



# **PAY AND OTHER SOCIAL CLAUSES IN EUROPEAN PUBLIC PROCUREMENT**

**An overview on regulation and practices with a focus on  
Denmark, Germany, Norway, Switzerland and the United  
Kingdom**

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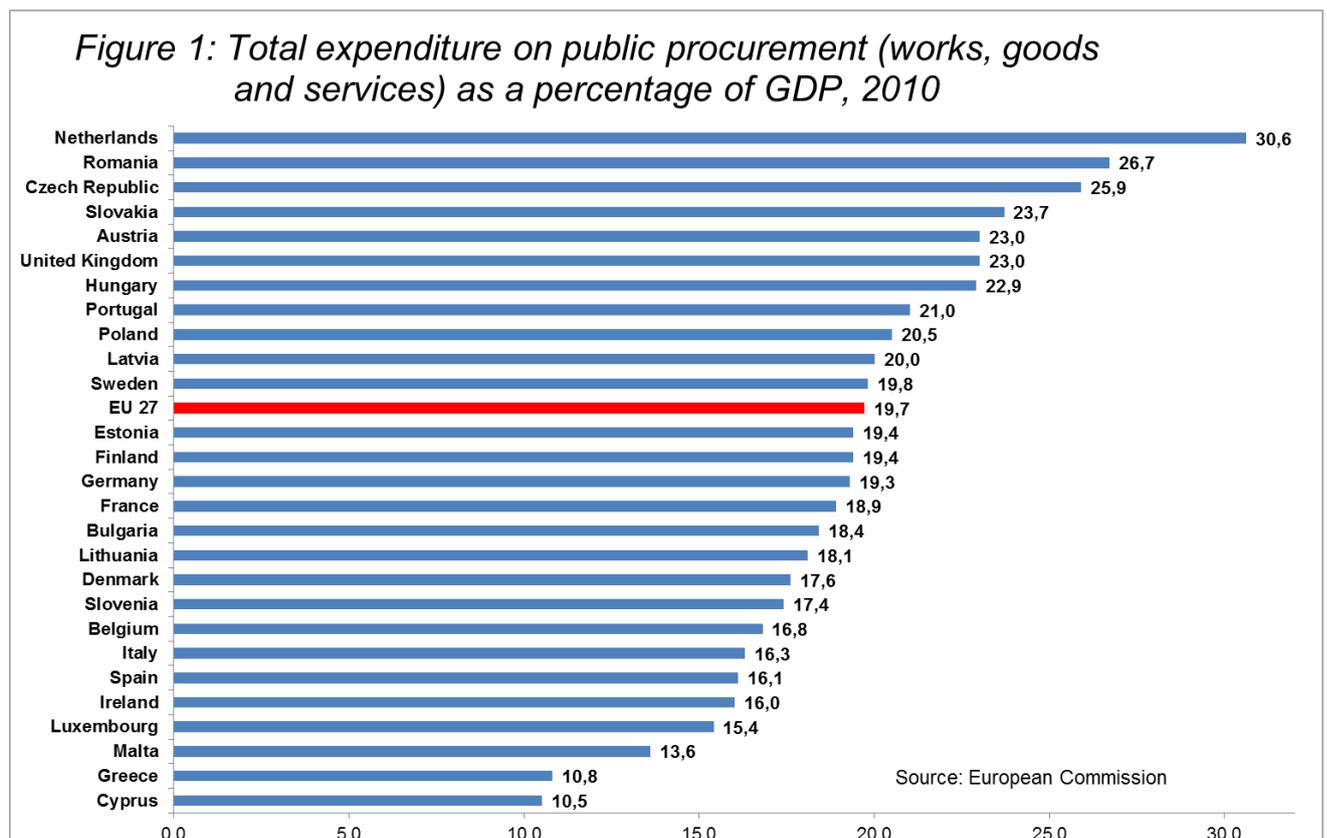
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# 1. Introduction

In 2010, the public sector in the European Union (including public authorities at all levels, state agencies and state-owned enterprises) spent more than 2,400 billion Euros for works, goods and services. This amount corresponds to nearly one fifth (19.7 per cent) of total EU Gross Domestic Product (GDP) varying between 10.5 per cent of GDP in Cyprus and 30.6 per cent in the Netherlands (*Figure 1*). The money is spent by a very large number of more than 250 000 contracting authorities in Europe. In recent years the economic importance of public procurement has even been growing as many European states have followed a policy of liberalisation and privatisation of public services, so that the state no longer provides such services itself directly but purchases them from private companies and other organisations.



The high economic importance of public procurement gives the public sector a significant market power which can be strategically used not only for economic but also for wider social and political purposes. As the European Commission has noticed in its recent evaluation report on the “Impact and Effectiveness of EU Public Procurement Legislation”, there has even been “*growing policy interest in re-orienting public expenditure towards solutions that are more compatible with environmental sustainability, promote social policy considerations, or support innovation*”.<sup>1</sup> Among others, the consideration of social criteria in public contracts becomes more and more acknowledged as a core principle of a modern procurement policy. In practice the development of “socially responsible public procurement” (SRPP) may include a wide range of policy issues such as employment opportunities, decent work, compliance with social and labour rights, social inclusion, and equal opportunities etc.

<sup>1</sup> European Commission, Impact and Effectiveness of EU Public Procurement Legislation - Evaluation Report, Commission Staff Working Paper, SEC (2011) 853 final, Brussels, 27.6.2011, p. IX

This study, which has been carried out on behalf of the European Federation of Public Service Unions (EPSU), will give an overview of the use of social requirements in European public procurement with a special focus on *pay clauses* in public contracts. While in general social considerations are widely accepted, pay clauses have, as yet, played a minor role in the debates on European public procurement policy. This is rather astonishing for many reasons: First of all, labour costs are often – especially in services – the most important cost factor and therefore have a major influence on competition among bidders for public contracts. There has always been a strong incentive for companies to push down labour costs in order to get a competitive advantage in the tender process. Consequently, there is already a long history of pay clauses in public procurement dating back to the late 19<sup>th</sup> century. Such clauses determine certain minimum pay standards in order to avoid downward wage competition. In 1949 the International Labour Organisation (ILO) even adopted a specific Convention on “Labour Clauses in Public Contracts” (Convention No. 94) which aims to ensure that workers hired in contracting companies do not receive less favourable conditions than those laid down in appropriate collective agreements or other forms of pay regulation. More recently, the issue of pay clauses in public procurement finally gained some prominence by the European Court of Justice (EJC). In the so-called Ruffert-Case (C-346/06) in 2008 the EJC took the view that pay clauses in public contracts that refer to local collective agreements which have not been declared to be generally binding, are against EU law, since they contravene the principle of freedom of services.

This study will first give an overview on the use of pay and other social clauses in European public procurement. Afterwards there will follow in-depth case studies of five countries (Denmark, Germany, Norway, Switzerland and the UK) where the use of pay clauses is of some importance in national procurement policy. Finally, the report ends with a concluding chapter discussing the need for a legal clarification on the use of pay clauses in public procurement at European level.

## **2. Pay and other social clauses in public procurement – a European overview**

*Thorsten Schulten*

### **Social requirements in European public procurement**

Considering its significant market power as a public contractor the state has always used public procurement for the promotion of certain social policy outcomes. Early attempts to include social requirements in public procurement can be found already in the mid-19<sup>th</sup> century, in particular in England, France and the United States (McCrudden 2004, 2007). Originally, the social award criteria focused very much on certain working conditions in the contracting companies such as minimum wages, working time and health and safety standards (Kaiserliches Statistisches Amt 1907). The reasons for that were twofold: On the one hand there was a general aim to promote the improvement of working standards, whereby the state wanted to set a positive example. On the other hand there was also already the awareness that certain working conditions have to be guaranteed in order to secure a **frictionless and satisfying** completion of public orders. Considering this, social requirements were seen right from the beginning of modern public procurement not as “procurement alien factors” but as inherent award criteria reflecting the close link between the quality of working conditions and quality of work.

## **Box 2.1: Possible requirements for socially responsible public procurement in the European Union**

### *Employment opportunities:*

- promotion of youth employment;
- promotion of gender balance (e.g. work/life balance, fighting against sectoral and occupational segregation, etc.);
- promotion of employment opportunities for the long-term unemployed and for older workers;
- diversity policies and employment opportunities for persons from disadvantaged groups (e.g. migrant workers, ethnic minorities, religious minorities, people with low educational attainment, etc.);
- promotion of employment opportunities for people with disabilities, including through inclusive and accessible work environments

### *Decent work:*

- compliance with core labour standards;
- decent pay;
- occupational health and safety;
- social dialogue;
- access to training;
- gender equality and non-discrimination;
- access to basic social protection.

### *Compliance with social and labour rights:*

- compliance with national laws and collective agreements that comply with EU law;
- compliance with the principle of equal treatment between women and men, including the principle of equal pay for work of equal value, and promotion of gender equality;
- compliance with occupational health and safety laws;
- fighting discrimination on other grounds (age, disability, race, religion and belief, sexual orientation, etc.) and creating equal opportunities.

### *Social inclusion and promoting social economy organisations:*

- equal access to procurement opportunities for firms owned by or employing persons from ethnic/minority groups - cooperatives, social enterprises and non-profit organisations, for example;
- promoting supportive employment for persons with disabilities, including on the open labour market.

### *Accessibility and design for all:*

- mandatory provisions in technical specifications to secure access for persons with disabilities to, for example, public services, public buildings, public transport, public information and ICT goods and services, including web based applications. The key issue is to buy goods and services that are accessible to all.

### *Ethical trade:*

- the possibility, under certain conditions, to take into account ethical trade issues in tender specifications and conditions of contracts.

### *Corporate social responsibility (CSR):*

- working with contractors to enhance commitment to CSR values.

### *Protecting against human rights abuse and encouraging respect for human rights*

Source: European Commission (2010: 7ff.)

Over time the scope of possible social consideration in public procurement became more and more widespread including not only working conditions in a narrow sense but also other social and employment policy issues (Scherrer et.al. 2010). In 2010, the European Commission documented a long list of possible policy issues which might be taken into account within the framework of a “socially responsible public procurement policy”. The list ranges from the promotion of employment opportunities for various groups of employees, the promotion of decent work, the compliance with social and labour rights and the support for social inclusion to the encouragement of human rights and the consideration of ethical and fair trade principles (see: *Box 1*).

According to the European Commission (2010: 5) a socially responsible procurement policy is about “*setting an example and influencing the market-place*”, in order to “*give companies real incentives to develop socially responsible management*”. Moreover, it is seen as one instrument to “*foster the European social model*” as a “*vision of society that combines sustainable economic growth with improved living and working conditions*” (ibid: 10).

### **Legal foundations for social requirements in procurement**

The use of social requirements has also become widely acknowledged in public procurement law both at national and at European level (Arrowsmith and Kunzlink 2009; European Commission 2011a). According to Article 26 of the EU Directive (2004/18/EC) “*contracting authorities may lay down special conditions relating to the performance of a contract (...) The conditions governing the performance of a contract may, in particular, concern **social** and environmental considerations*” (my emphasis). A similar phrase can also be found in Article 70 of the European Commission’s proposal for a new directive on public procurement from December 2011 (European Commission 2011b). Most recently, it has also been confirmed by the European Court of Justice in a case against the Netherlands (C-368/10) “*that contracting authorities are also authorised to choose the award criteria based on considerations of a social nature.*” Apart from the principle legal legitimacy of social considerations in public procurement, there is a general reservation that these requirements have to be “compatible with Community law” (Article 26, Directive 2004/18/EC). As a result of this reservation, there might be important restrictions for the use of social award criteria.

The most prominent example for such a restriction has been created by European Court of Justice (ECJ) with the so-called Ruffert judgment from 2008 (C-346/06) on the use of pay clauses in public procurement.<sup>2</sup> The Ruffert judgement, which dealt with the public procurement law of the German federal state of Lower-Saxony, stated that public authorities are no longer allowed to oblige companies under public contracts to pay their workers at least the rates set by the current local collective agreements. The ECJ ruled that such a provision would be in breach of the freedom to provide cross-border services as laid down in the EU treaty. Following a rather contested interpretation of the European Posted Workers Directive (96/71/EC) the Court pointed out that public authorities can only impose labour provisions on foreign companies if they are based either on statutory regulation or on extended collective agreements. In the case of German public procurement laws, however, reference was made to collective agreements which were not declared universally applicable.

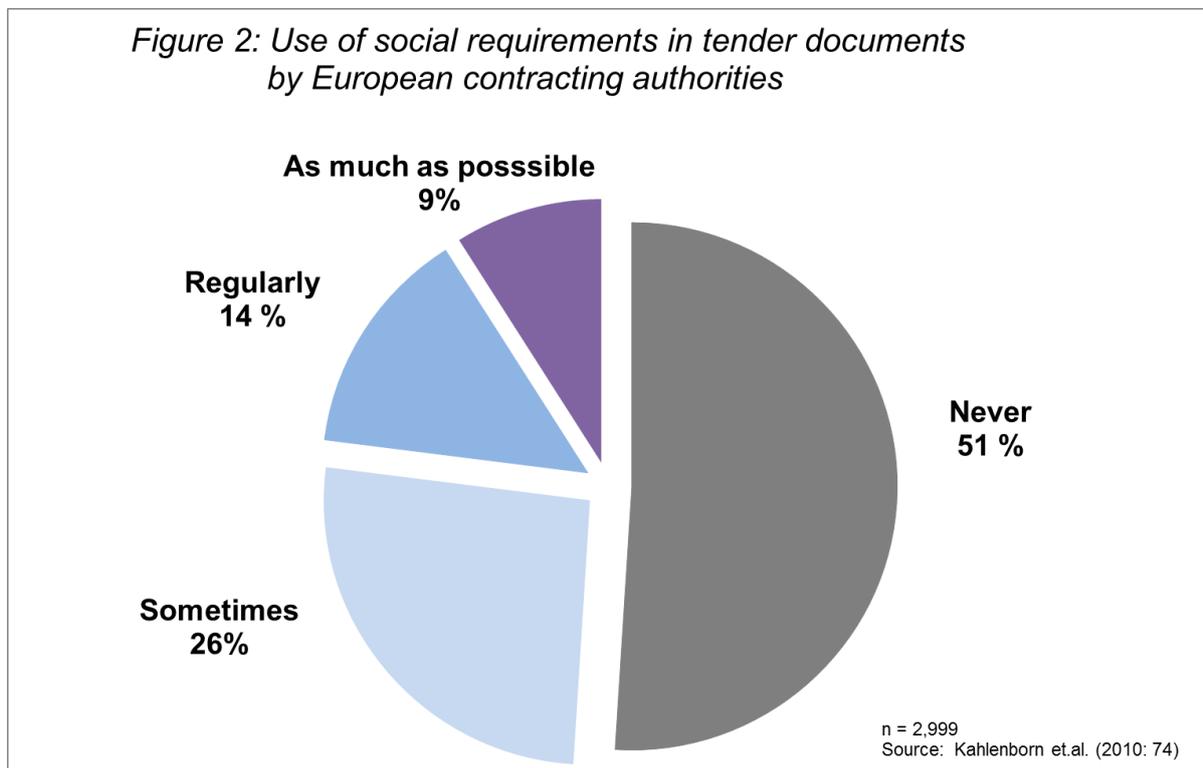
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<sup>2</sup> For a critical evaluation of the Ruffert judgement see among others: Ahlberg and Bruun 2012, Bruun et.al. 2010, Hänlein 2008, Kocher 2008, McCrudden 2011.

