's credit liabilities to Cristalbank. On October 18, 2010, Cristalbank had replied that its client had at that time credit defaults (non-performing loans) – principal plus interest -- amounting to around 4 million Bulgarian Leva (2 million Euro). The bank subsequently warned that if **Firststroy** did not commence debt repayment by the end of the year, it would file a motion with the court to declare the company insolvent.

What Tsvety finds especially perplexing is how the tendering commission was able to obtain sensitive credit information on Firststroy from Cristalbank and why Cristalbank obliged the request to divulge information on its client's finances. Does this not suggest some kind of collusion between actors? What does not make sense to Tsvety, however, is that in spite of all the financial turmoil, **Firststroy** declared assets (which included real estate property and equipment) of more than 15 million Bulgarian Leva (7.5 million Euro) on its balance sheet. Stranger still is that in **Firststroy's** bid, its quoted price for the project was 25% lower than that of the Greek company **Midos** – the eventual public procurement winner. In its bid, **Firststroy** attributes its lower price to its ownership of a quarry and asphalt plant in the village of Banovo, which is located in the middle of the

highway section under construction. Due to the region's high unemployment, **Firststroy** claimed it would be able to recruit labour with remuneration bordering on what was agreed on in the collective work contract with the branch trade unions.

The final reason citing **Firststroy's** disqualification comes as a result of its non-compliance with the tendering commissions request that the company submit photocopies of contracts for similar road construction projects over the last five years. The company failed to comply with this request and instead only provided a list of similar projects with a few details on them. Having read all the documentation as to why **Firststroy's** bid was disqualified, Tsvety leans back in her chair and begins examining the tiles of her apartment's ceiling. She wonders why they are dotted with tiny holes. Her mind quickly turns to back to the tender. If **Firststroy** failed to fulfill the Commission's demands with regards to providing all the proper documentation and was therefore disqualified, how did the Commission learn of their bid price? According to article 69a and 82 of the Public Tender Legal Act, if the tender commission disqualifies a company under the auspices of its "first envelope" which includes details on the technical performance bid and other documents related to the company's activities, the Commission is legally not allowed to open the "second envelope" which includes the price bid.⁷ With regard to Firststroy's bid, proper protocols were not used. It also seems strange that Firststroy could not provide the basic requirements in the "first envelope" like information on previous projects. Could this be chalked up to an amateurish mistake? Also, why did the Commission not do more to support the company's bid if its quoted price was 25% lower than the winner and would create jobs for a region of the country struggling with high unemployment? Shouldn't there be more consideration for a Bulgarian owned and operated company?

With the sun going down behind her and with what's left of the daylight struggling to find its way into her dimly lit apartment, Tsvety turns on her desk lamp. "I might be up late tonight" she thinks to herself. As she rifles through the stacks of documents now teetering precariously high on the corner of her desk she begins her search for information on the Macedonian company **Tetovostroy** and its disqualification from the tender. After a few minutes of sifting through files she finds what she was looking for. A MoRD document had disqualified **Tetovostroy** under the auspices that the company offered insufficient justification for its building materials and labour prices. Given that the price offered was 40% less than average price quoted by **Midos**, **Baum** and **Barge**, the Commission

⁷ See the Bulgarian Procurement Act, available online at: <http://www.mi.government.bg/en/library/public-procurement-act-357-c25-m258-1.html>

requested a breakdown of prices by operation. The company was given five days to provide the specifics and followed through with the request but the quoted price was still deemed unrealistic by the Commission. The company also did itself no favours by not designating subcontractors or material suppliers that would enable the Commission to assess the extent of the project's feasibility within the prices quoted. Compounding problems further for **Tetovostroy** was the fact that according to annual audit report from 2009, it was clear to the Commission that the company did not have the necessary construction machinery and would therefore have to lease it. **Tetovostroy's** bid had guaranteed a warranty of 10 years for the surface layer of asphalt and had envisioned a construction period of two years. Unlike **Firststroy**, **Tetovostroy** had submitted copies of contracts and references for previous road work projects in the last five years – a 20km section of the Skopje – Kumanovo, a 60km section of Prizren – Orjahovo and a 16km section from Obilic to Lazarevo.

