Brief 35

Public Procurement

Abnormally Low Tenders

CONTENTS

• Introduction
• Risks related to choosing an abnormally low tender
• How to identify an abnormally low tender
• What the Directive says about abnormally low tenders
• Investigation procedure
• Abnormally low tenders and state aid
• Other issues – Questions and Answers
• Utilities
• Further Information

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Introduction

The activities of public institutions and the decisions made by them should be governed by the pursuit of objectives in the public interest and by the need to spend public funds efficiently. Public procurement decisions and activities are no exception, as a significant part of taxpayers’ money is spent in this way.

In many cases, procurement decisions are made on the basis of the lowest price, which is a permitted award criterion falling within the concept of the “most economically advantageous tender”. Contracting authorities may argue that the least expensive offer ensures the achievement of the important financial goal of budgetary savings.

The lowest price, however, is not always the offer that is the best value for money in the long term. The 2014 Public Sector Directive (the Directive)\(^1\) acknowledges this fact by requiring that “contracting authorities shall base the award of public contracts on the most economically advantageous tender”. The Directive also provides a framework for the use of life-cycle costing and other cost-effectiveness approaches, encouraging contracting authorities to consider more than just the initial purchase price and to take into account qualitative issues in their evaluation of tenders. See SIGMA Public Procurement Brief 8, Setting the Award Criteria, and SIGMA Public Procurement Brief 34, Life-cycle Costing, for further information on these issues.

In the current economic climate, there is often keen competition between economic operators, which submit competitive, low-price bids in order to secure work, retain employment and maintain their presence on the market. Low prices can, potentially, result in significant financial benefits to contracting authorities. It may also be the case that low-priced tenders are “too good to be true” and will be very poor value for money or will not be delivered at all. It is in this context that the concept of “abnormally low tenders” arises.

The Directive contains provisions for dealing with tenders that are suspected of being abnormally low. These rules enable contracting authorities to avoid the negative consequences of accepting a tender that appears extremely advantageous but, in practice, is not viable. In addition to protecting the public interest against the risk of non-performance or poor performance of a contract, these provisions are also aimed at supporting genuine competition between economic operators and reducing unfair advantages. For example, the provisions permit a contracting authority to reject a low-priced tender where the low price is a consequence of illegal support from public funds or from breaches of specific labour, social or environmental laws.

The Directive does not define an “abnormally low tender”. This concept is nevertheless generally recognised as referring to the situation where the price offered by an economic operator raises doubts as to whether the offer is economically sustainable and can be performed properly.

There are various reasons for the appearance of abnormally low tenders in public procurement procedures.

**Misunderstanding or misinterpretation:** The submission of an abnormally low tender may be the result of the economic operator’s misunderstanding or misinterpretation of the requirements of the contracting authority.

For example, Company A may not understand the full scope of the procurement and, as a consequence, it submits a tender that does not include all of the mandatory requirements. Company A’s tender may be for a much lower price than the prices of the tenders of other economic operators, which took into account all of the contracting authority’s requirements in their tendered price.

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In such a case, the price offered seems to be very good, but further investigation shows that the tender is not compliant with the requirements of the contracting authority, as it does not provide for all of the services or works required.

**Underestimation of risks:** The submission of an abnormally low tender can be the result of an underestimation of the risks attached to the execution of the contract. This phenomenon is referred to in economic literature as “the winner’s curse”.

For example, Company B submits a tender that is compliant with all of the requirements of the contracting authority, but in calculating the tendered price Company B was too confident about the cost of executing the contract. There is a risk that Company B may not be able to perform the contract correctly or that it will perform the contract, but with delays or with a product of lower quality.

**Non-compliance with social, labour and environmental laws:** The submission of an abnormally low tender can be the result of non-compliance with binding legal requirements concerning social, labour or environmental law.

For example, if Company C does not pay wages in accordance with legal requirements or does not ensure labour conditions that comply with those regulations, then it has an unfair competitive advantage.

**Subsidy:** The submission of an abnormally low tender may be the consequence of the receipt of a subsidy by the economic operator.