## The use of social requirements in the practice of procurement

In a recent evaluation report on the “impact and effectiveness of EU Public Procurement Legislation” the European Commission (2011a: ix) came to the conclusion that in practice public procurement is increasingly used to support the achievement of other policy objectives. This is true, in particular, for the promotion of environmental goals but also for the support of innovations and the development of social standards. The Commission’s estimation is based on the so-called “Adelphi-Study” which contains a broad empirical evaluation on the “strategic use of public procurement in Europe” (Kahlenborn et. al. 2011). According to this study, which carried out among others a web-based survey of contracting authorities (CAs) in Europe, 45 per cent of all surveyed CAs have said that they take into account some form of social considerations in their procurement policy (ibid.: 72).

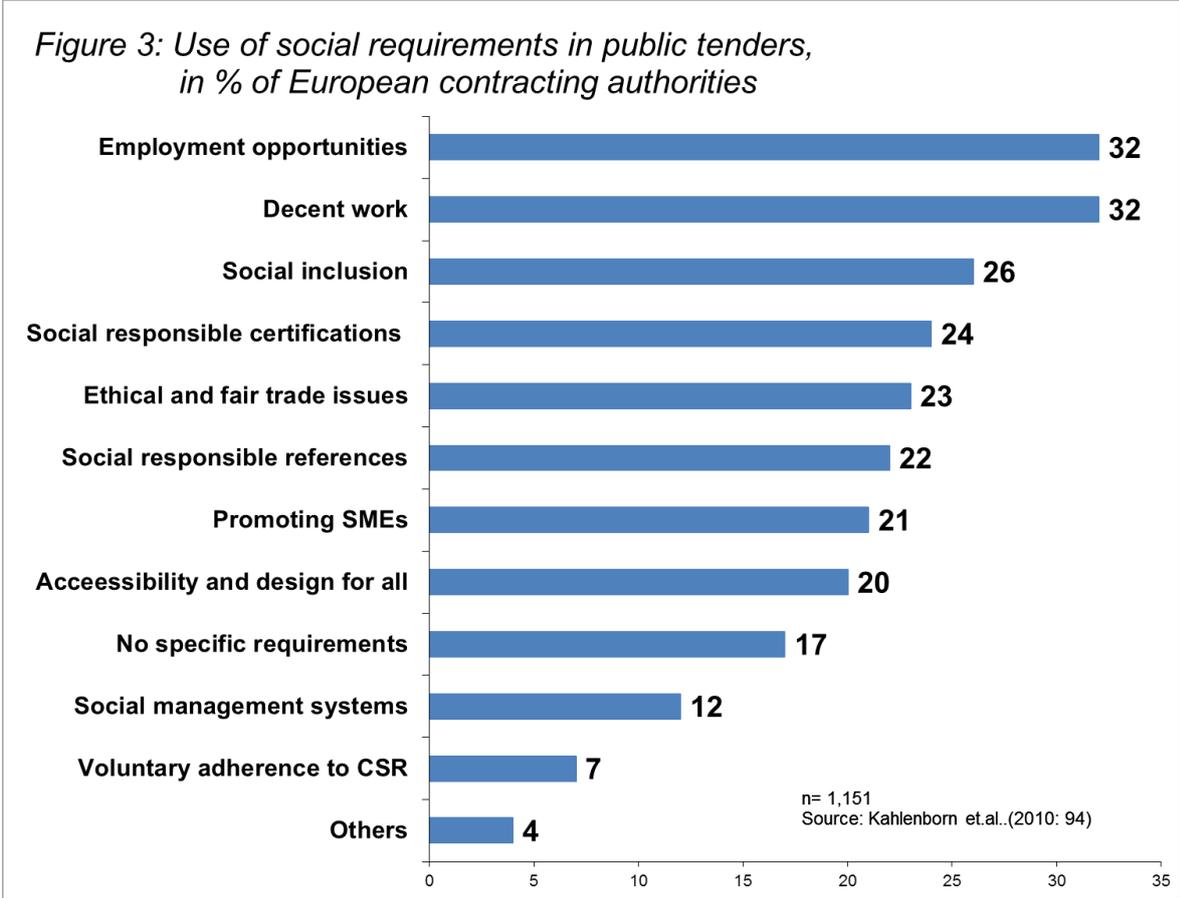
Nearly half of all CAs (49 per cent) confirmed that they use social requirements in the tender documents. 26 per cent use them “sometimes”, 14 per cent “regularly” and 9 per cent “as much as possible” (see: *Figure 2*). Social requirements in the tender documents are most widespread in the UK, where more than 80 per cent of the CAs makes use of them, followed by the Netherlands with more than 70 per cent and Norway with nearly 70 per cent. The lowest usage rate with less than 30 per cent can be found in Poland and Slovenia (ibid.: 75).



The most widespread social topics in public procurement are the “promotion of employment opportunities” and “the promotion of decent work”. In each case 32 per cent of the CAs in Europe confirmed that they include these topics in the tender documents (see: *Figure 3*). Other important topics are “social inclusion” (26 per cent), “social responsibility certifications” (24 per cent) and “ethical and fair trade issues” (23 per cent).

The diffusion of social award criteria is also positively correlated to the existence of national initiatives for a socially responsible procurement policy which occur in somewhat more than half of the EU member states. Among these several countries (e.g. Austria, Belgium,

Denmark, France, Germany, Italy, the Netherlands and the UK) have included social considerations in their National Action Plans on public procurement (ibid. 35f.).



**Public support for social requirements in public procurement**

The increasing importance in the use of social requirements in public procurement meets great support among the European public. According to a special survey of Eurobarometer only 13 per cent of the people in Europe think that the “cheapest price” should be the most important factor for awarding public contracts while the overwhelming majority takes the view that the best offer for a public contract should be judged on a mix of characteristics including social, environmental and other factors (European Commission 2011c: 113f.). 88 per cent of the EU population supports the consideration of social aspects in public procurements even if this would make public contracts more expensive (see: Figure 4). The same holds true also for environmental aspects (87 per cent), but also for the creation of new employment opportunities (85 per cent), especially if they are created at local level. The support for social requirements in public procurement is evenly spread across Europe varying between 96 per cent in Cyprus and 80 per cent in Portugal (see Figure 5).

Figure 4: Support for the consideration of political aspects in public procurement in Europe, even if it makes public contracts more expensive (2011, in %)

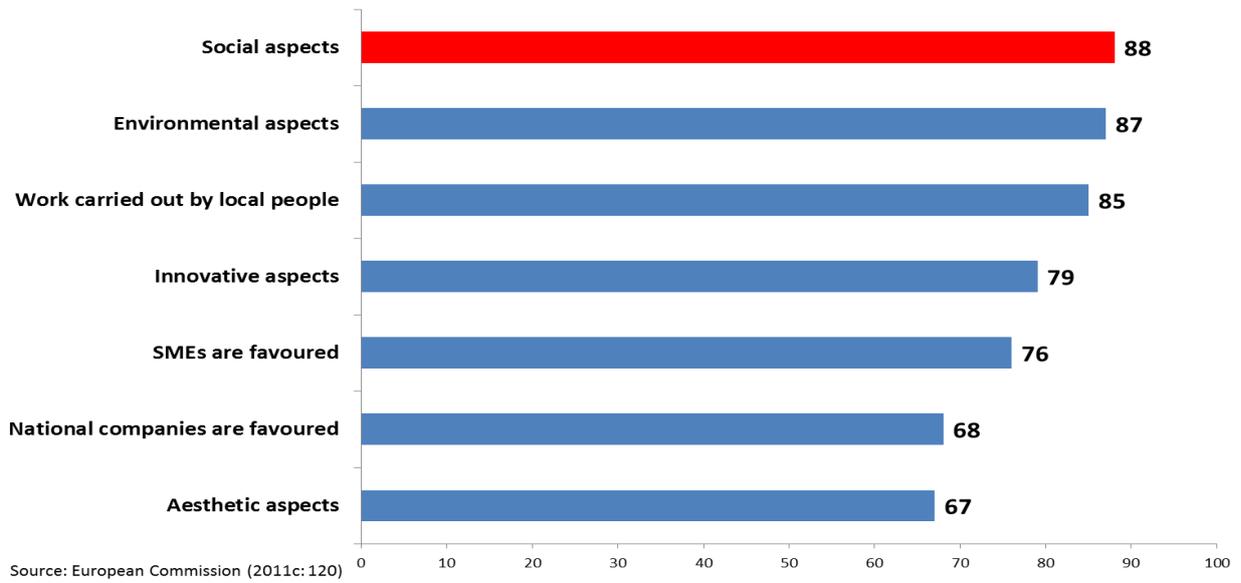
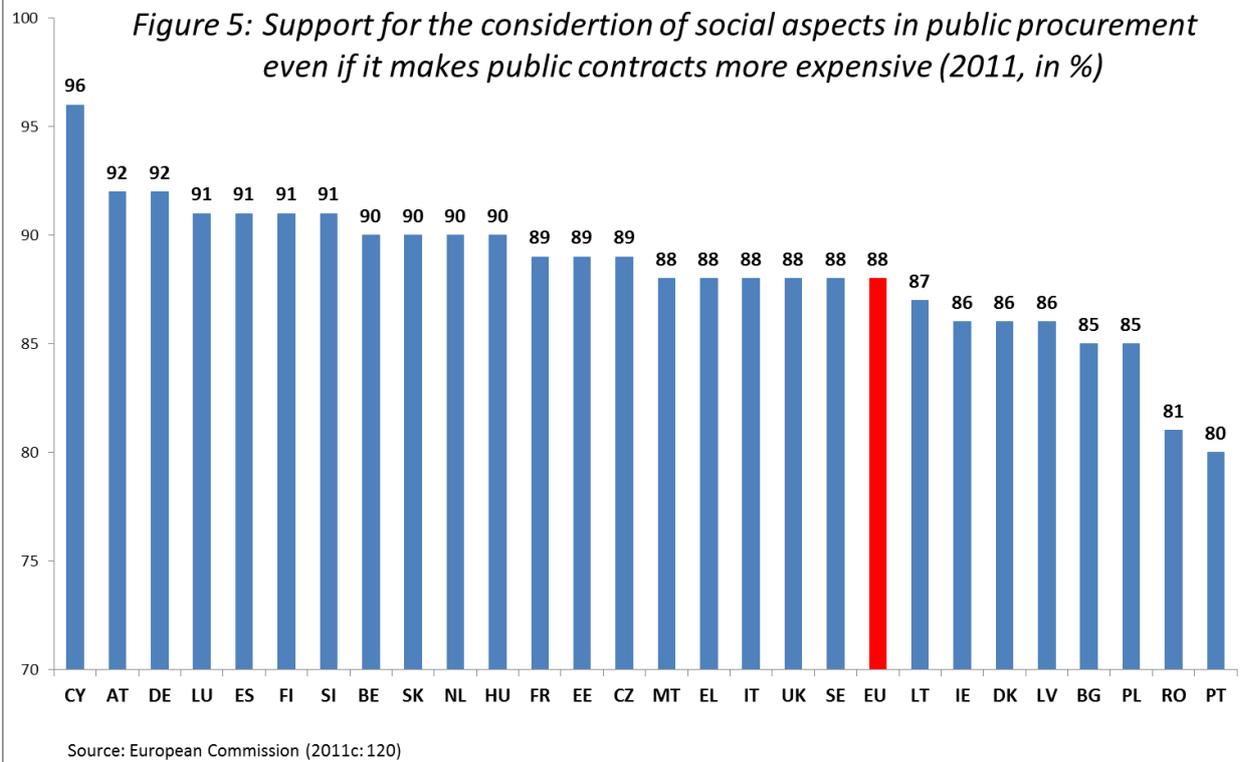


Figure 5: Support for the consideration of social aspects in public procurement even if it makes public contracts more expensive (2011, in %)



## The particular importance of pay clauses in public procurement

Among all social aspects in public procurement, perhaps the most important single issue is the payments for the workers that are hired by the contracting companies and fill public orders. This is true especially in the more labour intensive industries such as construction, public transport, cleaning, social and health services, security services etc. which affect a large part of public procurement. Since labour costs are the most important cost factor in these industries, they also play a major role in determining the price for the offer in the tender process. As contracting authorities often tend to accept the cheapest bid, companies have a strong incentive to push down labour costs in order to get a competitive advantage against other bidders. This might lead to wage dumping strategies at the expense of the affected workers.

Considering the high importance of workers' payments it is all the more astonishing that they play only a minor role in the current debates on social procurement criteria. The recently published EU Guide for a socially responsible procurement policy, for example, mentions "decent pay" only as one sub-bullet point without any further comments or explanations (European Commission 2010: 8). This is even more incomprehensible as pay clauses in public procurement have already a long history in many European countries.

The principle aim of pay clauses in public procurement is to secure workers under public contracts certain (minimum) pay levels which are not below prevailing wage standards. Moreover, for the bidding companies these clauses create a certain competitive order where wages are taken out of competition in the tender process. With the establishment of a level-playing field, pay clauses enable a system of "fair competition" which focuses more on innovation and quality of products and services rather than on labour costs.

## History of pay clauses in public procurement

The historical origins of pay clauses in public procurements date back to the 19th century where they first were adopted in the United States and afterwards spread to many European countries (Abelsdorff 1907; McCrudden 2007: 37ff.). After the establishment of various provisions at local and regional level, the first nation-wide regulation was adopted in 1891 in the United Kingdom with the "Fair Wage Resolution" which obliged the contracting authorities to secure that workers under public contracts receive the prevailing wage levels (Beaumont 1977; Bercusson 1978). In a revised version of the Fair Wage Resolution from 1909 reference was made for the first time not only to *prevailing* but also to *collectively agreed wages*. This meant that in sectors with collective agreements contracting companies had to consider the collectively agreed pay standards.

A similar development took place in France where a national decree on "*les conditions du travail dans les marchés passés au nom de l'Etat, des départements, des communes et des établissements publics*" was adopted in 1899, according to which only those companies were allowed to get public orders which guaranteed their workers prevailing wages and working conditions. Moreover, many local and regional procurement regulations prescribed that contracting companies had to pay their workers certain minimum wages. The latter became the historical predecessors for general statutory minimum wages (Rudischhauser 2000).

In the first decade of the 20<sup>th</sup> century pay clauses in public procurement law also spread quickly over Germany and some other European countries such as Austria, Belgium, the Netherlands, Italy and Switzerland (Abelsdorff 1907; Kaiserliches Statistisches Amt 1907). As these pay clauses in procurement made more and more reference to collective agreements, they have been identified as an important factor in the early development of the collective bargaining system (Rudischhauser 2000).

Finally, in the 1930s pay clauses in procurement became again rather prominent in the United States with the adoption of the Davis-Bacon Act from 1931 and the Walsh-Healey

Public Contracts Act from 1936 which both determine until today that workers under public contracts have to receive prevailing wages (Madland and Walter 2010; Whittaker 2005). The developments in the United States also had a strong influence on the debates within the International Labour Organisation (ILO) which started in the second half of the 1930s to discuss the issue of public contract wages (International Labour Office 2008; Bruun et.al. 2010; Ruchti 2010: 97ff.).