Attached to the statement by the Commission detailing **Tetovostroy's** disqualification was a letter sent by the Bulgarian Ministry of Foreign Affairs with an attached photocopy of an article published in the Kosovo newspaper “Bota sot”, claimed that the company allegedly laundered the Albanian mafia's drug money. Ekrem Rama, the majority owner of the company was sentenced by the then Yugoslav court to five years in prison in 1995 for drug trafficking to Western Europe. Having served his time, Rama settled in Flora, Albania and has used his significant financial influence to support politicians in Kosovo. Rama is the main sponsor of the Liberal-Democrat Party leader in Kosovo, Hasim Taci. The “Bota sot” article was discovered and submitted to the Bulgarian Ministry of Foreign Affairs by the political officer at the Bulgarian embassy in Pristina.

After reading all the documentation on **Tetovostroy**, a sense of relief rushes over Tsvety. She can't help but think that the handling of this bid could not have gone better. Cooperation like this between ministries is rare and sharing information is not as commonplace as it ought to be. Nevertheless, she wondered – why is it that the MoFA was so meticulous? The rejection of the company's tender by pooling information together should act as a blueprint going forward, she thinks to herself.

Having familiarized herself with the reason for two bids dismissal, Tsvety turns to the final ranking of the remaining bidders and notes the following:

In first place is the Greek company, **Midos**. The reasons for the decision can be attributed to a good business and professional profile, the submitted recommendations for completed projects in the field of road construction projects; the relatively good overall

justification for the project completion and price affordability – the bid is a little bit lower than those of the other two. The warranty for surface layer of asphalt pavement is 10 years, which is the norm according to Bulgarian and European standards. The period for highway construction completion is fixed at two years. While the subcontractors and materials suppliers are not specified, it is the company's intent to find them among Bulgarian companies. The most persuasive reason for choosing **Midos** came in the form of a recommendation from Directorate F of the General Community Directorate of the European Commission which is responsible for controlling and auditing the spending of funds in the "Transport" program. In its recommendation, Directorate F noted that **Midos** had completed similar projects in different EU countries and had not received any claims for poor quality, nor had there been any record of irregularities. Directorate F did explicitly note in its letter however that while its recommendations were advisable, they were not compulsory. The EC institution went on to suggest that payment be made through the Greek bank Pelagos, which had the capacity to exert supervision on the road construction process and was viewed as financially stable and reliable. The Bank was also the guarantor for EU financing. As an additional argument in support of its recommendation for **Midos**, the Directorate noted the perfect performance of the tandem (Pelagos – **Midos**) in other EU projects.

In second place was the Austrian company, **Baum**. Its general construction price was about 10% higher than that of **Midos**, but lower by 5% than the one submitted by **Barge**. As grounds for the price increase, **Baum** pointed out the necessity to supply asphalt from its plant in the Serbian town of Zajcar, which would be of better quality. This part of its offer was backed up by the claim that the building materials made in Bulgaria would be unable to guarantee the standard 10-year warranty for a surface layer of asphalt pavement. In addition to the official documents, numerous professional and scholarly articles (in Bulgarian, German and English) are attached that supported the company's assertion. By working with materials supplied from Zajcar, **Baum** would be able to provide a warranty for a minimum of 20 years. The relatively higher price was also justified under the auspices of recruiting specialists from Austria in specific categories who have significant experience in road construction and are familiar with the European standards and technologies. Given these competencies, **Baum** could guarantee a much higher quality of asphalt pavement. The high quality asphalt pavement "know-how" is considered a company secret, known only to the company staff. Consequently, assuring the long-term warranty would be predicated on combining the technical characteristics of the materials produced in Zajcar and the new technology, which is patented by **Baum**.

Additionally, **Baum** would be required to pay an import duty tax for the asphalt to Bulgaria, as Serbia is not an EU member state, which would further raise costs. The period for highway construction completion is fixed at 2.5 years, with the possibility of quicker construction, depending on winter weather conditions.