For example, Company D is in receipt of financial support from the government accorded to start-up companies. Company D may be in a position to offer a price that is much lower than those of its competitors, which do not have access to this support. Subsidised companies are allowed to participate in public procurement procedures but, as explained below, their tenders should be rejected if they are abnormally low because of illegal state aid.

**Deliberate strategy of an economic operator:** The submission of an abnormally low tender may represent the deliberate action or strategy of an economic operator.

For example, Company E offers an extremely low price in order to provide continued employment for staff. Company F offers a low price in order to drive competitors out of the market. Company G offers a low price on the assumption that it will be able to agree on future amendments to the contract and increase remuneration by means of negotiation during the execution phase of the contract.

**Risks related to choosing an abnormally low tender**

Awarding a contract to an economic operator that offers an abnormally low tender is hazardous for the contracting authority (and in general for the public interest) for a number of reasons, as follows.

**Default risk:** An abnormally low tender entails a risk of default, particularly in the case of an economic operator that has misunderstood the complexity of the procurement or has not taken into account all of the risks related to the delivery of the object of the procurement. The result could be that the economic operator would be unable to fulfil the contract or would even become insolvent. The contracting authority would then need to re-tender the services or works that the economic operator has failed to deliver. The outcome would be lost time as well as additional administration and costs incurred by the contracting authority.

**Additional charges or price increases:** An economic operator that was chosen on the basis of a very low tender might, in the course of the execution of the contract, seek to charge the contracting authority for extra costs and request increased remuneration. During the execution phase, the economic operator’s bargaining position is often strong. For example, an economic operator may demand additional payments that were not included in the contract.
and threaten to opt out of the contract if the contracting authority does not agree to those additional payments.

**Quality risk:** Another risk is that the goods or services provided will be of a lower quality than they should be according to the terms of the contract. For example, an economic operator that had proposed a very low tender could try to cheat the contracting authority by replacing materials of high quality with less expensive substitutes or by not performing all of the required services.

**Avoidance of social, labour and environmental obligations:** With an abnormally low tender there is also a risk that binding social, labour and environmental regulations will not be correctly applied. For example, the economic operator will try to avoid paying due taxes, minimum wages or social charges. In consequence, the market will be distorted and honest, law-abiding companies will be discouraged from applying for public contracts. In the long term, competition is lowered, as a smaller number of firms take part in procurement procedures, and in turn, prices are inflated.

**How to identify an abnormally low tender**

The Directive neither defines an abnormally low tender nor provides any specific methods of identifying such tenders. The Directive states only that a contracting authority should require explanations from economic operators proposing prices or costs that “appear to be abnormally low in relation to the works, supplies or services”.

In practice, the following methods are often used for the identification of tenders that appear to be abnormally low:

- An analysis of the price (costs) proposed by an economic operator is made in comparison with the object of the procurement.

- A comparison is launched of the tender price with the value of the procurement, as estimated by the contracting authority prior to the procedure. The contracting authority assesses the proportion of deviation of the price from the estimated value.

- A comparison is made of the tender price with the prices proposed in all of the other compliant tenders. The contracting authority assesses either the deviation from the mean price or verifies the extent of the difference between the tenders, or it applies both methods.

- A combination of all or some of the above-mentioned methods is applied.

According to the case law of the Court of Justice of the European Union (CJEU), arithmetical methods can be applied in order to identify abnormally low tenders, but they may not result in the “automatic” exclusion of such tenders\(^2\). The CJEU has made it clear that a contracting authority having received a bid that it suspects to be abnormally low must request an explanation of the bid from the relevant economic operator. The economic operator must have the opportunity to explain why it was able to submit such a tender and cannot be automatically excluded without having had the opportunity to explain the bid in question\(^3\).

In any event, an arithmetical method should be applied cautiously for a number of reasons, as outlined below:

- An arithmetical method may not be very practical for intellectual services, where differences between prices may be significant.

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\(^2\) CJEU, Case C-285/99 Impresa Lombardini.

\(^3\) CJEU, Cases 76/81 Transporoute, C-103/88 Fratelli Costanzo, C-599/10 SAG ELV Slovensko and Others.
• Such a method may be misleading in cases where a very small number of tenders were submitted; some Member States require a minimum number of tenders for the use of this method.