### **The ILO Convention No. 94**

In 1948 the International Labour Office (1948) carried out a comprehensive report on “Fair Wage Clauses in Public Contracts” which gave an overview on national regulations on pay clauses in public procurement which existed at that time. Moreover, the report presented the results of a survey according to which a majority of the ILO member had expressed their support for an ILO Convention on that issue. On 29 June 1949, the 32<sup>nd</sup> International Labour Conference of the ILO finally adopted the *Convention No. 94* and the *Recommendation No. 84* on “Labour Clauses in Public Contracts” which came into force on 20 September 1952. (documented in: International Labour Office 2008: 135ff.).

According to the ILO Committee of Experts on the Application of Conventions and Recommendations the ILO Convention 94 has two principle objectives:

*“First, to remove labour costs being used as an element of competition among bidders for public contracts, by requiring that all bidders respect as a minimum certain locally established standards.*

*Second, to ensure that public contracts do not exert a downward pressure on wages and working conditions, by placing a standard clause in the public contract to the effect that workers employed to execute the contract shall receive wages and shall enjoy working conditions that are not less favourable than those established for the same work in the area where the work is being done by collective agreement, arbitration award or national laws and regulations”* (International Labour Office 2008a: xiii).

In order to fulfil these objectives the main provision of ILO Convention 94 is, that all public contracts *“shall include clauses ensuring to the workers concerned wages (including allowances), hours of work and other conditions of labour which are not less favourable than those established for work of the same character in the trade or industry concerned in the district where the work is carried on*

*(a) by collective agreement or other recognised machinery of negotiation between organisations of employers and workers representative respectively of substantial proportions of the employers and workers in the trade or industry concerned; or*

*(b) by arbitration award; or*

*(c) by national laws or regulations”* (ILO Convention 94, Article 2, Paragraph 1)

Reflecting different interpretations of that provision the ILO Committee of Experts made clear that this provision is not fulfilled if public contracts only refer to the compelling labour legislation. Instead labour clauses should guarantee the “most favourable working conditions” provided by one of the three instruments (collective agreements, arbitration awards or national law) (ibid.: 15 and 35). As collective agreements usually determine more favourable conditions than those laid down in national law, labour clauses in public contracts should refer to the prevailing collective agreements regardless whether they are universally applicable or not.

The ILO Convention 94 shall be applied to all contracts awarded by public authorities **both at central as well as at regional and local level** shall also apply to work carried out by

subcontractors.<sup>3</sup> Moreover, the ILO Recommendation No. 84 adds that labour clauses might be used also “in cases where private employers are granted subsidies or are licensed to operate a public utility.” Therefore, ILO Convention No 94 is also relevant for concession contracts.

Regarding the determination of the labour clauses the ILO Convention 94 asks the public authorities to consult “the organisations of employers and workers concerned.” Furthermore the public authorities shall take appropriate measures for the enforcement of the labour clauses and shall provide adequate sanctions against companies which fail to observe the provisions of labour clauses in public contracts.

**Ratification of ILO Convention 94 in Europe.**

In comparison to many other ILO Conventions the acceptance of Convention 94 has always been rather limited. All in all there are currently 62 countries, which have ratified the ILO Convention 94, which corresponds to roughly one third of all ILO member states. Within Europe there are 15 countries, of which 10 are EU member states (Austria, Belgium, Bulgaria, Cyprus, Denmark, Finland, France, Italy, Netherlands and Spain). Most of the ratifications took place already in the early 1950s, while more recently only a very few countries have ratified the Convention 94. One of them was Norway, which has ratified the Convention 94 in 1996. The two most recent ratifications, however, came from the two Balkan states Bosnia and Herzegovina and Macedonia which adopted the Convention in 2010. So far, the UK is the only country which denounced the Convention 94 in 1982, after it was among the first countries which had ratified it already in 1950.

**Table 2.1: European countries which ratified the ILO Convention 94**

| Countries   | Year of ratification | Countries              | Year of ratification |
|-------------|----------------------|------------------------|----------------------|
| Austria     | 1951                 | Denmark                | 1955                 |
| Finland     | 1951                 | Cyprus                 | 1960                 |
| France      | 1951                 | Turkey                 | 1961                 |
| Belgium     | 1952                 | Spain                  | 1971                 |
| Italy       | 1952                 | Norway                 | 1996                 |
| Netherlands | 1952                 | Armenia                | 2005                 |
| Bulgaria    | 1955                 | Bosnia and Herzegovina | 2010                 |
|             |                      | Macedonia FYROM        | 2010                 |

Effective October 2012

Source: ILO (<http://www.ilo.org/ilolex/cgi-lex/ratifce.pl?C094>)

<sup>3</sup> In the ILO Convention 94 it is stated: “The competent authority shall determine the extent to which and the manner in which the Convention shall be applied to contracts awarded by authorities other than central authorities” (Article 1, 2). As the ILO Committee of Experts on the Application of Conventions and Recommendations has pointed out, the “Convention No. 94 principally addresses itself to contracts awarded by a central authority. It explicitly permits, however, application to other authorities as the competent national authorities may freely decide.” Considering the objectives of the Convention 94, for the ILO Expert Committee it makes obviously no sense to exclude “a large number of persons working under public contracts made with non-central authorities” (International Labour Office 2008: 25).

## Pay clauses in national public procurement regulation

While at a global level the ILO Convention 94 seems to be of a rather limited importance, it has at least some relevance in Europe. This is all the more true as there are also a couple of countries which follow the policy of the Convention without having ratified it. All in all, almost all countries in Europe have some form of reference to pay and working conditions in their national procurement laws (see: *Table 2.2*).

**Table 2.2: Provisions on pay and working conditions in national procurement regulation**

| <b><i>Countries which have ratified the ILO Convention 94</i></b>                |   |
|--|---|
| Pay clauses and/or explicit references to compliance with collective agreements  | Austria, Belgium, Bulgaria, Denmark, Finland, Italy, Norway |
| Only general references to the compliance with pay and working                   | Cyprus, France, Netherlands, Spain,                         |
| <b><i>Countries which have not ratified the ILO Convention 94</i></b>            |   |
| Pay clauses and/or explicit references to compliance with collective agreements  | Germany, Luxembourg, Sweden, Switzerland, UK                |
| Only general references to the compliance with pay and working conditions        | Czech Republic, Hungary, Malta, Romania, Slovakia, Slovenia |
| Request to monitor working conditions only in the case of abnormally low tenders | Estonia, Latvia, Lithuania                                  |
| No references to pay and working conditions                                      | Poland, Portugal  |

Source: Own composition on the basis of the legal overview in the annex of this chapter

Among the European countries, which have ratified the ILO Convention 94, the only country which makes an explicit reference to the Convention in its national procurement law is Austria. Moreover, Denmark has a national decree on the implementation of the ILO Convention 94, which obliges public authorities at central level to use labour clause in public contracts. In addition to that, there are several Danish municipalities which use labour clauses on a voluntarily basis.<sup>4</sup> Furthermore, also Belgium, Finland, Italy, and Norway<sup>5</sup> have an explicit provision in their national procurement regulation, according to which pay and working conditions of workers under public contracts have to be in compliance not only with the labour laws but also with the current collective agreements, regardless whether they are universally applicable or not. Finally, in Bulgaria the national procurement law asks for consideration of a “minimum monthly amount of the contributory income differentiated by economic activities and occupations grouped by qualification” for workers under public contracts but has no reference to collective agreements. In contrast to that, there are also four countries (Cyprus, France, Netherlands and Spain) which have ratified the ILO Convention 94, but where the national regulation on procurement contains only a general reference to the compliance with prevailing pay and working conditions.

<sup>4</sup> For more see the chapter on Denmark in this study

<sup>5</sup> See also the chapter on Norway in this study.

Among the countries, which have *not* ratified the ILO Convention 94, there are nevertheless at least five countries in which pay clauses play an important role in the national procurement policy (Germany, Luxembourg, Sweden, Switzerland and the UK). In Switzerland the national procurement law contains a provision according to which public contracts can only be given to companies which comply with “locally prevailing working conditions”. The latter are first and foremost defined as those provisions determined by collective agreements, regardless whether or not these agreements have been declared as generally binding.<sup>6</sup> A similar regulation can be found in Luxembourg where a National Decree on the Implementation of the Public Procurement Act contains a separate article on “wages” according to which workers under public contract are not allowed to pay less than what has been determined by law or collective agreements for the respective industries or professions.

In Germany, many regional procurement laws at the level of the Federal States contain pay clauses, according to which workers under public contracts have to receive either specific procurement-related minimum wages or wages determined by collective agreements. While after the Ruffert judgement the German procurement laws mostly refer only to collective agreements which are universally applicable, this is not the case for procurement in the public transport sector which is seen as a special legal case not affected by the Ruffert case.<sup>7</sup>

Similarly, there is also no national regulation on pay clauses in Sweden, but the instrument has been frequently used in procurement regulation at regional and local level (Ahlberg and Bruun 2010: 56ff). The Swedish Association of Local Authorities and Regions has released a circular in which it recommends the public authorities “to stipulate that contractors pay wages in accordance with current collective agreements” (Ahlberg and Bruun 2012: 16). However, especially after the Ruffert judgement there is a lot of legal uncertainty in Sweden whether such pay clauses in procurement are in conformity with EU law (Ahlberg and Bruun 2010, 2012; Vinterskog 2011). There is also an ongoing debate on whether Sweden should ratify the ILO Convention 94 as it has been strongly demanded, for example, by the Swedish trade unions (LO 2012)

In the UK, the focus of using pay clauses in public procurement is also very much on local level. While the national regulation on procurement contains on a weak reference to pay and working conditions, several municipalities in the UK have, in the meantime, followed the example of the Greater London Authority and have established a policy on “living wages”. Although these living wage regulations are not strictly legally binding, they produce a high moral and political commitment for contracting companies to pay the recommended living wages which are far above the national statutory minimum wage.<sup>8</sup>

Most of the Eastern European countries, which – with the exception of Bulgaria and most recently Bosnia and Herzegovina and Macedonia – have not ratified the ILO Convention 94, have only a very general reference in their national procurement regulation, according to which contracting companies have to be in compliance with legally binding pay and working conditions. According to the procurement law of the Baltic States working conditions of contracting companies have only be taken into consideration in the case of an abnormally low tender. Finally, there is no reference at all to working conditions in the procurement legislation of Poland and Portugal.

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<sup>6</sup> For more see the chapter on Switzerland in this study

<sup>7</sup> For more see the chapter on Germany in this study.

<sup>8</sup> For more see the chapter on the UK in this study.

**Pay clauses in procurement and national collective bargaining system**

The real meaning of pay clauses in public procurement can only be understood within the framework of the national collective bargaining systems (*Table 2.3*). There are many countries in Europe where most of the collective agreements are declared generally binding (Schulten 2012), so that they also have to be considered within public procurement. Among these countries are states like Austria, Belgium, France, the Netherlands or Spain, which all have ratified the ILO Convention 94, but where procurement-related pay clauses have only very little meaning in practice. Due to a very high bargaining coverage as the result of universally applicable collective agreements pay clauses in procurement have no additional advantage in these countries, perhaps except for the fact that procurement might create a further area of control and enforcement.<sup>9</sup>

Pay clause in public procurement have the highest practical relevance especially in those countries where (most) collective agreements are not universally applicable. This holds true for countries like Denmark, Sweden or the UK, which have no system of declaring collective agreements generally binding at all, as well as for countries like Germany, Norway or Switzerland, where the legal extension of collective agreements is limited to a very few sectors. In all these countries pay clauses in procurement create a kind of compensatory regulation for the missing of comprehensive legal extension mechanisms.<sup>10</sup>

**Table 2.3: The use of pay clauses in public procurement of selected European countries**

|                                       | Pay clauses in procurement are frequently used ...<br>... because (most) collective agreements are <b>not</b> universally applicable | Pay clauses procurement are <b>not</b> much used ...<br>... because most collective agreements are universally applicable (or functional equivalents) |
|---------------------------------------|--|---|
| ILO Convention 94 ratified            | Denmark, Norway  | Austria, Belgium, Finland, France; Italy, Netherlands, Spain  |
| ILO Convention 94 <b>not</b> ratified | Germany, Sweden, Switzerland, UK.  | Portugal  |

Source: Own composition on the basis of Schulten (2012)

It is, therefore, rather paradoxical that the ECJ in its Ruffert judgement allows pay clauses in procurement only when they refer to statutory minimum wages or universally applicable collective agreements. The Ruffert judgement is totally ignoring the different national collective bargaining systems and traditions of industrial relations and has no understanding on the real meaning of pay clauses in procurement. Moreover, it turns against the logic of the

<sup>9</sup> As the collective bargaining systems in some European countries (e.g. Spain) are currently undergoing some dramatic changes including a dismantling of extension procedures (Busch et.al. 2012), pay clauses in public procurement might regain some importance in these countries.

<sup>10</sup> In Germany pay clauses in public procurement are sometimes even called “*kleine Allgemeinverbindlicherklärung von Tarifverträgen*” which means a “smaller version of legal extension of collective agreements”.

ILO Convention 94 (Bruun et.al. 2010) which aims to create an additional protection for workers under public contracts and is not only reviewing regulation which is legally binding anyway. If the instrument of pay clauses in procurement should continue to have an independent meaning in Europe, a political clarification is necessary in order to repeal the basic notion of the Rüffert judgement. The obviously most direct way to do this, would be an explicit reference to the ILO 94 Convention in the European Public Procurement Directive, as it has been demanded, for example, by the European Parliament (2011).