The company, **Barge**, registered in the town of Pleven, Bulgaria, was awarded third place. Its offered price was about 15% higher than **Midos'** and the proposed warranty for the surface layer of asphalt pavement was placed at 10 years. The price increase would be attributed to the transport expenses for road construction materials from its base in the village of Gorna Mitropolia, in the Pleven region (approximately 150 km. away from the place of the construction works). **Barge** guarantees the construction will be completed with exclusively Bulgarian material and labour, drawing from the regions of Pleven and Lovech, where unemployment is particularly high. The period for highway construction completion is fixed at 2 years. The company has huge construction machinery potential, of which more than 70% is unexploited. In the bid, its productivity gains, calculated in the lump sum are about 50% of its competitors.

As far as Tsvety can tell from the various records, **none** of the nominated or disqualified bidders **contested** the Commission's final decision before the Commission for the Protection of Competition or the Administrative Court. With no contestation, the final award contract, designating **Midos** for project implementation, was concluded on December 12, 2010. Before the announcement, the tender entity published a notice of voluntary transparency in both the Registry of Public Tenders and the Official Journal of the European Communities. On December 17, 2010 the Public Procurement Agency was informed by letter about the contract. On the same day, a copy of the public tendering commission's decision on the various bidders was sent to the European commission. A working group of 5 professional experts (4 from the MoRD and one from the Public Procurement Agency) were nominated to carry out checks on project implementation. The inspections were conducted on a weekly basis. The reports indicated that project implementation went according to the presented plan, with no serious deviations from the approved technical construction design. At the beginning of March 2011, the Public Financial Inspection Agency by the Ministry of Finance performed an audit on the initial spending on the project but did not find irregularities.

For Tsvety, there are two aspects about the procurement process that stand out and need answering – **Firststroy's** unusual bid and subsequent disqualification and the composition of the Public Procurement Commission. Perhaps with a better

understanding of who was picked to sit on the commission, **Firststroy's** disqualification will make more sense, she thinks to herself. Determining who comprised the Public Procurement Commission is easily found through the MoRD's records. The Commission included 5 members – a representative from the Ministry of Economics, one representative from the Ministry of Transport, the MoRD's Legal Department Director and the MoRD's Deputy Minister, Lubomir Tanev accounted for the government officials. Deputy Minister Tanev is a member of the United Centre Party, which is part of the governing coalition. The coalition enjoys large electoral support from the populace in the Vratza and Vidin regions, where unemployment has remained stubbornly high. The United Centre party has a good relationship with the ruling party in Greece and their representatives in the European Parliament, with the two parties both members of the same faction in the European Parliament. The Deputy Minister Tanev contracted, as its consultant, Vassilev Ltd. Before the bid's opening session, the commission members were briefed by an expert from the Public Procurement Agency about their rights and obligations. All commission members were forced to sign a statement ensuring that they would not provide outside parties with any information pertaining to bid details which were considered confidential. Tsvety can find no record of Deputy Minister Tanev or Vassilev submitting a declaration for a "conflict of interest."

Having a better understanding for the composition of the Public Procurement Commission, Tsvety turns her attention to **Firststroy's** bid disqualification. She decides to investigate by checking with the Commission for Protection of Competition (CPP). After an exhaustive bureaucratic process, Tsvety finally manages to obtain the files on tender. To her amazement, she finds information alleging collusive negotiations between the Greek company, **Midos** and **Firststroy**. The allegations came in the form of an anonymous letter, with the author claiming that in the beginning of September 2010, representatives from both companies met in Sofia in an effort to coordinate their activities related to the upcoming MoRD tender. As part of these negotiations, **Midos** proposed becoming the guarantor of **Firststroy's** debt to Cristalbank, thus avoiding bankruptcy. In exchange, the Bulgarian company would apply for the public tender award but at bid proposals and, more importantly, prices indicated by **Midos**. Additionally, **Firststroy** was promised that if **Midos** was awarded the contract, they would be given some of the construction works to complete. During the course of these negotiations several options for potential cooperation were discussed. In the end, however, the negotiations failed because **Firststroy's** management board deemed the provisions utterly disadvantageous for the company. The author of the anonymous letter went on to claim

that Deputy Minister Tanev had initiated the talks before taking office in the current government.