• The average price of tenders used as a reference may be affected by “outliers”. This term refers to very high “courtesy” offers, where an economic operator participates in a procurement procedure for the purpose of attracting the attention of the contracting authority to its existence, but it does not expect to obtain the contract. For this reason, legislation in some Member States excludes such outliers from an average price assessment.

• A significantly lower price may be a genuine and correct price where, for example, some economic operators have colluded in a bid-rigging scheme and have proposed inflated prices, whereas the offer with a significantly lower price has been made by a bidder that is not involved in this scheme.

National solutions concerning the identification of abnormally low tenders

Many Member States do not provide for any specific method for the identification of abnormally low tenders. The contracting authority makes this assessment on a case-by-case basis, taking account of specific circumstances.

Arithmetical methods for the identification of tenders that are suspected to be abnormally low have also been applied in the past in some Member States, for example in Italy, Poland, Portugal, Romania, Slovakia and Slovenia. Those methods are based on a comparison of the tender price with the estimated value of the procurement, the average price of submitted tenders, or differences between the lowest and second lowest tenders.

Italy – the “anomaly threshold”

In Italy, although the price is the only criterion for the award of contracts, the law provides for the investigation of tenders showing deviations from the “anomaly threshold”. Five different methods may be used for the calculation of the anomaly threshold, and the contracting authority determines the one that is to be applied in a specific case by lottery. To avoid the manipulation of prices by bidders, the method of calculation of the anomaly threshold is not revealed in advance.

For example, the contracting authority is obliged to request explanations from all bidders that have submitted tenders with a discount that is equal to or higher than the mean of all discounts proposed in compliant tenders compared to the “base price” (set by the contracting authority), with the exclusion of 10% of the highest and lowest discounts (rounded up to full figures) and increased by the average divergence from the mean of discounts above this average discount.

For example, there are 11 compliant tenders with the following discounts: 8%, 9%, 11%, 13%, 14%, 16%, 17%, 18%, 20%, 21% and 25%. For the purposes of calculation of the average discount, the two lowest discounts – 8% and 9% – and the two highest – 21% and 25% – are set aside (10% of 11 = 1.1; rounded up to a full figure, it becomes 2). The average discount is 15.57%. Four tenders show discounts larger than 15.57%: 16%, 17%, 18% and 20%. Their average deviation from the average discount amounts to 2.18%. The threshold for mandatory investigation (“anomaly threshold”) is then 17.75% (15.57% + 2.18%). In conclusion, the contracting authority will have to request explanations from bidders that proposed the discounts of 18%, 20%, 21% and 25%, since their discounts had discounts

exceeding the “anomaly threshold”.

As the criterion of the most economically advantageous tender is applied, the contracting authority is obliged to request explanations from bidders that obtained, in terms of the price and other award criteria, at least 4/5 of the maximum number of points envisaged in the contract notice. For example, the following criteria are applied in the procurement procedure: the price – maximum of 20 points; the quality – maximum of 20 points, the organisation and qualifications of the team – maximum 20 points; the innovation – maximum of 20 points; and the time frame for execution – maximum of 20 points. The investigation procedure concerns all tenders that obtain at least 16 points for their prices and at least 64 points for all other criteria.

Other Member States do not provide for such sophisticated arithmetical methods.

**Poland**

In Poland, contracting authorities are obliged to require explanations from bidders that submit tenders containing prices that are lower by more than 30% than the estimated value or the average price of all submitted tenders. There is no requirement concerning a minimum number of submitted tenders for this method to be applied.\(^5\)

**Portugal**

In Portugal, a tender is regarded as being abnormally low if its price is lower than the budgeted price set by the contracting authority (“base price”) by the following:

- 40% or more for public works contracts;
- 50% or more for other types of contracts.