## Annex: Provisions on pay and working conditions in national procurement regulation

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|------------|---|
| Austria    | <p><b>National Procurement Law from 2006</b> (<i>Bundesvergabegesetz</i>) contains an explicit reference to the <b>ILO Convention 94</b> (Article 84,1).</p> <p><a href="http://www.bka.gv.at/DocView.axd?CobId=16901">http://www.bka.gv.at/DocView.axd?CobId=16901</a></p>   |
| Belgium    | <p><b>National Law on the Public Orders for Works, Supplies and Services from 2006</b> (<i>Wet overheidsopdrachten en bepaalde opdrachten voor werken, leveringen en diensten/Loi relative aux marchés publics et à certains marchés de travaux, de fournitures et de services</i>) contains a provision according to which working conditions of workers under public contracts have to be in compliance with what is determined by law or collective agreements (Section 3, Article 42,1).</p> <p><a href="http://www.belgium.be/fr/binaries/lois_marches_publics_wetten_overheidsopdrachten_tcm116-21592.pdf">http://www.belgium.be/fr/binaries/lois_marches_publics_wetten_overheidsopdrachten_tcm116-21592.pdf</a></p> |
| Bulgaria   | <p><b>National Public Procurement Law from 2004</b> contains a provision according to which each tender must contain “<i>a declaration to the effect that the price tendered complies with the minimum labour cost requirement</i>” (Article 56, 1, 10) According to Article 147, 1 of the Supplementary Provisions “<i>Minimum labour costs shall be the minimum amount of remuneration of labour, defined as a minimum monthly amount of the contributory income differentiated by economic activities and occupations grouped by qualification.</i>”</p> <p><a href="http://www.oecd.org/countries/bulgaria/39641248.pdf">http://www.oecd.org/countries/bulgaria/39641248.pdf</a></p>                                    |
| Cyprus     | <p><b>National “Coordination of Procedures for the Award of Public Works Contracts Law” from 2006</b> contains a provision according to which contracting authorities have to review compliance with employment protection and prevailing working conditions at national, regional and local level for workers under public contracts (Article 29).</p> <p><a href="http://www.olc.gov.cy/olc/olc.nsf/all/F13A3A5B76A2F01C42257758003295AE/\$file/Law%2012%20of%202006%20FINAL.pdf?openelement">http://www.olc.gov.cy/olc/olc.nsf/all/F13A3A5B76A2F01C42257758003295AE/\$file/Law%2012%20of%202006%20FINAL.pdf?openelement</a></p>  |
| Czech Rep. | <p><b>National Act No. 137/2006 Coll. on Public Contracts</b> points out that “<i>in the case of a public service contract or public works contract, the contracting entity is entitled to indicate in the tender documentation an administrative body or another entity wherefrom the economic operators may obtain information concerning the obligations arising from separate legal regulations relating to the employment protection provisions and to the working conditions</i>” (Article 44, 7).</p> <p><a href="http://www.compet.cz/fileadmin/user_upload/Legislativa/VZ/CR/2006_137_Eng.pdf">http://www.compet.cz/fileadmin/user_upload/Legislativa/VZ/CR/2006_137_Eng.pdf</a></p>                               |
| Denmark    | <p><b>National “Circular communication on the application of the ILO Convention 94” from 1966</b> (<i>Arbejdsministeriets cirkulæreskrivelse nr. 114 af 18. maj 1966</i>) prescribes that all contracts by the central authorities of Denmark should include a labour clause.</p> <p>Although there is no obligation for labour clauses in public contracts at local level, <b>several municipalities</b> are prescribing such clauses.</p>   |
| Estonia    | <p><b>National Public Procurement Act from 2007</b> determines that “<i>if the contracting authority finds that the value of a tender is abnormally low</i>” the contracting authority shall request information on “<i>provisions in force in the place of performance of the public contract, which regulate the protection of employees and working conditions</i>” (Article 48.4)</p> <p><a href="http://www.legaltext.ee/text/en/XXX0005.htm">http://www.legaltext.ee/text/en/XXX0005.htm</a></p>  |

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| Finland   | <p><b>National Act on Public Contracts from 2007</b> makes reference to “<i>compliance with the provisions of the International Labour Organisation (ILO) conventions</i>” and contains a special provision according to which “<i>public works contract awarded by a central government authority to a private employer shall be accompanied by a clause, added to the contract before the contract is signed, according to which the employment contracts relating to the public works contract shall comply with the minimum terms of employment which must be observed in similar work pursuant to Finnish law and collective agreements</i>” (Article 49, 2)</p> <p><a href="http://www.finlex.fi/fi/laki/kaannokset/2007/en20070348.pdf">http://www.finlex.fi/fi/laki/kaannokset/2007/en20070348.pdf</a></p> |
| France    | <p><b>National Law on Public Contracts from 2006</b> (<i>Code des marchés publics</i>) makes reference to the prevailing local working conditions (Article 55)</p> <p><a href="http://www.legifrance.gouv.fr/affichCode.do?cidTexte=LEGITEXT000005627819">http://www.legifrance.gouv.fr/affichCode.do?cidTexte=LEGITEXT000005627819</a></p>  |
| Germany   | <p><b>National legal framework for procurement</b> which is part of the ‘<b>German Act against Restraints on Competition</b>’ (<i>Gesetz gegen Wettbewerbsbeschränkungen</i>) contains only a general provision according to which “<i>social consideration</i>” can be taken into account in procurement (Article 97,4)</p> <p><a href="http://www.gesetze-im-internet.de/bundesrecht/gwb/gesamt.pdf">http://www.gesetze-im-internet.de/bundesrecht/gwb/gesamt.pdf</a></p> <p><b>Procurement Laws of various Federal States</b> (<i>Vergabe- und Tarifreuegesetze</i>) contain provisions on minimum wages and the compliance with collective agreements for workers under public contracts</p> <p><a href="http://www.boeckler.de/index_tarifreue.htm">http://www.boeckler.de/index_tarifreue.htm</a></p>        |
| Italy     | <p><b>National Decree on Public Procurement from 2006</b> (<i>Decreto Legislativo 12 aprile 2006, n. 163 codice deo contratti pubblici die lavori, servizio, furniture</i>) include a pay clause according to which “<i>the contract holder is required to observe the economic and other conditions established in national and regional collective bargaining that apply in the region in which the contract is carried out</i>” (Article 118,6).</p> <p><a href="http://www.urp.cnr.it/copertine/ente/ente_evidenza/dlgs163_06.pdf">http://www.urp.cnr.it/copertine/ente/ente_evidenza/dlgs163_06.pdf</a></p>   |
| Hungary   | <p>According to the <b>National Act CVIII of 2011 on Public Procurement</b> “<i>contracting authority may take into consideration objective explanations relating in particular to ... the compliance with employment protection provisions and working conditions in force at the place of performance of the public works, services, or supply contract</i>” (Article 69, 4e)</p> <p><a href="http://www.kozbeszerzes.hu/static/uploaded/document/PPA%202012_011.pdf">http://www.kozbeszerzes.hu/static/uploaded/document/PPA%202012_011.pdf</a></p>   |
| Latvia    | <p><b>National Public Procurement Law from 2007</b> determines that “<i>If a tender for a specific public works, supply or service contract is unjustifiably low, the commissioning party</i>” shall provide – among others – information regarding “<i>the labour protection provisions and the conformity of working conditions with the location where buildings works are performed, goods supplied or services provided</i>” (Article 48,2,4)</p> <p><a href="http://www.knab.gov.lv/uploads/eng/public_procurement_law1.pdf">http://www.knab.gov.lv/uploads/eng/public_procurement_law1.pdf</a></p>  |
| Lithuania | <p><b>National Law on Public Procurement from 1996</b> determines that “<i>in order to obtain justification of the abnormally low price, the contracting authority</i>” shall provide information regarding “<i>the compliance with the regulations on safety at work and working conditions, valid in the place of provision of supplies, services or performance of works</i>” (Article 40, 2, 4)</p> <p><a href="http://www.vpt.lt/admin/uploaded/VPI_vertimas_2007_red.pdf">http://www.vpt.lt/admin/uploaded/VPI_vertimas_2007_red.pdf</a></p>   |

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| Luxembourg  | <p><b>National Decree on the Implementation of the Public Procurement Act from 2009</b> (<i>Règlement grand-ducal du 3 août 2009 portant exécution de la loi du 25 juin 2009 sur les marchés publics</i>) contains a separate article on “wages” according to which workers under public contract are not allowed to pay less than what has been determined by law or collective agreements for the respective industries or professions. (Article 32, 1).</p> <p><a href="http://www.legilux.public.lu/leg/a/archives/2009/0180/a180.pdf#page=2">http://www.legilux.public.lu/leg/a/archives/2009/0180/a180.pdf#page=2</a></p>  |
| Malta       | <p><b>National Public Contracts Regulations from 2004</b> determines that “<i>the contracting authority may state in the contract documents ... appropriate information on the obligations relating to the employment protection provisions and the working conditions which are in force in Malta, or the region or locality in which the services are to be performed and which shall be applicable to the performance of the contract</i>” (Article 56, 1)</p> <p><a href="http://www.oecd.org/countries/malta/35015641.pdf">http://www.oecd.org/countries/malta/35015641.pdf</a></p>   |
| Netherlands | <p><b>National Regulation on Public Procurement from 2005</b> (<i>Besluit aanbestedingsregels voor overheidsopdrachten</i>) contains a provision on locally prevailing working conditions for workers under public contract (Article 56, 2)</p> <p><a href="http://www.rijksoverheid.nl/documenten-en-publicaties/besluiten/2008/12/10/besluit-aanbestedingsregels-voor-overheidsopdrachten-bao-recent.html">http://www.rijksoverheid.nl/documenten-en-publicaties/besluiten/2008/12/10/besluit-aanbestedingsregels-voor-overheidsopdrachten-bao-recent.html</a></p>   |
| Norway      | <p><b>National administrative regulation on pay and working conditions in public contracts from 2008</b> (<i>Forskrift om lønns- og arbeidsvilkår i offentlige kontrakter</i>) according to which “<i>in areas covered by a regulation that declare collective agreements generally applicable contracting authorities shall require that pay and working conditions are in accordance with applicable regulations. In areas not covered by a regulation that declare collective agreements generally applicable contracting authorities shall require that pay and working conditions are in accordance with applicable nationwide collective agreements for the industry</i>” (Article 5) .</p> <p><a href="http://www.lovdatta.no/cgi-wift/ldles?doc=/sf/sf/sf-20080208-0112.html">http://www.lovdatta.no/cgi-wift/ldles?doc=/sf/sf/sf-20080208-0112.html</a></p> |
| Poland      | <p><b>National Public Procurement Law from 2004</b> contains no explicit reference to pay or working conditions.</p> <p><a href="http://www.oecd.org/poland/39645964.pdf">http://www.oecd.org/poland/39645964.pdf</a></p>  |
| Portugal    | <p><b>National Decree on Public Contracts from 2008</b> contains no explicit reference to pay or working conditions.</p> <p><a href="http://www.dgap.gov.pt/upload/Legis/2008_dl_18_29_01.pdf">http://www.dgap.gov.pt/upload/Legis/2008_dl_18_29_01.pdf</a></p>  |
| Romania     | <p><b>National Law on Public Procurement from 2006</b> states that “<i>the contracting authority has the obligation to point out in the tender documentation the compulsory rules related to the specific employment protection and working conditions that are in force at national level and that have to be respected during the performance of the contract or to indicate the competent bodies which from the economic operators may obtain appropriate information regarding the respective regulations.</i>” (Article 34)</p> <p><a href="http://www.oecd.org/countries/romania/39646004.pdf">http://www.oecd.org/countries/romania/39646004.pdf</a></p>  |
| Slovakia    | <p><b>National Act on Public Procurement from 2005</b> prescribes that “<i>the contracting authority and contracting entity may indicate institutions in the tender documents from which a candidate will obtain information regarding obligations relating to taxes, environmental protection, labour protection and working conditions applicable in the place of building works or services during the contract performance. In the event such information is provided, the tender documents will request that each of the candidates in their tenders submit a declaration that obligations concerning labour protection and</i></p>   |

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|             | <p><i>working conditions were taken into account when drawing up the tender</i>" (Article 34. 16).</p> <p><a href="http://www.oecd.org/slovakia/39646945.pdf">http://www.oecd.org/slovakia/39646945.pdf</a></p>  |
| Slovenia    | <p><b>National Public Procurement Act from 2006</b> prescribes that "<i>tenderers or candidates in the public procurement procedure ... have taken account, when drawing up their tender, of the obligations relating to employment protection provisions and working conditions which are in force in the locality where the works are to be carried out or the service is to be provided</i>" (Article 40)</p> <p><a href="http://www.dkom.si/util/bin.php?id=2007100210195957">http://www.dkom.si/util/bin.php?id=2007100210195957</a></p>  |
| Spain       | <p><b>National Law on public contracts from 2007</b> (<i>LEY 30/2007, de 30 de octubre, de Contratos del Sector Público</i>) contains a provision on the compliance with valid regulation on working conditions (Article 103).</p> <p><a href="http://www.boe.es/boe/dias/2007/10/31/pdfs/A44336-44436.pdf">http://www.boe.es/boe/dias/2007/10/31/pdfs/A44336-44436.pdf</a></p>  |
| Sweden      | <p><b>National Public Procurement Act from 2007</b> (<i>Lag (2007:1091) om offentlig upphandling</i>) includes a general provision according to which "<i>social considerations</i>" can be taken into account "<i>if the nature of the procurement motivates this</i>" (Chapter 1, Article 9a). Furthermore, it allows the contracting authorities to lay down special social conditions relating to the performance of a contract (Chapter 10, Article 13).</p> <p><a href="http://www.kkv.se/upload/Filer/ENG/Publications/Swedish_Public_Procurement_Act.pdf">http://www.kkv.se/upload/Filer/ENG/Publications/Swedish_Public_Procurement_Act.pdf</a></p> <p><b>There are many procurement provisions at regional and local level</b> which make reference on decent pay and the compliance with collective agreements for workers under public contracts</p> |
| Switzerland | <p><b>National procurement law from 1994</b> (<i>Bundesgesetz über das öffentliche Beschaffungswesen</i>) contains a provision according to which public contracts can only be given to companies which comply to locally prevailing working conditions (Article 8,b). According to a further <b>national Decree on Public Procurement from 1995</b> (<i>Verordnung über das öffentliche Beschaffungswesen</i>) the "<i>prevailing working conditions</i>" are first and foremost provisions which lay down in collective agreements (Article 7,1).</p> <p><a href="http://www.admin.ch/ch/d/sr/1/172.056.1.de.pdf">http://www.admin.ch/ch/d/sr/1/172.056.1.de.pdf</a></p>   |
| UK          | <p>The <b>National Public Contract Regulations from 2006</b> determine that "if an offer for a public contract is abnormally low" contracting authority has to request an explanation including information on the "<i>compliance with the provisions relating to employment protection and working conditions in force at the place where the contract is to be performed</i>" (Article 30,7).</p> <p><a href="http://www.oecd.org/unitedkingdom/39647169.pdf">http://www.oecd.org/unitedkingdom/39647169.pdf</a></p> <p>Moreover, many cities have developed <b>local (non-binding) provisions</b> on the payment of „living wages“ to workers under public contracts</p>  |

Source: Own composition on the basis of national sources

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### 3. Denmark

*Klaus Pedersen*

#### Introduction

This chapter sets out and analyses the Danish situation on the formal requirements, practice and use of pay and social clauses in public procurement. In addition, it outlines how administration and control in this area is actually conducted. Finally, it identifies and discusses examples of good and bad practice in the field of pay clauses.

An analysis of this kind is inherently normatively based, and involves consideration of both the substantive and structural requirements of existing Danish social clauses in public procurement. Given the fact that they are combined in complex ways, it is frequently difficult to distinguish and separate the one from the other.

After having gone through the formal provisions and their practical application it is endeavoured, in the summing up of the findings in this case-study, to look deeper into the meaning of this relation between material workers protection and structural requirements.

#### Danish labour market regulation

The intention here is *not* to uncover the functioning and the structures of the Danish system of labour market regulation. However, in the context of the aim of describing and analysing the way in which national labour market instruments operate to protect employees from wage dumping and undercutting of other labour conditions, a brief introduction to the system's general features seems appropriate.

At the outset it is important to note that the Danish labour market model is to a high degree a voluntaristic one (Scheuer, 2007, Due et al 2010). Thus the regulation of the labour market is almost entirely left to the Danish social partners. This means that wages, working time and regulations on hiring and laying off employees, in both the private and the public sectors of the labour market, are left to autonomous regulation through collective agreements concluded by the social partners, with the state and the civil society accepting that the settlement of these arrangements sometimes includes the use of industrial conflict and the associated risk of a reduced operation of those social spheres involved.

Collective agreements are in the possession of the social partners, meaning that only unions and employers organisations at the outset are entitled to state the rights and obligations for workers and employers contained in the agreements. However, both employers and workers have access to some basic legal means of securing their rights on wages and working conditions through litigation in the civil courts, should the social partners refrain from taking action .

In Denmark no general system of national minimum wage or sectoral *erga omnes* procedure has hitherto been introduced to protect wages and working conditions. This differentiates Denmark from all other EU countries, except Sweden (Andersen et al, 2007).