A closer inspection of CPP documents revealed that none of the tendering commission members reported “a suspicion of collusion or coordinated practices amongst the candidates” according to the requirement of the Protection of Competition Act. The **Commission for Protection of Competition** [hereinafter “CPP”] did not file a case, nor did it open an administrative procedure for inquiry due to the lack of real claimant. The records that Tsvety managed to pry from CPP bureaucrats showed that the CPP only sent a letter for information to the MoRD and with it, the copy of the anonymous statement alleging the private negotiations between **Midos**, **Firststroy** and Deputy Minister Tanev’s involvement. Again, much to Tsvety’s disbelief, **no answer** was received by the MoRD.

Supporting documents detail personal interviews that were conducted by the Inspectorate Division of the MoRD. These interviews had been carried out by one of Tsvety’s predecessors who had since retired. The personal interviews were carried out with each of the tendering commission members, but they too did not yield any results. Tsvety’s predecessor had not detected any indication of collusion in the tender’s provisions or in any of the candidates’ bids. All commission members flatly refused any interference, recommendations or pressure with regards to how to vote for the bids.

Tsvety can simply not understand how her predecessor, or anyone for that matter, could not see the obvious conflict of interest of including Deputy Minister Tanev in the procurement process, particularly given his previous involvement in negotiations between **Midos** and **Firststroy**. It is painfully obvious to Tsvety that Deputy Minister Tanev’s former business interests guided his actions and were instrumental in **Midos’** awarding of the contract. The question remains, however, to what extent is Deputy Minister Tanev’s personal network, which includes his brother and his ties to Pelagos, responsible for interfering in the public procurement process? Perhaps looking elsewhere will yield fresh insights.

Having closely examined the companies competing for the tender and composition of the tendering commission, Tsvety decides to now concentrate her efforts on some of the banks involved in the procurement process. The role played by the banks in the procurement process is one that she has thus far neglected to investigate. As the construction companies are dependent on banks for financing and given the key

relationship between **Midos** and Pelagos in previous EU projects, it seems worthwhile for Tsvety to take a closer look at any possible relationship between the construction companies and the banks. One of the tools at her disposal in acquiring information on regional bank activities is a database known as “BIBA” or Bank Interests Balkan Analysis. BIBA found that the Greek bank Pelagos had purchased stakes in Bulgarian banks as follows: in September of 2009, 16% in Rila Bank, in January 2010, 22% in Cristalbank and in December of 2010, 8% in Balkan bank. In all these instances, the Commission for Protection of Competition approved the deals. Two of these banks, Rila and Cristal, Tsvety is already familiar with as they are publically known to have serious problems with their solvency.

Tsvety is far less familiar with the Greek bank, Pelagos but soon discovers from various sources that the bank has increased its global profile and market share considerably over the last few years and maintains a presence in more than 56 countries, on five continents. Its capital amounts to more than 30 billion euro and it holds shares in more than 200 banks. Part of its assets comes from investments in French, German, Spanish and Italian pension funds. This is to ensure that the governments of those countries watch its financial state carefully. Due to its popularity, the Pelagos share prices raise continuously. The bank is the guarantor and broker for payments on about half of the infrastructural projects financed by the EU. Its management director, Georgios Stamatakis, is a former Greek Minister of economics between 2002 and 2006. His wife Elefteria Stamatakis is Deputy Minister of Ecology in the current government and was the former press secretary of the ruling party.

Further digging on Pelagos and its dealings in Bulgaria by Tsvety reveals some potentially damning information. An asset declaration provided by the Personnel Department at the Ministry of Foreign Affairs dated 2010 shows that Kiril Tanev (Lubomir Tanev’s brother and Consul-General in Thessaloniki) signed a contract with Pelagos for crediting the living expenses of his son and daughter, both of which were studying in the US. Kiril Tanev’s daughter had also committed to a one year traineeship at a Pelagos bank branch in Albany, New York. The contracted credit amount was \$25,000 USD and the agreement was signed according to the general conditions of the bank for a period of 10 years.