The contracting authority may also set different “anomaly thresholds”, but it should provide this information in advance to potential bidders in the tender documents.\(^6\)

**Romania**

In Romania, former procurement regulations provided that a tender would be considered as abnormally low in relation to what was to be performed or provided when the tendered price, excluding VAT, was (a) less than 85% of the estimated value of the contract – if fewer than five valid tenders had been submitted; or (b) less than 85% of the arithmetic average of the price of the submitted tenders, without taking into account the lowest and highest prices proposed – if at least five valid tenders had been submitted.\(^7\) These provisions were deleted when a new Public Procurement Law was adopted in 2016, and the new Law does not envisage an arithmetical criterion for the identification of an abnormally low tender.\(^8\)

**Slovakia**

In Slovakia, a tender is understood as abnormally low if the following conditions have been met:

1) At least three tenders, submitted by qualified bidders, fulfil the requirements of the contracting authority.

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\(^6\) Código dos contratos públicos aprovado pelo Decreto-Lei nº 18/2008, de 29 de janeira, Article 71.

\(^7\) HOTĂRÂRE nr. 925 din 19 iulie 2006 pentru aprobarea normelor de aplicare a prevederilor referitoare la atribuirea contractelor de achiziție publica din Ordonanța de urgenta a Guvernului nr. 34/2006 privind atribuirea contractelor de achiziție publica, a contractelor de concesiune de lucrări publice și a contractelor de concesiune de servicii.

\(^8\) Lege Nr. 98/2016 din 19 mai 2016 privind achizițiile publice.
2) The tender offers a price that is at least 15% lower than the average price of all other offers.

3) The tender offers a price that is at least 10% lower than the second lowest offer.

It is enough to consider the tender abnormally low if conditions (1) and (2) or conditions (1) and (3) are met⁹.

What the Directive says about abnormally low tenders

Contracting authorities are obliged to require economic operators to explain the price or costs proposed in their tenders where those tenders appear to be abnormally low in relation to the works, supplies or services (Article 69 (1) of the Directive).

This means that the contracting authority is not allowed to:

- accept a tender that appears to be abnormally low without having first conducted this investigation;
- reject a tender that appears to be abnormally low without having allowed the bidder to explain the low level of the price or costs.

The Directive stipulates that the explanations required from economic operators may refer “in particular” to the:

- economics of the manufacturing process, services provided or methods of construction;
- technical solutions chosen or any exceptionally favourable conditions available to the tenderer for the supply of the products or services or for the execution of the works;
- originality of the works, supplies or services proposed by the tenderer;
- compliance with obligations deriving from mandatory EU law or from national law that is compatible with EU law in the fields of social, labour or environmental law or international labour law;
- possibility for the tenderer to obtain state aid.

The Directive uses the words “in particular” before listing the possible explanations and therefore the list is not exhaustive. It is nevertheless not purely indicative either. According to the case law of the CJEU, contracting authorities are not allowed to limit the scope of factors or elements to which explanations may relate.

Investigation procedure

The Directive requires the contracting authority to assess the information (explanations) provided by the consulting economic operator.

In accordance with good procurement practice, the contracting authority should set a reasonable time limit for the submission of explanations concerning the low level of the price or costs. The Directive does not specify the minimum time period to be set by the contracting authority. This period is determined by national regulations or jurisprudence, and Member States have different approaches in this regard. For example, Italian provisions require the time period for the submission of explanations to be no shorter than 15 days, whereas French case law confirms that a period as short as four days is sufficient.

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⁹ ZÁKON z 18. novembra 2015 o verejnom obstarávaní a o zmene a doplnení niektorých zákonov, §53 (3).
The Directive does not specify whether the contracting authority may make only one request for information. The wording of the Directive does not preclude requests by contracting authorities for additional information or clarifications if the first explanations provided by the bidder were not sufficiently clear. The details are determined by national laws or by practices in Member States.

**Decisions concerning tenders accepted after conclusion of the investigation process:**
Following the investigation process, the contracting authority must make a decision concerning the tender that was suspected of being abnormally low.

The Directive states that the contracting authority may only reject a tender where the evidence supplied does not satisfactorily account for the low level of the proposed price or costs, taking into account the explanations provided by the economic operator. The contracting authority is only entitled to reject the tender where it has established, following investigation, that the tender is, indeed, abnormally low. If the explanations provided by the economic operator, which the contracting authority has analysed in consultation with that economic operator, show that the price (cost) is genuine, the tender cannot be considered to be abnormally low and cannot be rejected.