The Danish autonomous labour market system is widely supported by the political, legal and administrative systems. Apart from a deep rooted consensus on retaining the autonomous labour market model, a range of public and semi-public institutions exists to support the process of voluntary collective labour market agreement. This supportive system can be differentiated into two levels:

- A conflict prevention system, consisting of the industrial arbitration boards, the State Conciliation institution and the scope for mediators to interlink collective agreement proposals in the membership ballot procedure.
- A conflict resolution system, under which the Danish national labour court, the industrial arbitration boards and parliament may decide on and intervene in conflicts.

These institutions serve as supportive institutions to the autonomous and *closed* labour market system, helping it to focus on achieving integrative and balanced consensus solutions and preventing it from fulfilling its functions and securing legitimacy through recurring conflicts. “Closed” is meant here in the sense that these institutions are able to create their own communication and rationality, because their decisions cannot “abandon” the system to other court systems or state board systems outside the collective labour market system through resort to grievance procedures or appeals.

### **Danish legal regulation on pay determination**

To understand the voluntary constitution of the Danish labour market model, it is important to understand that the model is rooted and still based entirely on the general principle of freedom to contract. This furthermore entails that employment contracts are basically regulated only through private agreement, either as collective agreements or as private bilateral agreements between the individual employee and employer. This goes for the private as well as the public labour market. The general act on contract law (1996) simply states the absolute basic wage requirement that must be met for the contract to be legal. Under this, the agreement could be set aside if it would be “...[u]nreasonable or contrary to good faith to enforce it” (Paragraph 36). This shows the wide scope for freedom of contract in the Danish context. On the other hand, in practice, case-law interpreting this provision suggests that the courts will not accept an hourly salary below 8-10 Euros, depending on type of work and required qualifications.

### **Special regulation guarding wages and labour relations**

Even though the general Danish principle covering employment contracts is that of freedom of contract, some legislation exists that grants special protection to employees regarded as vulnerable or employed in special positions. However, in some cases these categories are based rather on their historical status or contexts than on present facts.

Presently the only current specific Danish regulation specifying a wage and setting working conditions deals with au pairs. However, this administrative regulation on the provision of residence permits for au pairs does not in fact regard au pairs as employees. Rather, the definition of au pair and their functions follows from a European Council agreement (1969) which emphasises the element of intercultural exchange.

The Danish administrative regulation requires that the au pair-hosts pay monthly (gross) 3.050 Dkr. (410 Euros) for a maximum 30 hours of work a week, and with the right for the au pair to stay in Denmark for a maximum period of two years. Furthermore, the au pair must be given room and board and return travel expenses for au pairs from outside of Europe must be covered by the host.

The most comprehensive Danish piece of legislation regulating the labour market – The Salaried Employees Act (2009) - does not lay down specific levels for wages and other working conditions. This Act basically establishes the right to a voluntarily agreed wage that is one set down by collective agreement. Additionally it guarantees that the agreed wage should continue to be paid when the employee is not in work for a range of reasons, such as during holidays, illness, temporary stoppage etc. The Salaried Employees Act dates back to the 1950s, when salaried employees were mainly managerial personal or public servants who lacked effective instruments to determine working conditions through collective bargaining.

Another category of legislative protection of wages and working conditions was the Danish transitional schemes following the EU enlargements in 2004 and 2007 and applied until the expiry of the transitional scheme in May 2009. The regulation covered individual labour migrants from the new EU Member States in East- and Central Europe (EU10). It was formalised in the Immigration Act (2004), which stated that EU10 citizens would only be

granted access to Denmark in order to work if they had obtained a work contract with an employer established in Denmark prior to their arrival under working conditions that accorded with the normal Danish standards, basically those set by collective agreement. The access for service providers from EU10 and accompanying posted workers were not restricted. Regarding non-EU labour migration in general, the regional jobcentres are involved in a formal recognition process securing that the wage and employment condition of the relevant Danish collective agreement (circular, 1998).

Outside the field of ordinary employment, some training, education and unemployment job-activation schemes, involving employment-like qualification activities, are covered by additional legislation that lays down the process and level of wage setting. The Vocational Training Act, 2011, Paragraph 55 states that the wage during practical company training must equal the collectively agreed wage in the relevant industry. If no such wage exists, a special board may determine the wage. This board resembles the special Danish Labour Court. Both unemployed foreigners, taking part in an integration scheme (2010), and the unemployed in general are obliged to perform so-called company-practice for a maximum period of 26 weeks and only receive their normal introduction benefit, social security benefit or unemployment insurance benefit and an additional employment supplement of around 2 Euros per hour, while the practice is performed (cf. Paragraph 23b).

### **Industrial relations perspective on legislative wage settings**

Wage setting in Denmark is by and large solely left to the social partners and negotiated according to the internal strength of the social partners and the external context, such as the overall economic situation, international competition etc. Basically this system calls on a high degree of legitimacy that is achieved through the relatively high organisation rates of both employers and employees.

This has historically been the situation, although fluctuations have been experienced over the years. This relative uniformity as regards formalisation of wages and working conditions has been seen as a product of the historical non-interference on the part of the Danish state in the social partners' formal wage setting and administration. Both employers and workers have mutually and generally been satisfied with this state of affairs, which offers a relatively high level of flexibility on both sides. Thus the repeated periodical collective bargaining rounds provide both parties with frequent opportunities to connect their demands to the prevailing economic and employment situation. Furthermore, the system of social protection for laid-off workers, governed and largely financed by the state, as well as flexible hire-and-fire formalities for employers amount to an overall system of so-called "flexicurity" (Mailand, 2008).

In this context, any statutory regulation of wages would be seen as an unacceptable interference in the autonomy of the parties, creating a situation of double standards which most probably would end up blocking the most attractive regulation seen from an employers' perspective. Therefore both employers' organisations and unions have resisted any kind of statutory wage regulation outside the above mentioned special situations. Furthermore, it is a firm belief among unions that state control and sanctioning for breaches of wage and working conditions would not function efficiently, referring to experiences in other European countries that apply such models (Pedersen and Andersen 2007).

Regarding the fundamental question on pay clauses, the general Danish stance towards the statutory regulation on wages is that this is not an optimal tool for protecting and supporting ordinary employees. The dominant view is that wages set by statute would entail the risk of downgrading and freezing progressive wage developments, undermining the present system based on voluntary collective bargaining that encompasses sector level and company-level-bargaining. Leaving wage-determination to a political decision made by parliament would undermine the effective functioning of the labour market. However, in situations where the Danish labour is at risk of coming under external pressure, the social partners have accepted

legislative support. This was the case when Denmark chose to introduce the above-mentioned transitional labour market protective scheme in 2004 and 2007, when 10 countries in East and Central Europe acceded to the EU.

### **Pay clauses in public procurement law**

To some extent external pressure on national worker protection was also present when the International Labour Conference of the ILO adopted Convention no. 94 on labour clauses in public contracts in 1949. Only few years after the Second World War, the reconstruction of Europe was accelerating, generating new approaches on how to labour might be deployed transnationally.

As the convention is one of the relatively few ILO Conventions that grant access for the social partners to interfere in basically state competences, the Danish social partners were positive towards a Danish ratification of the Convention. This is emphasised because most ILO Conventions make use of shared competences including all three parties – employers, unions and state, which in a Danish context – somewhat paradoxically - often will limit the broad autonomy of the social partners if such conventions were ratified.

Ratification of ILO Convention 94 in 1956 meant that this became the first more general piece of legislation stating a minimum level of wages and working conditions that would apply when tendering for public contracts. The convention requires that public labour contracts include clauses ensuring the workers' *wages* (including allowances), *hours of work* and *other conditions of labour* are not less favourable than those established for the same kind of work in the trade or industry concerned at the location, where the work is carried out (Article 2, 1). According to the Convention, national measures for the regulation of wages and working conditions are collective agreements, arbitration awards, and national laws and regulations (Art. 2,1,a-c).

The Danish ratification in 1956<sup>11</sup> took place seven years after the adoption of the convention in 1949, 18 years before Denmark became a member of EEC. Eleven years passed before Denmark formally implemented the Convention in Danish legislation. This was done in 1966 through a circular directed at Danish state authorities, such as Ministries and their subordinate institutions, obliging them to use a clause on labour conditions set down by the Ministry of Labour after consultation of the central unions and the employers' organisations. The clause, enclosed in the circular (see Box 2.1) is designed as a fill-in paragraphing in public tendering contracts.

The circular states that main- and sub-contractors must treat workers according to the relevant collective agreement covering the performed work. If no such agreement exists, the conditions applied must be those normally applicable at the geographic location where the work is performed. The circular serves as the implementation of Convention 94, which is very elaborate on this point, foreseeing that work in a region or location might be take place without coverage by a collective agreement, collective agreements or arbitration award. In these situations, wages and working conditions must equal conditions in another region or in a similar profession (cf. ILO Convention 94, Article 2, 2).

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<sup>11</sup> Published in Law Journal C, as regulation no. 1, January 4, 1957.

### **Box 3.1: Circular communication on the application of the ILO Convention no. 94 on labour clauses in public contracts (1966)**

(Unauthorised translation of the author)

1. July 22, 1955 Denmark ratified convention no. 94 on labour clauses in public contracts, a convention adopted by the ILO International Labour Conference in 1949. The convention text is published in Regulation no. 1, January 4, 1957.

The convention states that contracts on which the convention is applicable must contain provisions (clauses) that safeguard workers' wages, working time and other working conditions, which are not inferior to conditions stated by collective agreement, arbitration award, national legislation or administrative regulations covering work of the same kind within the relevant industry or sector on the location where the work is performed, cf. the specific provisions in article 2 of the convention.

Denmark has informed the ILO that the conditions on the Danish labour market and the practice followed on the field covered by the convention – even without formal requirements equal to the convention – is seen to guarantee workers' wages and working conditions according to the convention.

However, the ILO office and the Labour Conferences' Application committee found that the formal prerequisites in the convention could not be ignored, regardless of the Danish situation.

The Ministry of Labour has negotiated the ratification of the convention with the Danish Employers' Federation (DA) and with the Danish Confederation of Workers (LO), and thus consequently requires the relevant government agencies to take the following points into consideration:

2. Contracts funded by the Danish State and agreed to by a central authority (Ministry or directly connected institution), and which regards:

construction and building work, including reconstruction, repair and demolition.

fabrication, compilation, manufacturing and shipping of materials, equipment or attachments,  
or

performing of services

are committed to enter a provision in the contract stating the obligation mentioned in the annex to this circular, as it has been negotiated with LO and DA.

If similar clauses are already used by a government agency, these can be upheld. In cases where an agency finds it necessary to use a clause containing text that deviates from the annexed paradigm this is possible if the agency avails itself to monitor if such a text is in accordance with the convention. If a deviating clause is used, the responsible government agency should – if requested – negotiate questions with the relevant employers' and employees' organisations.

Attention is directed at article 1, section 2 of the convention, according to which the government agency must decide how and to what extent the convention should be applied on contracts settled by non-central public authorities.

3. According to the Ministry of Labour (since 2001: The Ministry of Employment), the convention provisions are not applicable on contracts regarding procurement of physical products, which are part of the contractors' ordinary production or stock, unless the item is produced only for the benefit of the State.

As it follows from the convention, the clause is neither necessary if the contract sum is beneath a specific settled amount. It is the response of every government agency to state this amount after having consulted the relevant employers' and employees' organisations.

4. In every situation that requires the use of the clause, the government agency is responsible for securing that tenderers are aware of the clause. This can be done *inter alia* by inserting information about the conventions' obligations in the competitive bidding material or in the request for proposals.

The convention requires that the relevant government agency – responsible for the convention – sufficiently monitor and control its' application, cf. article 4 and the annexed paradigm. The contracting party should be requested to inform employees working on the public contract about the wage and working conditions according to the convention. Information should be easily accessible to the employees (posters at the workplace).

Ministry of Labour, May 18, 1966

Erling Dinesen (Minister)/K. Kampmann (Head of Section)

According to Article 3 of the ILO Convention, workers in public procurement contracts must be ensured health, safety and welfare. This requirement is not directly formally implemented into Danish law. However, in these fields of regulation, public provision is mainly financed through tax and therefore available to all workers legally working in Denmark. Regarding health and safety, the Danish Working Environment Act applies to all work and employment on Danish territory, regardless of the companies' or the workers' origin.

A further circular from 1990 did not add any new material rights or duties to the 1966 circular; it merely broadens the scope of the Convention, requesting the Danish Regions and Danish Municipalities to use labour clauses in building and construction contracts. The Danish Regional authorities as well as municipalities are administratively autonomous, and as the circular format is an administrative instrument, the 1990 circular leaves Regions and Municipalities to decide whether or not to follow the 1966 circular.

Furthermore, the 1990 circular encourages each Ministry to clarify the extent and procedures for the application of labour clauses in contracts concerning State companies, licensed companies and institutions. One material provision is presented in the 1990 circular as it states that the State institutions, Regions and municipalities can limit their application of Convention 94 labour clauses to contracts exceeding the threshold limit for EU tenders on building and construction projects.

### **Other Danish regulation referring to ILO-94**

Apart from the mentioned circulars, a range of Danish legislation refers to the Danish commitments on public procurement. A non-binding guide that deals with situations when municipalities and public regions perform services for other public authorities includes a reference to ILO Convention 94 regarding other issues that should be observed while tendering for public procurement (Guidance No. 107 from 30 June 1995).

It seems somewhat surprising that the Danish implementation of the EU Public Procurement Directive (2004/18/EC) does not refer to the Danish ratification of ILO Convention 94. The EU Directive refers to the core ILO Conventions: however, these do not include Convention 94. The same applies for the Danish circular on tendering and outsourcing of state operational and construction projects. In the 1994 edition of this legislation, reference is made to ILO Convention 94 in paragraph 13, stating that tenders must contain relevant information regarding labour regulation, including the Convention 94 requirement (Circular No. 42 from 1 March 1994). However, in the 2002 revised edition of the same circular, no trace of ILO Convention 94 obligations remained. The same is the case for the presently applicable circular, dating from 2010 (Circular No. 2 from 1 January 2010).

Neither the law on obtaining tenders regarding public and public supported services nor the law on building and construction projects (Law Regulation No. 1410 from 12 July 2007) have any mention of ILO Convention 94 or any other reference to labour clauses or conditions that a contractor must fulfil.

It has not been possible to ascertain exactly why Convention 94 appears to have departed from the regulation of public procurement and it is only possible, therefore, to speculate about the motives for this. One explanation might be that the reference to Convention 94 disappeared due to neglect or omission; another possibility could be that scepticism had been aroused at the administrative and governmental level concerning the compatibility between the Convention and the EU's principle of free movement.

### **Relations between labour clauses and EU-regulation**

It has been an on-going issue, whether or not ratification and implementation of ILO Convention 94 is in accordance with EU principles and regulations on free movement of labour (workers and services). Thus the question that has repeatedly been raised in a Danish

context is whether this Convention was in conflict principally with Article 56 TFEU of the Lisbon Treaty, which states that there can be no national restrictions hindering the free movement of services. As the free movement principles concern transnational movements, the EU regulation moves close to the ILO-94 convention, leaving it open if or not public authorities' requirements of specific national wages and working conditions are in conformity with the basic EU principle.

In December 2007 this question moved from being somewhat abstract and academic to become factually relevant. This was when the European Court of Justice (ECJ) in the Laval case (C-341/05) stated that Swedish legislation and labour market practice was in breach of Article 56 TFEU, when a Latvian construction company that was performing services in Stockholm was met by industrial conflict after it had declined to sign a Swedish collective agreement. Combining the EU Treaty provisions on free movement with the Directive on Posting of Workers (1996), the ECJ found that host country requirements cannot exceed the protection referred to in the Posted Workers' Directive - that is, minimum wage, working time and holiday payments - and that the directive covers only national minimum levels of protection.