Stage III

With having seemingly exhausted all the available documentation on this case, the only stone left unturned at this point is getting in contact with Petar Dobrev, the young journalist who broke the story of alleged corruption in the tendering process. Getting a hold of Petar proves surprisingly easy, especially in comparison to all the other bureaucratic hurdles Tsvety's been forced to endure thus far. It turns out that they share a few mutual acquaintances from their respective days at Sofia University and a former classmate of Tsvety's was at one time, romantically involved with Petar. After reaching Petar over the phone, they decide to meet for coffee at Café Laguna, a cozy café on Hristo Belchev Street in the middle of the city centre. After exchanging pleasantries and a bit of small talk, they delve into the case. Petar discloses the fact that he had initially received information on the prices for the highway section of Komotini to Thessaloniki from his Greek colleague, Georgios Fotos, a journalist with the centre-left newspaper Ethnos. Georgios, in his 50's, has over 20 years of professional experience and has built a career by focusing on corruption at the top level of political management. In 2008, he was awarded by the International Association of Journalists for the best journalistic inquiry. In a somewhat hushed tone, Petar tells Tsvety that Georgios Fotos had exposed the current Greek government for accepting illegal financial support from Pelagos bank to support its candidates for the European Parliament elections in the summer of 2010. Fotos' article was then published in Ethnos and created a significant uproar. A subsequent Greek Parliamentary Commission investigated the allegations but shockingly, failed to prove that the case constituted political corruption. As a result, Fotos' findings were neither shared nor submitted to the public prosecutor.

It was during Fotos' research on Pelagos' illegal financing of party candidates that he stumbled across information related to the construction of the Komotini – Thessaloniki highway section, which was co-financed by the EU and **Midos** in 2007. At the end of February 2010, Fotos had learned that **Midos**, following the public procurement procedure, had won the rights to build the Vratza – Vidin stretch of highway. It was then, Petar explained, that he was contacted by Fotos to find out under what conditions its bid was awarded. Petar went on to state that Fotos also had information that Pelagos had purchased shares in Bulgarian banks but that he did not specifically which Bulgarian banks were involved.

With this information in hand, Petar Dobrev approached the Public Procurement Agency under the auspices of the Access to Public Information Act (art.4). While Petar was not granted access to some of the documents, considered by the tendering commission as

confidential, he did become familiar with the prices for the highway construction and compared them to those of the project completed in Greece.

When Tsvety asked Petar to verify the allegations involving Pelagos and Bulgaria's Consul-General in Thessaloniki, Petar explained that another Bulgarian official at the Consulate had leaked this information to Fotos in an off-the-record conversation. This official verified that Kiril Tanev had in fact sent his children to universities in the US and that they had been sponsored by Pelagos. Petar went on to say that Georgios Fotos had met many people of influence through his connections at the Bulgarian Consulate in Thessaloniki, including Dimitri Vassilev, who he had met when Vassilev still worked for Pelagos.

On the issue of Dimitri Vassilev, Petar said that there was little coincidence that Vassilev's company had found itself on the Public Procurement Agency's roster of professional entities from which tendering institutions could contract as external consultants in the run-up for carrying out public tenders. Consequently, Vassilev's company was chosen on the recommendation of Deputy Minister of the MoRD, Lubomir Tanev. His recommendation was taken seriously by Public Procurement Agency's Director, Nikolai Valov, who was a former classmate of Lubomir Tanev and from the same town.

More interesting still, when Petar checked the register of the Public Procurement Agency, he discovered an anonymous letter claiming that on January 17th 2011, **Midos** had purchased 60% of **Firststroy's** debt owed to Cristalbank and subsequently blackmailed **Firststroy** into signing a contract for the supply of aggregates and asphalt prices approximately 30% lower than the average market price. Again, this time, no action was taken for three reasons. First, the anonymous nature of the letter. Secondly, because of the discrepancy between what was alleged in the letter and the actual contracted provisions made in the transaction documents. Thirdly, it would be impossible to ascertain the veracity of the allegations. The only attempt made at verifying the allegations was through a post-contract control on public procurement performance. It was only discovered then that **Firststroy** had in fact signed a contract for supply materials after the tendering procedure had ended, even though the prices contracted were still within the range of average market prices. The public prosecutor's office was not informed of this issue, nor was there a request for assistance to check the veracity of the allegations.