If the contracting authority decides to reject a tender on the grounds that it is abnormally low, it is obliged to inform the economic operator of the reasons for the rejection of its tender as rapidly as possible, and in any event within 15 days of receipt of the economic operator’s written request for that information.

The reasons for the rejection of tenders found to be abnormally low should also be included in the individual report on the procurement procedure prepared by the contracting authority.

**Abnormally low tenders and state aid**

One of the explanations for the submission of a tender with a low price or low costs may be that the economic operator benefits from state aid. The Directive provides special rules concerning the rejection of tenders in such cases.

A contracting authority may reject the tender on these grounds alone, but only if the economic operator is unable to prove, at the contracting authority’s request, that the aid it has received was compatible with the internal market. The burden of proof concerning the legality of the aid is on the economic operator.

The contracting authority must set a “sufficient”, i.e. reasonable, time limit for the economic operator to prove that the aid received was lawful state aid. The contracting authority, in consultation with the economic operator concerned, conducts an analysis of compliance with the provisions on state aid. The economic operator must respond within the time limit fixed by the contracting authority.

Furthermore, the contracting authority is obliged to inform the European Commission of the rejection of a tender under these circumstances.

**Questions and Answers**

*Is a contracting authority obliged to reject abnormally low tenders?* The Directive does not state clearly whether the contracting authority is obliged to reject in all cases a tender where the explanations provided by the bidder do not justify the abnormally low price or costs.

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10 Art. 69 (3)
11 Art. 55 (2) b)
12 Art. 84
However, in one specific case the Directive obliges the contracting authority to reject a tender. This case concerns a situation where the contracting authority has established that the tender is abnormally low because it does not comply with “applicable obligations in the fields of environmental, social or labour law established by Union law, national law, national collective agreements” or by provisions of international environmental, social and labour law.

The fact that the Directive emphasises the obligation to reject a tender in this specific case may suggest that in all other cases where the low price/costs is not convincingly explained by the bidder, the contracting authority is not obliged to reject that tender but merely allowed to do so. In other words, it is up to the contracting authority to decide whether to accept such a tender or to reject it.

The national laws of some Member States are explicit in this regard. For example, in Poland and in France contracting authorities are clearly obliged to reject a tender where it has been confirmed that the price is abnormally low. The national laws of other countries reflect the wording of the Directive.

**Is a contracting authority permitted to automatically exclude a tender that is suspected of being abnormally low?**

A contracting authority is prohibited from automatically excluding a tender that appears to be abnormally low. Before excluding such a tender, the contracting authority must first allow the economic operator concerned to explain the low price or costs.

Member States are not permitted to require contracting authorities to automatically reject abnormally low tenders. The prohibition of automatic exclusion applies not only to contracts covered by the Directive but also, in accordance with the case law of the CJEU, to contracts having smaller values but a particular cross-border interest.

The automatic exclusion of tenders that are considered to be abnormally low in the case of contracts of a particular cross-border interest may amount to indirect discrimination. It may be discriminatory because, in practice, it may place economic operators from other Member States at a disadvantage. An economic operator from another Member State may have genuine reasons for the low tender, while the execution of the contract remains viable. The low price or costs may, for example, be due to different cost structures, economies of scale, or a deliberate reduction in profit margins with a view to entering the market.

According to the case law of the CJEU, it may nevertheless be acceptable, in public procurement below the EU financial thresholds, to automatically exclude tenders on the grounds that they are abnormally low. This exclusion is possible, provided that certain conditions are met. First, there must be an unduly large number of tenders. Second, the obligation to undertake a comparative evaluation of such a large number of tenders would exceed the administrative capacity of the contracting authorities. Third, the delay that such an evaluation would entail might jeopardise the implementation of the project.

In such limited circumstances, national or local legislation or even the contracting authorities themselves would be entitled to set a reasonable threshold for the automatic exclusion of abnormally low tenders.