The Danish social partners reacted to the verdict by amending the National Posting of Workers Act (2008), so that it now safeguards the right of the autonomous Danish labour market actors to resort to industrial conflict vis-à-vis foreign service providing companies to secure compliance with Danish collective agreements on the part of these companies. However, it is a prerequisite for this that the collective agreement covers the whole Danish territory and has been concluded by the most representative social partners in the sector. Furthermore, any entitlements in collective agreements that will not be available to posted workers must either be left out of the national agreement or capitalised into a wage amount. These so called "Laval agreements" have been applied in particular in the construction sector.

Following the amendment, there was further discussion among labour lawyers and unions and employers' organisations representatives as to whether or not the Danish solution was in line with EU law and especially the requirements of the Posted Workers' Directive. Discussions were further fuelled when it appeared that Sweden had chosen a different approach to the Laval verdict. For example, the Swedish amendments to their national legislation on posted workers prohibits the use of industrial conflict where an EU foreign service provider has submitted information showing that wages and working conditions in the company are equal to Swedish collective minimum standards. This meant that the Swedish parliament – in contrast to its Danish counterpart - actually regards collective agreements as an illegal hindrance to transnational service provision, unless such agreements serves the factual aim of securing for foreign posted workers any national employment minimum standards that fall within the range defined by the Posted Workers' Directive.

However, what really triggered doubts about the legality of the repeated Danish promotion of collective agreements that were very close to ordinary Danish agreements was the ECJ's judgment in the Rüffert case (C-346/06), which stated that national minimum standards on wages or working conditions cannot be exceeded by any local or special regulation. In the Rüffert case, the local provision enacted by the government of the *Land* of Niedersachsen was set aside as constituting an illegal hindrance to free movement, as it required that the local collective agreement was complied with for building and construction work carried out for public authorities in the state. Furthermore, this obligation was noted in the contract with the main contractor, and thus the situation corresponded very closely with the requirements of ILO Convention 94.

However, since Germany is one of the 10 EU Member States that have not ratified ILO Convention 94, the Rüffert judgment does not constitute a test of whether ILO Convention 94 is in conflict with EU free movement principles in the case of transnational European service providers.

At present the European Surveillance Authority (ESA) agreement authority has been considering a Norwegian case for litigation at the EFTA court.<sup>12</sup> The case concerns Norway's recent application of ILO Convention 94 in public contracting performed by regional authorities. However, Norway has chosen to amend the regulation so that only minimum wage and working condition requirements clauses are stated in public contracts. Additionally, only the so-called 'hardcore' requirements in the Posted Workers' Directive (cf. Article 3(1)) are included. The EEA has not yet decided whether or not to proceed with the litigation. Even if ESA decides to drop the case, it leaves Denmark with plenty of questions as to whether further amendments are needed, at least in contracts involving a service provider from an EU-country. The risks are that the legality of the Danish practice might be merely based on Article 351 TFEU which states that international obligations undertaken by Member States before affiliation to the EF/EU will be respected by the EU. Anyway, this might be a doubtfully effective defence, as the treaty also obliges Member States to remove obstacles that hinder meeting EU obligations (cf. Article 351(1) TFEU).

### **Use of pay clauses in practice**

No data exists concerning the extent to which the ILO Convention 94 has actually been used by Danish public authorities in the more than 50 years that it has been part of Danish legislation. However, its use is thought to be relatively limited. Normally, the ILO Convention is noted only when conflicts arise around the labour clauses. Danish reporting to the ILO on ratified conventions also contains only superficial information regarding problematic cases.

There are some case studies documented on the use of the ILO Convention at municipal level (Andersen-Mølgaard 2012). However, in May 2011 a Danish labour market journalist contacted all 95 Danish municipalities regarding their use of labour clauses (cf. ILO Convention 94).<sup>13</sup> He received answers from 45 municipalities. Fifteen of these replied that they used Convention 94 in procurement contracts. Furthermore, seven municipalities stated that they also used other forms of labour clauses, and one municipality was considering such a step.

Interviews with Danish trade union representatives reveal that they have not as yet been focused on Danish government authorities' formal application of the labour clauses in ILO Convention 94. Unions have approached foreign Danish and foreign companies performing work based on a public procurement contract in the very same way as they do other employers, and ask the employer to sign the relevant Danish collective agreement. This can be effected either by joining the employer organisation that is a signatory to the agreement or by way of an accession agreement signed directly with the union. This procedure actually reflects a more realistic scenario than the formal procedures stated for the Danish implementation of Convention 94. It follows that the conflict would only become politicised by a union reference to the Convention if the employer rejected the request. Furthermore, it follows from this description that unions and employers' organisation are mainly concerned about their ability to regulate the labour market by means of collective agreements. In this regard ILO-94 has only a minor and indirect role.

The status of ILO Convention 94 in Denmark is also revealed by the social partners' approach to the other material parts of the Danish implementation of the Convention. As mentioned previously, the Convention and the Danish circular state that workers performing work according to a public contract should have information about the applicable wage and

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<sup>12</sup> See also the contribution of Kristin Alsos on Norway in this study.

<sup>13</sup> This is non-published information, performed by a journalist Andersen Pedersen, while working for the trade union newsletter, 3F.dk.

working conditions through posters placed at the worksite. Such an act would be very far from the present Danish labour market culture and hardly imaginable.

Likewise, the Danish sanction for employers is mild – exclusion from obtaining a new public contract until the deficiencies have been corrected. There is no knowledge among the social partner representatives consulted as to whether this sanction has been applied. However, this is not as strange as it might seem, partly because the efficiency of unions in securing the coverage of new companies by collective agreement, and partly because, under Danish contract law, an employer's non-payment of wages gives the employees the right to cease work immediately. Furthermore, in such cases the employer risks being confronted with a bankruptcy charge.

### **Control and enforcement of pay clauses**

ILO Convention 94 provides that the national state applies sanctions on companies that breach national wage and working condition requirements. The Convention points to different options for such sanctions, including withholding payment of the contractual sum. As mentioned, Denmark has chosen a somewhat more gentle reaction, as it is stated in both the circular and in the annexed contract paradigm that the party in breach of labour condition requirements can be excluded from future similar contracts until the shortcomings are rectified. It has not been possible to find a single case in which this sanction was inflicted.

Neither the circular nor the contract paradigm settles procedures for control or measures on enforcement of the Convention, apart from the potential exclusion from future contracts.

While the Convention obliges the ratifying state to inform workers at the relevant workplace about the labour clause requirement (cf. Article 2(4)), the Danish circular states only that the public contracting party should encourage the provider to inform employees about the meaning of the labour clause. Furthermore, no specific measures are indicated in this regard.

The circular leaves it to the party issuing the tender to set a possible minimum contract amount before the labour clause applies. This requirement seems somewhat vaguer than the Convention, which in Article 1 (4) enables the authorities to exempt contracts below "a fixed limit" after negotiation with the relevant organisations.

Finally, the Article 4 of the Convention requires that an efficient scheme be introduced for monitoring and enforcement of the obligations on wages and working condition. The Danish implementing provision instructs the public contracting party to monitor suppliers' compliance with the labour clause. The Danish circulars do not take any explicit initiative on this issue. The intention seems to be that monitoring and enforcement should follow the procedures of the Danish labour market model, leaving any follow-up to the social partners through their ability to use industrial conflict to secure collective agreements with suppliers. Furthermore, enforcement within this context will be pursued through the Danish institutions for conflict resolution, mainly the Labour Court, the sectoral arbitration boards and the State conciliation board. However, in the mentioned practical examples below, it is noted that this regulation and the conflict procedures are somewhat vague and less effective in the case of foreign suppliers.

### **Example of practices**

It is fair to say that over the first almost 40 years of EU membership, Denmark was not flooded by foreign labour, possibly due to both economic and institutional factors. However, from the time of the EU enlargements in 2004 and 2007 Denmark has, for the first time,

experienced an influx of labour migrants<sup>14</sup> without precedent in modern Danish labour market history (Pedersen and Andersen, 2007; 2008).

In this recent period, pay clauses based on ILO Convention 94 have seemingly been limited and conflicts regarding foreign service providers have been almost completely absent from the public sphere. However, we refer below at the end of the following section to an example of a case that was publicly reported case as it reveals some of the challenges associated with the combination of strong regulation on pay clauses and the autonomous, voluntaristic Danish labour market model.

As previously mentioned, the perspective of “good examples” is naturally a normative one and hence justification as to the content of such an evaluation. In line with this, this study mainly considers the existing mainstream approach as being “good”, entailing that existing labour market institutions, in the broad sense of this term, are preserved to the largest extent possible, regardless of the external influence and the potential concomitant long term risks.

### ***“Good practice” example no. 1***

Based on what, therefore, could be called a conservative perspective, one case dating from 2003 seems to fall within the range of “good practice”, although the case began initially on the other side of this distinction – as a “bad example”. In Southern Jutland the Danish Regional Road Directorate had chosen a German company following a tender to renew crash fences on regional motorways. In the process of forming the tender documents, neither the directorate nor its regional branch was aware of Denmark’s ratification of ILO Convention 94 and its implementation into Danish legislation, which obliged central state authorities such as the Danish Road Directorate to apply pay clauses in contracts above a specified threshold.

As is generally the procedure in Denmark, the local union representative quickly became aware that German employees working on the site were paid below the relevant Danish collective agreed pay rates in the industry. The Danish Road Directorate is an institution under the responsibility of the Danish Minister for Transport: as a consequence, the conflict at an early stage became political at the parliamentary level. Questions were raised in the Folketinget (the Danish parliament) as to how the minister would respond to the presumed breach of the ILO Convention. In his reply to parliament, the Minister acknowledged the errors in the contract with the German company.

It was not possible to rectify the actual case, so focus remained on how to avoid a repetition. In agreement with both the Traffic and the Employment Minister, the Road Directorate modified the clause in standard tender documents related to wages and working conditions. Henceforth, the main contractor would be required to enter into an obligation to ensure that all employees at subcontracting firms would be given terms, which were not “...less favourable than those wages and employment conditions applicable at the site where the work performed”.

In order to implement the ILO Convention 94 requirements in Danish practice as efficiently as possible, the obligations were introduced in the “Special Condition 92” (SB92) appendix to the “Normal Condition 92” (AB92) standard contracts for the building and construction sector. AB92 are almost universally referred to in all Danish building and construction contracts, whereas SB92 is used more optionally and selectively for special branches. Furthermore, SB92 contains interpretations and specifications of the material content of AB92.

As follow up to the “crash fences case” a new section was included in SB92, stating that: “...work, not covered by collective agreement, cannot be awarded less favourably concerning

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<sup>14</sup> Mainly in three forms: individual labour migrants, workers posted to Denmark by foreign service providers and self-employed, one-person companies.

wages and working conditions than conditions which normally govern workers performing similar work” (see Box.3.2). SB92 stress that the obligation also regards subcontractors to the main contractor, claiming a so-called third-party liability-clause.

Furthermore, SB92 strengthens the Danish 1966 implementation of ILO Convention 94 where the circular states that contracting parties that do not apply the wage and working conditions requirement can be sanctioned through exclusion from potential future contracts until the matter is settled. SB92 thus entitles the contracting authority to withhold a part of the contractual sum for covering the employees’ legitimate claims (cf. SB, p. 19).

Through membership of the Danish Association of Construction Clients the Road Directorate has advocated a general use of the referred part of SB92 in building and construction tenders. However, it is not known to what extent this has been successful. Interviews with the relevant actors in the construction sector give the impression that contracting parties are not especially alert to this subject<sup>15</sup>.

### **Box: 3.2: Special contract condition in the building and construction sector (SB92 text)**

(Unauthorised translation by FAOS)

The new text of the SB92 (Special contract condition in the building and construction sector) as the look following the adjustment of Danish legislation after the ECJ Laval-verdict and the ECJ Rüffert verdict:

“In compliance with ILO Convention No. 94 on labour clauses, the contractor in public contracts is required to ensure that employees and any labour hired by subcontractors is guaranteed salary (including allowances), hours and other working conditions which are no less favourable than Danish collective agreements, arbitration award, national laws or regulations applicable to the work of the same type within the trade or industry in which they work.

This requirement refers to collective agreements concluded by the most representative social partners in Denmark, which apply to the entire Danish territory and the agreements having the requisite clarity indicating the payable salary.

The contractor undertakes to ensure employees, including subcontractors’ employees, work in Denmark with task performance, salary and conditions as mentioned above and is obliged to inform employees about the current working conditions.

If the contractor does not meet the above requirements and this results in a legitimate claim for additional pay from the employees, payments to the contractor in order may be withheld by the contracting authority to ensure the staff's terms of employment.”

#### **Proposed paragraphing regarding working condition clause:**

*“If employment relations regarding this contract are not covered by collective agreements at the location where the work is performed, then the payment and working conditions must not be inferior to the conditions usually granted in the industry or sector in which the entrepreneur (supplier) is active.*

*The company management is responsible for the application of these requirements.*

*Similar provisions covers work performed by a subcontractor or persons granted the responsibility to perform the contract. In these cases, the manager of the main contractor is responsible for monitoring and controlling that the clause is applied.*

*If the main contractor does not respect the convention provisions, then ..... (insert name of the government agency) can rightfully exclude the contractors access to future similar contracts until the shortcomings have been corrected.”*

Source (in Danish): [www.hnygaard.dk/Udkast%20SB-P%20for%20drift.doc](http://www.hnygaard.dk/Udkast%20SB-P%20for%20drift.doc)

<sup>15</sup> In an interview with the author, chief consultant Søren Lange Nielsen of the Danish Employers Construction Organisation and head of the collective bargaining section, Peter Hougaard, in the construction workers union (3F) did not recognise this as the general or even common Danish contracting standard.

Following the judgment of the European Court of Justice (ECJ) in the Rüffert Case, SB92 was amended in January 2009. The change was furthermore seen as a consequence of the Danish response to the ECJ Laval case (C 341/05, see above), which was understood as demanding specification and clarification of wages and working conditions that legally can be required from foreign service providers<sup>16</sup>.

### **“Good practice” example no. 2**

Another example of “good practice” in the same field also concerns the Danish Regional Road Directorate, which established a so-called Public Private Partnership Company (PPP) to handle construction of a 25 km four-lane motorway in Southern Denmark. In February 2010 a PPP-contract was signed with an Austrian consortium. Both developer and main contractor responsibility were transferred to the PPP. This road construction project is the first example of a major project in which the PPP concept aimed to combine the construction and operation of the road for 26 years. The project sum is around 2 billion Dkr. (350 Mill. euros).

The draft contract states in its general provisions (p. 15) that fulfilment of the contract requires the contractor to comply with legislation and standards as well as *international conventions regarding labour relations*. Furthermore, it is specified (p. 16) that, under ILO Convention 94, the PPP company is obliged to ensure that employees, including those of subcontractors, are guaranteed wages and special allowances, working time and further conditions of employment that should not be inferior to prevailing collective agreements, arbitration awards, national legislation and administrative provisions for the same kind of work.

Additionally the PPP contract states that the applicable collective agreement must be the one that has been agreed upon by the most representative Danish social partners, must cover the whole Danish territory and must clearly and transparently state the obligation on the level of wages to be paid. This obligation repeats what was added to the Posting of Workers Act by the “Laval-amendments” noted above.