Furthermore, during the post-contract control on public procurement it was determined that on January 26, 2011 the company **Midos** had signed a contract with the Bulgarian

company **Barge** under the auspices that it was to hire road construction machinery and servicing specialists. The contracted price for the machinery per hour work corresponds to the price fixed in the **Midos** bid.

Having finished her investigation of the alleged complicity in bid rigging and corrupt practices of the Dunav Highway public procurement tender, Tsvety feels an overwhelming sense of exasperation. With so much of the procurement process shrouded in mystery and obvious cases of collusion between powerful actors, Tsvety's sense of self-preservation tells her it would be foolhardy to pursue the matter any further. The culpability between companies, banks and political figures would be simply too much for anyone to contend with, particularly for someone of her pedigree. Tsvety must consider her future and burgeoning professional career. Nonetheless, Tsvety cannot bring herself to be involved in such a system where corrupt practices are committed with impunity. She decides she has no other choice but to resign from her position, effective immediately.

Teaching Notes

Introduction

Instructing students on public procurement corruption requires not only imparting important knowledge on what constitutes corruption but it also necessitates a firm understanding of the cultural, political and legal context in which the corruption takes place. While the main objective of teaching a case study on public procurement corruption is to hone and further cultivate student's analytical skills and knowledge, it will be of limited value if the instructor neglects the national context in where the corruption occurs. The instructor should therefore pay particular attention to the national context and be prepared to answer questions that may arise during the discussions, specifically as it relates to the cultural, political and legal environment. Consequently, what follows below provides some background information on corruption in Bulgaria and may provide some aid to the instructor as they moderate and encourage discussion.

Corruption in Bulgaria

After more than two decades of democratization, corruption remains endemic in Bulgaria. In contrast to the eight other post-communist EU member states that joined the EU earlier, Bulgaria and its neighbour to the north, Romania, are categorized as semi-consolidated democracies by Freedom House.⁸ Bulgaria's ongoing challenge of combating corruption can be partially attributed to its communist past which could be characterized as highly clientelistic and one that benefited from a weak civil society coupled with low levels of industrialization. With the end of communist rule in 1989, politicians, who championed themselves as agents of democratic change, acted quickly to enrich themselves and their inner circles through networks of corruption. As a result, this process of state capture entrenched systematic corruption.⁹

While Bulgaria has undergone significant domestic institutional reform as part of its path towards EU membership and Schengen region ascension, the Corruption Monitoring System, conceived by Coalition 2000 (a multi-stakeholder initiative aimed at combating corruption through a process of cooperation, drafting of an Anti-Corruption Action Plan for Bulgaria, and implementing an awareness campaign and a monitoring system) recorded its highest level of involvement of the Bulgarian population in corruption

⁸ See SIEPS 2012, The EU's Cooperation and Verification Mechanism: Fighting Corruption in Bulgaria and Romania after EU Accession, *available online at*: < http://sieps.se/sites/default/files/2012_1epa%20EN_A4.pdf >

⁹ Ibid.

transactions over the last 15 years in 2014. Over the course of 2014, Bulgarians conceded to being involved in roughly 158,000 corruption transactions a month.¹⁰ Currently, most corruption transactions are initiated by the state administration which exerts corruption pressure on those seeking public services. Consequently, the exceedingly high levels of corruption have made criminal law enforcement initiatives ineffective and inadequate.