An example of a situation where national legislation would permit this type of approach is found in Italy. The Italian provisions on public procurement allow contracting authorities to automatically reject tenders with prices that are lower than a particular “anomaly threshold”, provided that:

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13 CJEU Case C-147/06 SECAP and Santorso.
• the award criterion is the price only;
• the value of the procurement is below the EU thresholds;
• at least ten tenders were submitted in the procurement procedure.

Is a contracting authority permitted to automatically reject the lowest tender and the highest tender? One of the popular myths of public procurement is the existence in some Member States of a procedure according to which both the lowest priced tender and the highest priced tender are automatically rejected, and the best tender is chosen after evaluating the remaining tenders. This practice is not permitted.

The origin of this myth may be a misconception relating to the use of “anomaly thresholds”, which are set on the basis of the average bidding price. Indeed, according to some national legislation, any tenders involving prices that diverge significantly from the average price are not taken into account when the average price of the submitted tenders is calculated. This practice does not mean, however, that these divergent tenders are “rejected”. They are in fact evaluated, but when the contracting authority calculates the average price of tenders, with a view to identifying tenders that should be further examined due to their divergence from the average price, those tenders are not included in the calculation of the average price (in order to avoid the impact of divergent tenders on the average price).

Another possible explanation of this myth is the application in Italy and Spain in the 1980s and 1990s of the “average price” criterion, where the contract was awarded to the tenderer offering a price that was closest to the average price of all offers. The contract was not awarded to the bidder proposing the lowest or most economically advantageous tender, but to the bidder with the “average” price tender. Such a practice was found to be unlawful by the CJEU.14

Is the concept of an abnormally low tender limited to consideration of the price (costs) only or does it also relate to other factors or award criteria applied by the contracting authority? The Directive refers to “abnormally low tenders” and not to tenders with abnormally low prices (costs). The provisions in the Directive on abnormally low tenders refer specifically to the requirement to investigate “price or costs” that appear to be abnormally low. These provisions do not prohibit, however, the assessment of factors other than price or costs that may indicate that a tender is abnormally low.

There is no express provision stating that the concept of an abnormally low tender cannot be applied to criteria other than the criterion of price. If the contract is awarded to the most economically advantageous tender by applying a range of award criteria in addition to price, then the requirements stemming from provisions on abnormally low tenders apply not only to the price criterion but also to the other criteria used for the evaluation of tenders.

The Directive also permits the contracting authority to set a fixed cost or price, with the result that economic operators compete only with regard to quality criteria. In this situation, the offer may be abnormally low due to exceptionally favourable conditions offered by a tenderer, such as hours of service, duration of the guarantee period, or period of execution of the works or services. The price itself may be not so low as to raise doubts about its “normality”, but the whole tender may be abnormally low in terms of what is offered for the price tendered. In such a case, the explanations sought by the contracting authority do not concern the price itself but what is offered for this price.

The question of whether a tender is abnormally low should be considered with reference to all features of the tender. For example, if an economic operator offers substantially more services for the same or almost the same price as other economic operators offering fewer services, this tender may also be considered as abnormally low. The same applies to a tender with a

14 CJEU Case 274/83 Commission v. Italy.
significantly shorter period of execution of a contract or a smaller number of hours required to deliver a contract.\textsuperscript{15}

**Is a contracting authority permitted to seek explanations from economic operators in advance, for example in the tender documents?** The case law of the CJEU\textsuperscript{16} confirms that a contracting authority may, in order to streamline the procurement process, seek explanations in advance from economic operators concerning low prices (costs). In that case the contracting authority must disclose in advance in the contract notice (or procurement documents) the estimated value (or the “base price”) of the contract. It must also set the financial level below which economic operators that propose lower prices should provide explanations. In that way, the contracting authority may not automatically disqualify low tenders without first analysing the explanations given and allowing economic operators to provide additional clarifications or explanations.

**Utilities**

Article 84 of the Utilities Directive\textsuperscript{17} contains identical provisions to those of the Directive on abnormally low tenders.

\textsuperscript{15} CJEU Case T-495/04 Belfass.
\textsuperscript{16} C-285/99 Impresa Lombardini.
Further information

Publications

Public Procurement Briefs

SIGMA (2016), *Setting the Award Criteria*, Brief 8, OECD Publishing, Paris