### **“Bad practice” example no. 1**

This case is taken from the list of local municipalities that have implemented labour clauses, despite this not being a statutory requirement under Danish legislation. The Municipality of Copenhagen had introduced a clause similar to the circular 1966 model contract stating that locally-prevailing wages and working conditions should be applied by both the main supplier and any subcontractors. The contract in this case concerned the painting of a Danish public school. The main contractor subcontracted the work to an employer that was also covered by the labour clause. However, the second level subcontractor further subcontracted the work to a third level subcontractor. This subcontract did not contain a labour clause and the employer declined to sign a collective agreement for his Polish workers. However, following a large-scale industrial conflict involving both a blockade of the company itself and sympathy action from other unions directed at the employer, the employer gave in and signed the collective agreement.

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<sup>16</sup> Implemented through revision of Danish act on posting of workers (see in Danish: <https://www.retsinformation.dk/Forms/R0710.aspx?id=122901>). These changes (§6 a) state that Danish unions’ capacity to use industrial action in order to induce foreign companies to sign collective agreements requires, inter alia, that the wage demands are based on an existing collective agreement signed by the most representative social partners in the sector and that the agreement covers all Danish territory.

This case can be seen as an example of the lack of effectiveness of the implementation of the Danish ILO Convention 94 - but also the strength of industrial action in a Danish context. The case was not resolved due to the labour clause, as the Municipality of Copenhagen did not react according to the requirements of the clause by monitoring and sanctioning the breach. However, even though the company was concerned to avoid Danish collective agreements, eventually the coordinated response by the union forced the employer to concede.

### ***“Bad practice” example no. 2***

When the Icelandic artist Olafur Eliassons’ installation work (“Your rainbow panorama”) was installed at the Municipal Public Aarhus art gallery in 2009, AROS, the work was carried out by German metal and construction workers. At the point when the project was almost finalised, local unions became aware of the migrant workers’ actual wage and working conditions. The reason that the unions did not get acquainted with this situation at an earlier stage was complex. Firstly, the contract period was relatively short, leaving little time for a union reaction; and secondly, the Municipality of Aarhus and its’ Social Democratic mayor had previously, repeatedly promoted Aarhus’ application of decent working conditions in all contracts.

When the Danish construction workers’ trade union became aware of the case they found that the German migrant workers were only receiving the lowest wage in the relevant collective agreement instead of the piecework salary that would normally apply. Furthermore, the union found that the German subcontractor deducted a German statutory subsistence allowance from the wage.

A larger Danish Copenhagen lawyer firm (*Norrbom Vinding*) wrote a juridical response on the interpretation of ILO Convention 94 by the Municipality of Aarhus. The main points in the juridical response are as follows:

1. ILO Convention 94 is to be understood so that a subcontractor needs to respect the collective agreement in the construction sector, which is norm setting for the relevant kind of work in Denmark
2. The contract is concluded between the Municipality and a subcontractor, which means unions are not entitled to interfere regarding the interpretation of the collective agreement
3. This implies that the work could be performed on the lowest wage stated in the collective agreement and not as piecework payment, as it would normally be the case. Unions do not have a say in this regard.
4. The subcontractor is entitled to deduct workers expenses (German social insurance contribution, subsistence allowances paid to the workers according to German law) in their wages as ILO Convention 94 does not impede this. Furthermore, the Convention actually promotes this as it calls for the protection of workers for both wages and special allowances, including payments from the home country.
5. It is estimated that unions would not gain from lodging a complaint with the public authorities or the relevant ILO institutions, as these institutions could be expected to agree with the law firm.

The “bad” elements of this case, in regard to protection of labour, are that the case demonstrates the lack of monitoring and control in the Danish approach to ILO Convention 94. Although some of the lawyers’ conclusions can be disputed, the main challenge, however, concerns the lack of a clear structure of competence, revealing that unions have no directly formalised right to defend their own collective agreements unless they are actually

directly involved in the conflict. On a national labour market which is getting increasingly complex, with higher levels of transnational labour mobility, the task of monitoring and controlling the national labour market has become much more difficult in recent years. Companies in some sectors are crossing national borders within Europe at high speed, rendering it difficult for both authorities and unions to provide appropriate protection on the labour market for migrant as well as national workers.

### **Unions demands for further development of pay clauses**

In recent years, Denmark has experienced a revival of interest in social clauses in public contracts. This has been not least due to general societal needs in different fields. One main issue has been a lack of training places for young people in skilled and semi-skilled work. State institutions and Municipalities in larger cities have incorporated requirements in public contracts such that part of the evaluation of private partners in tenders will depend on their abilities to offer training places for young people. Recently this has generated several thousands of new training places.

Following the 2004 and 2007 EU enlargement, Danish unions and to some degree also employers' organisations have requested a greater focus on contract relations both in the private and public sector (LO 2011). Both parties in some industries have experienced a very rapid rise in the number of labour migrants and employers from the new Member States offering services at much lower levels of pay and working conditions than normally prevailing in Denmark. Some of the examples mentioned previously can be seen in this context.

The main challenges on the social dumping issue are found in the private sector, where private companies perform services for other private companies or for public authorities and institutions. As mentioned, unions are focussing on implementing demands on the issue of labour market integration – through unions and employers' organisation – as early as possible, which means incorporating this in the procurement contract. Practically, unions have tried to achieve this in the public sector through promotion of the ILO Convention 94 clause. In the private sector, in the last two collective bargaining rounds (2010 and 2012) unions have demanded a collective agreement regulation providing for an employer responsibility to only subcontract work to companies covered by a Danish collective agreement (third party liability) and a chain-liability provision making the main contractor responsible for subcontractor wage payments and working conditions set down in the collective agreement. In particular, the unions in the construction sector have been keen to achieve these demands. However, as yet they have not had much success and have only achieved the third-party liability clause in a collective agreement for a small part of the construction industry covering small employers (Jørgensen 2010).

The enhanced threat of social dumping, especially in the construction industry, in agriculture, in cleaning and transport has created political pressure on the Danish government to take action. Union efforts to secure action in this field have lately been fuelled by recent EU-level developments on the proposed instrument for implementing the Posted Workers' Directive, the proposed Monti-II declaration, as well as the recent proposals on relaxing national regulations regarding transnational access to deliver on public services of general interest.

### **Recent debates on an increased use of pay clauses to avoid social dumping**

A new Social Democrat led government came into power in September 2011. During the election campaign the new coalition argued that an enhanced strategy to respond to social dumping on the Danish labour market was needed. This proposal was in line with the wishes expressed by union representatives of both skilled and unskilled workers. In the Budget Act for 2012, it was decided to impose greater controls on companies established abroad

performing services in Denmark. The focus is mainly on whether or not they are appropriately registered in their home country. Secondly, it was decided to strengthen the control and enhance the level of fines in cases of illegal cabotage.

Thirdly, a commission for “the prevention of social dumping” was established composed by representatives of the various ministries of the Danish government as well as by the most representative trade unions and employers’ associations. The aim of this commission was mainly to explore the scope to strengthen the enforcement of legal norms on foreign companies in Denmark. Furthermore, it was required to investigate the possibilities of public authorities to use pay clauses in public procurement

In October 2012 the commission presented its report which gives an update overview on the use of pay clauses in public procurement reviews the ILO Convention 94 in relation to EU law (Danish Ministry of Employment 2012). According to the commission’s findings 59 out of 98 Danish municipalities are using pay clauses in construction solicitations, while, 51 municipalities are using them also in other types of contracting. Since 2008 all Danish regional authorities as well as all national ministries have applied the ILO Convention 94.

Regarding its conformity with EU law, the commission came to the result that the Danish ratification of ILO Convention 94 can be upheld, but the use of pay clauses have to give attention to the European Posted Workers Directive as well as to European procurement directives. Since there is no system of declaring collective agreements to be universally applicable in Denmark, the commission sees the use of pay clauses in line with EU law as long as they refer to the most representative collective agreements at national level.

Finally, the commission presented some concrete suggestions for the promotion of a more frequent use of pay clauses in procurement:

- removal of the present threshold of 37 Million Danish Kroner in construction contracts, so that labour clauses can be used regardless of the size and type of contract;
- extension of the obligation to use labour clauses in public owned companies and public institutions (hospitals, schools etc.);<sup>17</sup>
- raising local consciousness on the ILO Convention 94, e.g. through an agreement between the central government and the Danish federation of municipalities (KL) aiming to strengthen the use of pay clauses at local level;
- incorporation of the possibilities to use pay clauses in the new European procurement directives.

## Conclusion

This study has revealed that, over time, Denmark seems to have been in somewhat a circular movement around the issue of pay clauses in public contracts. Thus Denmark was among the first and the few European countries to ratify ILO Convention 94 on labour clauses in public contracts and has remained committed to the Convention. The Danish ratification of this Convention was all the more remarkable as Denmark has actually ratified relatively few ILO Conventions. One main reason seems to be that ILO Conventions are predominantly directed at tripartite labour market models, whereas the Danish model is

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<sup>17</sup> In autumn 2012 the Danish parliament adopted 2013 Budget Act which, for the first time, also includes a provision according to which state-owned companies have to use pay clauses. See agreement in Danish: [http://www.fm.dk/publikationer/2012/aftaler-om-finansloven-for-2013/~media/Publikationer/Imported/2012/Aftaler%20om%20finansloven%202013/aftaler%20om%20finansloven%20for%202013\\_pdfa\\_web.pdf](http://www.fm.dk/publikationer/2012/aftaler-om-finansloven-for-2013/~media/Publikationer/Imported/2012/Aftaler%20om%20finansloven%202013/aftaler%20om%20finansloven%20for%202013_pdfa_web.pdf), (page 51 ff).

extensively bipartite. However, Convention 94 gives the social partners unprecedented competence in a field that is normally a public affairs prerogative – that of procurement contracts.

Internally, Denmark has for decades been very harmonious on the issue of labour market organisation. On both sides – employers and employees – the organisational density has been, and still is, among the highest worldwide. So, even though the system is almost entirely voluntaristic, it has been able to produce a rather homogeneous and relatively well-functioning labour market.

This lack of anxiety about the issue of labour market regulation might additionally represent part of an explanation as to why references to Convention 94 in tendering regulation seem to gradually vanish during the 1990s and into the 2000s. Another competing or additional reason could be that the Danish administration and government representatives found the ILO Convention 94 references increasingly problematic in an EU context that was aiming at the progressive installation of the principle of free movement. Furthermore, Denmark has implemented ILO Convention 94 in a way that requires providers in public contracts to contact the relevant union or employers' organisation in order to sign a collective agreement. In this practical process, it makes little difference whether or not the contract informs a party that Danish collective agreements must be respected. The unions will need to find the company in any event in order to sign the agreement, monitor and control the actual conditions.

For many years the ILO Convention 94 seemed almost forgotten, with only ad hoc revivals in cases where the social partners found it difficult to secure a collective agreement with subcontractors in public procurement arrangements. This did not mean, however, that public contracts' were forgotten as a tool for social improvement in general. Corporate social responsibility (CSR) also looks toward public authorities and institution, and so pressure from NGOs in this field (not unions) have made both state and municipal institutions increasingly inclined to incorporate demands for hiring people with disabilities and establishing training places for young people into procurement contracts.

In recent years the pay-clause obligation in Convention 94 has received renewed attention. This development seems to a large degree to be related to the unexpectedly high influx into Denmark of labour migrants from the new EU Member States in East- and Central Europe in 2004 and 2007. Experiences have proven that at least some companies and workers from these countries are willing to perform work at wages and under working standards far below normal Danish standards, especially in construction, agriculture, cleaning and other categories of services. Additionally some companies are only in Denmark for a short period of time, leaving little scope for Danish unions to detect them and sign an agreement with them before they have left the country. Another challenge in this regard is to enforce a collective agreement in another EU country when a company has left without fulfilling its agreed obligations.

These developments, leading to an increasingly complex Danish labour market in which the social partners in general and unions in particular need assistance in the work of regulating and administering the labour market, have put the pay clause in Convention 94 back on the political and administrative agenda. During the latest collective bargaining rounds, unions in the construction sector and in transport have sought to insert third-party liability clauses and chain-liability clauses into collective agreements. As yet, employers have successfully resisted this development, and have instead given unions wider access to information and efficient follow-up mechanisms in cases of suspected irregularities regarding wages and working conditions.

One of the reasons why Danish employers have managed to obstruct new liability clauses is the uncertainty that presently surrounds the boundary between the EU principle of free movement and the right to protect national labour markets against social dumping. To some

extent this relation has for a long time triggered at least the Nordic labour market model, but nevertheless the shock effect was predominant when the European Court of Justice in December 2007 presented the Laval judgment. This stated that collective agreements obtained through the threat or use of industrial conflict are not in conformity with the EU free movement principle unless the demands are confined to the strict limits of the Posted Workers' Directive, regarding the content and level of employment conditions, and the instrument in question covers the whole industry or the designated location.

The shock of the Laval judgment for the trade unions was further exacerbated by the ECJ's 2008 judgment in the Rüffert case. This seemed to go beyond Laval, emphasising the economic and integrative potential of free movement and the need to relax any obstacles to the movement of labour transnationally imposed by regulation. By rejecting German federal state legislation, which required that public contracts were fulfilled in compliance with the requirements of the local collective agreement, the Rüffert judgment comes close to directly denying Member States the right to use pay clauses similar to the ones promoted by ILO Convention 94. However, whether Denmark will need to denounce its ratification of ILO Convention 94, at least in part, is not yet entirely clear<sup>18</sup>.

A Norwegian case which explicitly concerns ILO Convention 94 is presently being evaluated by the ESA-agreement authority as to whether the case ought to be tested at the EFTA court, which resembles the ECJ and closely follows the ECJ's case-law. Even though Norway has backed away from demanding full Norwegian labour market standards to be respected as the pay-clause requirement in Convention 94, such a case would certainly bring clarity both to the standing of Denmark's use of the Convention and furthermore about the Danish response to the Laval verdict, which led to the upholding of almost all normal Danish labour standards for foreign EU-service providers and their posted workers.

Finally, the external pressure on parts of the Danish labour market, especially from Central- and East European labour, seems to have swept some of the concerns that the Danish application of ILO Convention 94 and Danish response to the Laval judgement could be in conflict with the EU principles of freedom of movement. Thus, the new Danish Social Democrat led government has recently established a committee, one of the tasks of which is to look into Danish public authorities' and institutions' use of pay clauses and whether and how the use of such clauses could be enhanced in order to combat social dumping.

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<sup>18</sup> In the 2012 report from the commission for "the prevention of social dumping" the Ministry of Law and the Ministry of Foreign Affairs states that the Danish implementation is in conformity with all EU-legislation.

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## 4. Germany

Thorsten Schulten

### Introduction

Germany counts as one of the countries in this study with one of the longest traditions of using pay clauses in public procurement. As long ago as 1907, the German Imperial Statistical Office produced comprehensive documentation that included dozens of regional and municipal procurement regulations, all of which had some reference to the pay and working conditions of workers under public contracts (Kaiserliches Statistisches Amt 1907). Most of these procurement provisions required contracting companies to pay “prevailing” wages, and some of already referred to existing collective agreements. Some historians have even argued that in Germany pay clauses in public procurement had an important impact in promoting the emergence of a comprehensive collective bargaining system (Rudischhauser 2000).