It is important to note, however, that Bulgaria's less than impressive record at combating corruption can be somewhat attributed to the adoption of anti-corruption initiatives from outside the country that have failed to work. Such initiatives have been poorly funded, vague and too ambitious. These initiatives have also failed to capture the important cultural subtleties that are present in both local conditions and in the national mentality that help facilitate corruption. Implementation of these programmes by political authorities have also been unsuccessful, as politicians stand to benefit from maintaining the status quo, as opposed to instituting viable anti-corruption reforms.¹¹

The area of public procurement is particularly susceptible to corruption in former Warsaw Pact member states, as public procurement was non-existent during communist times. While examples of corruption between local and foreign business in this area are well documented, less is known about the experiences of corruption among public procurement officials themselves, particularly when there is evidence of corruption within their own ranks. The absence of public procurement during communism has resulted in the adoption of legislation from abroad. With a lack of any experience, public procurement officials have had to undergo extensive training but administering a complex legal framework with legislation that has been imposed from abroad is often fraught with challenges.¹² Chief among these challenges and not directly related to importing legislation designed to curb corruption is the lack of capacity within the civil service. In states like Bulgaria, inadequate legal and institutional traditions are further exacerbated by chronic underfunding and poor pay for civil servants.¹³ This pervasive administrative corruption has enabled political corruption and state capture to continue unabated. Thus,

¹⁰ See CSD 2014, Corruption Assessment Report: Anti-corruption Policies Against State Capture, *available online at*: < <http://www.csd.bg/artShow.php?id=17172> >

¹¹ See Communist and Post-Communist Studies 2011, Fighting corruption in public procurement in post-communist states: Obstacles and solutions, *available online at*: < <http://www.sciencedirect.com/science/article/pii/S0967067X11000055> >

¹² Ibid

¹³ See CSD 2014, Corruption Assessment Report: Anti-corruption Policies Against State Capture, *available online at*: < <http://www.csd.bg/artShow.php?id=17172> >

neutralizing political influence, particularly in the judiciary remains a key challenge in Bulgaria.¹⁴

Case Study Objectives

This case study shows that unfair competition in the public procurement process can often manifest itself in the form of anticompetitive agreements and price fixing between bidders. This disrupts both free market principles and the ethical norms of the relationship between candidates. The case study is designed to show that determining the culpability of business and public servants in undermining the public procurement process requires a wide range of experience and knowledge in law. Knowledge is especially needed in the field of legal regulations governing public procurement procedure, as well as in the area of economics, public and business management, professional, administrative and business ethics, psychology etc. Furthermore, other types of skills are also needed in order to find documents that could be available in various institutions. It is necessary for students to analyze the collected evidence and to compare it to the legal standards. Subsequently, students need to identify both the irregularities and the ways of circumventing the intricacies of a particular law.

Ultimately, fair competition between public procurement bidders is a matter of **business integrity**. The *ad hoc* cartelization, or the collusion of a set of companies, even within the framework of some agreement between them, may benefit some companies but is detrimental to other candidates and to society as a whole. The circumstances that allow for deviation from normative behavior and ethical standards, as well as the measures to overcome practices that are harmful to the public interest are complex in character.

Guidelines

The case study is designed for students in the field of public and/or business administration or law that are at fairly advanced stage of their schooling. It is recommended that the overall case study be completed within the framework of 6 hours. It envisages the combination of two educational approaches: Firstly, individual (independent) work, or work in groups. Secondly, it calls for collective discussions of the proposals and subsequent conclusions. The case study exercise is to be completed in three stages, as the information needed for the subsequent stage is predicated on the completion of the preceding stage. This helps to cultivate the students' research skills of where to look for the documents and evidence needed for the inquiry and analysis, as well as identifying the proper institutions where the required information is kept. The

¹⁴ Ibid

instructor will introduce a set of questions to be answered by students at the end of each stage.

In the **independent (individual) work stage**, students are introduced to the narrative text and the evidence included therein. On the basis of the analysis, they will have to decide what additional information is needed and where they could eventually obtain it. Throughout their process of searching, they acquire knowledge about basic legal acts, both national and EU, that regulate the public procurement process (exercise, performance). It is not a requirement of the case study analysis to review the existing regulation in Bulgaria or the EU, yet students should be in a position to identify the relevant legal documents. In the subsequent research work, they will become familiar with the most frequently occurring deviations from regulatory and ethical standards, as well as with 'good practices', which are instrumental in the prevention of attempts to counter public interest. They will also acquire a better understanding of the institutional and policy environment in which public procurement processes take place.

Through the **discussions**, students acquire skills to present their opinions on the topics and to put forward a reasoned defense of their own views. In addition, this method helps to educate them to tolerate the positions of others, even when they differ from their own. As a result, students gain insight into the arguments which support their opponent's standpoint. Subsequently, they may choose to accept a rival position, or it may urge them to strive to find some additional data that would disprove it. This brain-storming provides students with the opportunity to mutually complement their arguments or to define them more precisely, through which a common solution could finally be reached. Moreover, students should be in a position to understand where the red flags lie and where the possible conflicts of interests are in the relationship cobweb.

The **instructor's role** will be that of a mediator in the discussion. He/she could suggest some sources of information that students could have recourse to, voice provocative opinions and encourage students to express and defend their arguments on the case.

In the process of considering and solving the case and especially in the process of discussions, students are imbued with the basic guidelines of public and business integrity that could turn into a robust and formative methodological experience, which later-on could be useful to them in effectively coping with the real day-to-day life dilemmas.

Access to the internet, multimedia and flipchart are required to perform the case study tasks.

Case Study Questions

Questions for the students within the three stages:

First Stage Tasks:

1. Given the information provided in stage I, assess the level of corruption risk and indicate which relationships and for what reason might raise red flags?
2. If you were Tsvety, what would you have done?
3. What would you consider to be a conflict of interest?

Second Stage Tasks:

1. Is the procurement procedure properly conducted? From a legal perspective and including your rationale, give your reasons for and against.
2. Had it not been a public tender, but a private call for cooperation, which of the companies would you have chosen – and why?
3. What is the purpose of the Declaration of Fair Competition?
4. Does the tendering commission's selection, awarding criteria and other documents meet the national legal provisions and EU standards? Are any of the tendering commission's requirements discriminatory?
5. Were the companies Firststroy and Tetovostroy rightly rejected as non-responsive bidders?
6. Has the Commission for Protection of Competition reacted adequately to the anonymous letter?

7. Did Tsvety proceed correctly? Would you have done anything differently?
8. Was it necessary for engineer, D. Vassilev and the Procurement Commission member, Lubomir Tanev. (MoRD Deputy Minister) to submit a “conflict of interest” declaration?
9. Which facts and events do you consider to be red flags?
10. If you were Tsvety, would you take the materials home from your office?

Note: When giving answers, please refer to Bulgarian and EU legal acts.

Third Stage Tasks:

11. Has the Public Procurement Agency reacted adequately to the anonymous letter?
12. Are there indications of collusion between the companies bidding for the public tender?
13. Are there indications of corrupt practices?
14. How do you assess the business integrity in the behaviour of Baum, Midos and Pelagos?
15. How do you assess the professional integrity in the behavior of the two journalists? Should they reveal their sources and under what grounds?
16. What is the difference between corruption and nepotism?

Concluding remarks – evaluating performance and emphasizing takeaways

While the case study is complex in nature and may not offer obvious examples of corrupt acts, students are expected to think critically to uncover evidence of wrongdoing. Students should be able to recognize inconsistencies throughout the case and attention should be paid to the dubious track records and actions of companies like Midos. The stage is set early in the case study with the discovery of the 60% price difference in road construction cost by Midos between Vratza and Vidin and the two Greek cities. It should be apparent to students that the discrepancy in cost is cause for suspicion. Furthermore, the subsequent disclosure of various conflicts of interest involving the MoRD, Pelagos, Vassilev and the Tanev brothers should provoke students to ask questions and dig deeper. Upon recognizing and substantiating the reasons why the procurement procedure was improperly handled, the instructor is provided with a suitable basis in which to evaluate student performance.

At the end of the exercise, aside from further cultivating their analytical and research skills, students should be left with the impression that corruption is complex, capable of permeating all sectors and can be committed by a wide array of actors. Corrupt acts can occur both overtly, in plain sight, and surreptitiously, behind closed doors or shrouded in bureaucracy. Consequently, students should be aware that targeting and mitigating the effects of corruption necessitates support from government, civil society and the private sector.

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