Interestingly, a hundred years ago the arguments for the introduction of pay clauses in procurement were pretty much the same as they are today. According to another article from the year 1907, the basic assumption was that “*public procurement has an inherent tendency to push down wages. (...) In order to prevent the negative consequences of undercutting income of the workers, public contracts introduced special clauses, according to which the public authorities in one or another way keep their influence on the determination of wages for the workers which they hired indirectly*” (Abelsdorff 1907: 357, author’s translation). The instruments to prevent downward wage competition were also the same as used today: “*Either public authorities determine for the various categories of indirectly hired workers certain minimum wages on their own, or they oblige companies in public contracts to pay locally prevailing wages, as determined by collective agreements*” (ibid.).

Once a comprehensive collective bargaining system had emerged in Germany with a high level of coverage, pay clauses in public procurement lost their importance as, in most cases, contracting companies were in any event obliged to consider collective agreements. Against that background, the German government also refused to ratify ILO Convention 94 on Labour Clauses in Public Contracts in the 1950s. In the view of the German government there was simply no necessity for ratification as the principle objectives of the convention had been met through the existing system of free collective bargaining (Ruchti 2010: 140). After that, ILO Convention 94 was not an issue for decades, until most recently, in particular, the German trade unions began to call for its ratification (DGB 2012).

The issue of pay clauses in public procurement came back on the agenda in Germany in the second half of the 1990s. There were basically two related reasons for this. The first lay in changes in the German collective bargaining system, which led to a decline in coverage by collective agreements and a partial erosion of the overall structure. Secondly, there was a strong fear that increasing capital and labour mobility within Europe – especially after the EU’s Eastern enlargement – would place enormous pressure on German wage and labour standards. Against that background, around the turn of the century some of the German federal states (*Bundesländer*) started to adopt so-called *Tariftreuegesetze* (laws on ‘loyalty to collectively agreed standards’ or contract compliance provisions), according to which public contracts should be given only to those companies that applied collective agreements. In 2002, the German Federal Government even presented a draft bill for a national law on pay clauses in procurement, which, however, failed to get a majority in the Federal Assembly (*Bundesrat*) – the second chamber of the German Parliament representing the governments of the federal states. Instead, more and more German federal states passed their own regional procurement laws during the 2000s (Schulten and Pawicki 2008; Sack 2010). The

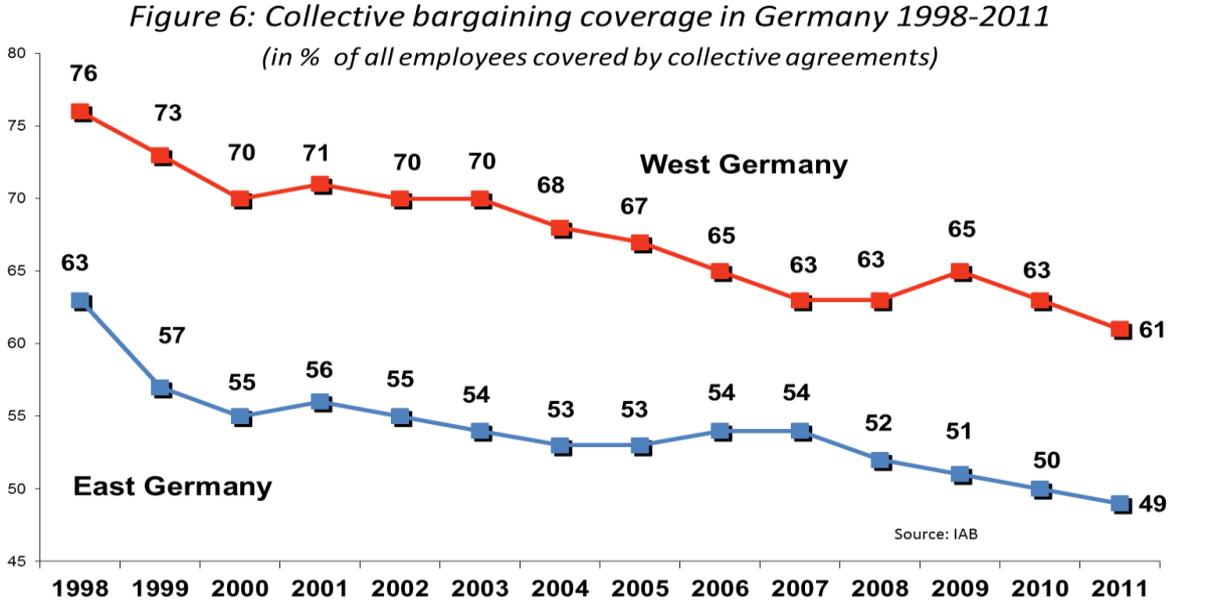
introduction of pay clauses in public procurement gained ground after a German Constitutional Court ruling in 2006 upheld the view that these clauses are in full conformity with the German constitution (Bundesverfassungsgericht 2006).

In 2008, however, this entire development came to a sudden stop after the European Court of Justice (ECJ) took its decision in the so-called Ruffert case (C-346/06). The ECJ stated that the regional procurement law of the German federal state of Lower Saxony, which required contracting companies to comply with local collective agreements, was not in conformity with EU law as it breaches the EU principle of freedom to provide services (Hänlein 2008; Kocher 2008). The problem for the ECJ was that the pay clause referred to collective agreements that were usually *not* universally applicable. According to a rather contested interpretation of the European Posted Workers Act by the ECJ, restrictions on the freedom to provide services are allowed only if these are based either on statutory minimum wages or on collective agreements which have been declared generally binding.

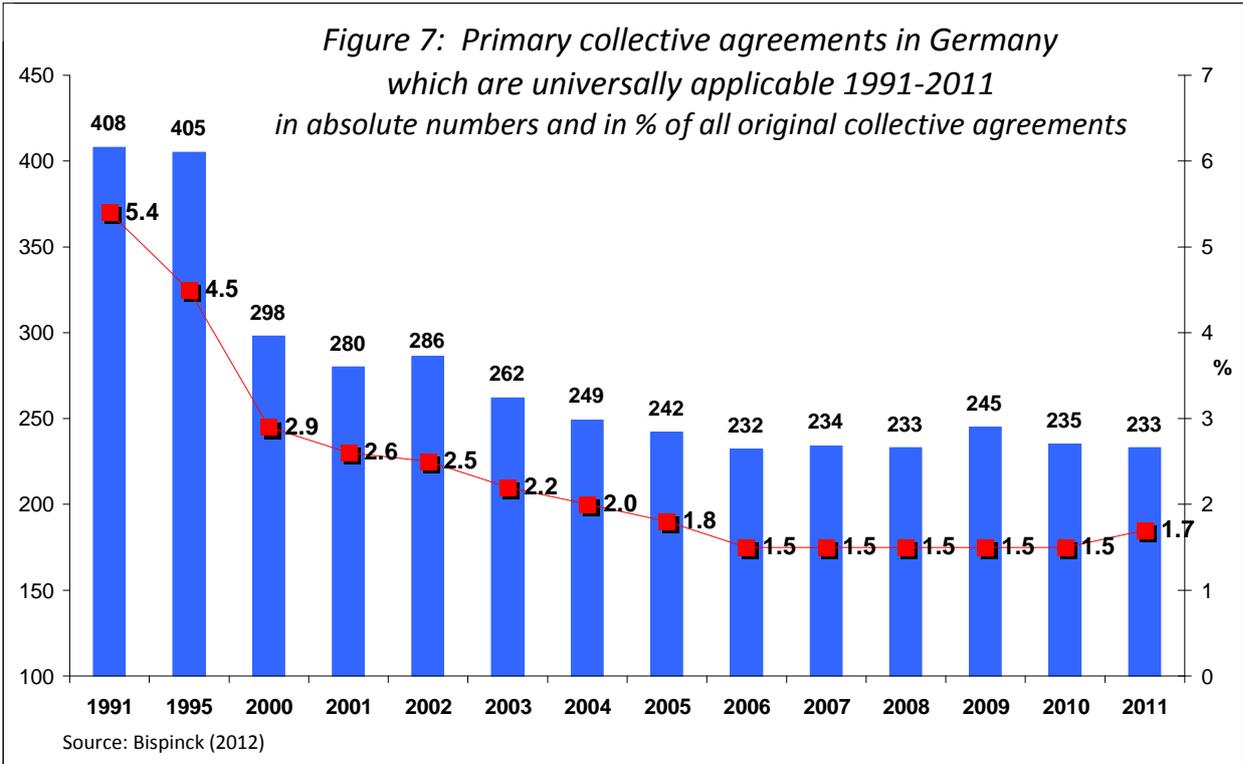
After the Ruffert judgement all German federal states initially suspended their procurement laws as they all included provisions similar to the one in Lower Saxony (Sack 2010). For a moment it appeared that with the ECJ’s ruling the whole concept of pay clauses in public contracts would disappear. Only a few years later, however, Germany has overcome the ‘Ruffert shock’ and pay and other social clauses have seen a strong revival in German public procurement policy (Schulten 2012a).

**Changes in the German collective bargaining system**

The main reason for the increasing importance of pay clauses in German public procurement can be found in the on-going changes in the German collective bargaining system. Since the mid-1990s, the German system of collective bargaining, with its traditional dominance of sector-level agreements, has been faced by a process of creeping erosion (Bispinck et al. 2010). The most obvious sign of this has been a steady decline in collective bargaining coverage over the past one-and-a-half decades. Roughly speaking, the percentage of workers covered by collective agreements has dropped from about 80 per cent in the mid-1990s to about 60 per cent in 2011 (Figure 6). The coverage is even lower in East Germany, where only half of the workforce is protected by collective agreements. A rather low bargaining coverage also exists, in particular, in many private services which – given the fact, that Germany has no statutory minimum wage – has led to a significant increase of the low wage sector (Schulten 2011).



Among the various different reasons for the decline in German collective bargaining coverage (Bispinck et.al. 2010), one of the most central is the sharp fall in the number of collective agreements which have been declared to be generally binding (Bispinck 2012). Although the extension of collective agreements in Germany has never been as important as in many other European countries (Schulten 2012b), it customarily played at least some role in stabilising the bargaining system. Since 1990, however, the percentage of primary collective agreements which are universally applicable fell from 5.4 per cent to only 1.7 per cent in 2011 (Figure 7). Moreover, most extended collective agreements are framework agreements, which set such conditions as working time and holidays: in contrast, there are only five sectors left that have generally binding **wage** agreements (Bispinck 2012).



The declining importance of using established administrative machinery to extend agreements has been compensated to only a very limited degree by the development of collectively agreed minimum wages, which have been declared to be generally binding in 13 sectors at the present time (Table 4.1). The mechanism for this is a procedure based on the German Posted Workers Act and this differs considerably from the original mechanism based on the German Collective Agreements Act. While under the older system extension applies to the entire pay scale in the agreement, in the new system only the lowest wage groups are universally applicable. Among the sectors now subject to generally binding minimum wages under the new procedure, however, there are many sectors (e.g. construction, construction related trades, commercial cleaning, waste industry, care sector, security services) for which public procurement is of significant importance. As a consequence, these minimum wages have become a point of reference in the new regional procurement laws (see below).

**Table 4.1: Sectoral minimum wages due to extended collective agreements on the basis of the German Posted Workers Act, in euro per hour**

| Sector                         | West Germany | East Germany | Sector                     | West Germany | East Germany |
|--------------------------------|--------------|--------------|----------------------------|--------------|--------------|
| <b>Care sector</b>             | 8.75         | 7.75         | <b>Painting</b>            |              |              |
|                                |              |              | non-qualified workers      | 9.75         | 9.75         |
|                                |              |              | qualified workers          | 12.00        |              |
| <b>Commercial Cleaning</b>     |              |              | <b>Roofing</b>             | 11.00        | 11,00        |
| interior cleaning              | 8.82         | 7.33         |                            |              |              |
| facade & window cleaning       | 11.33        | 8.88         |                            |              |              |
| <b>Construction</b>            |              |              | <b>Scaffolding</b>         | 9.50         | 9.50         |
| non-qualified workers          | 11.00        | 9.75         |                            |              |              |
| qualified workers              | 13.00        |              |                            |              |              |
| <b>Electrical contracting</b>  | 9.80         | 8.65         | <b>Security Services</b>   | 7.00-8.75    | 7.00         |
| <b>Further Training</b>        |              |              | <b>Waste Industry</b>      | 8.33         | 8.33         |
| pedagogic staff                | 12.60        | 11.25        |                            |              |              |
| <b>Industrial Laundries</b>    | 8.00         | 7,00         |                            |              |              |
| <b>Mining related services</b> |              |              | <b>Temporary Agencies*</b> | 7.89         | 7.01         |
| non-qualified workers          | 11.53        | 11.53        |                            |              |              |
| qualified workers              | 12.81        | 12.81        |                            |              |              |

\* On the basis of the Law on Temporary Agency Work  
Source: WSI Collective Agreement Archive (Effective October 2012)

Given the decline in the collective bargaining coverage, the revival of pay clauses in German public procurement can be understood as one attempt to stabilise the German collective bargaining system. This has also been explicitly confirmed by the principle ruling of the German Constitutional Court which states that “*the legislator can support the regulatory function of collective agreements by creating regulations which ensure that collectively agreed wages also have to be paid by employers that are not members of an employers’ association. This will serve to support the autonomous regulation of working life through associations – as intended by Article 9, Paragraph 3 of the German Constitution – by endowing pay rates set by collective agreement with more effective force*” (Bundesverfassungsgericht 2006: recital 90, author’s translation). Considering this, the use of pay clauses in procurement represents at least a partial compensation for the rather low number of universally applicable collective agreements in Germany.

### **Legal basis for German public procurement**

German public procurement regulation is based on a complex legal regime which includes various laws at national and federal-state level (Hertwig 2009; Jasper and Marx 2011). The more general guidelines are laid down in a separate chapter on procurement (Article 97-131) within the ‘German Act against Restraints on Competition’ (*Gesetz gegen Wettbewerbsbeschränkungen, GWB*). The GWB also transposes the European procurement directives into German law. The more specific regulation with the most important procedural provisions can be found in four major procurement ordinances which are the

- Award Rules for Public Contracts (*Verordnung über die Vergabe öffentlicher Aufträge*, VgV)
- Building Work Award and Contract Code (*Vergabe- und Vertragsordnungen für Bauleistungen*, VOB/A),
- Award and Contract Code for Supplies and Services (*Vergabe- und Vertragsordnungen für Leistungen*, VOL/A)
- Award Rules for Professional Services (*Vergabe- und Vertragsordnungen für freiberufliche Leistungen*, VOF)

According to the general rules of German public procurement, the competitive tendering procedure has to be carried out in a transparent and non-discriminatory manner and with contracts awarded to the “economically most advantageous offer” (*wirtschaftlichste Angebot*) (GWB Article 97, 1 and 5). As such, German procurement law explicitly does not follow a lowest-price approach, but calls for a more comprehensive evaluation that also considers possible follow-up costs.

As far as social aspects are concerned, German procurement law states that public contracts can only be given to “companies that comply with the law”, including social and labour laws. Moreover, there is a general provision that public authorities can determine additional award criteria which might include social (as well as environmental and innovative) aspects (GWB Article 97, 4). However, these additional award criteria can only be applied if they have been determined in additional laws at national or federal state level (*ibid.*). This latter provision has set the legal basis for the development of several new regional procurement laws within the various German federal states, which has led to the renaissance of pay clauses in German public procurement (Schulten 2012a).

### **Spread of pay and other social clauses in German public procurement**

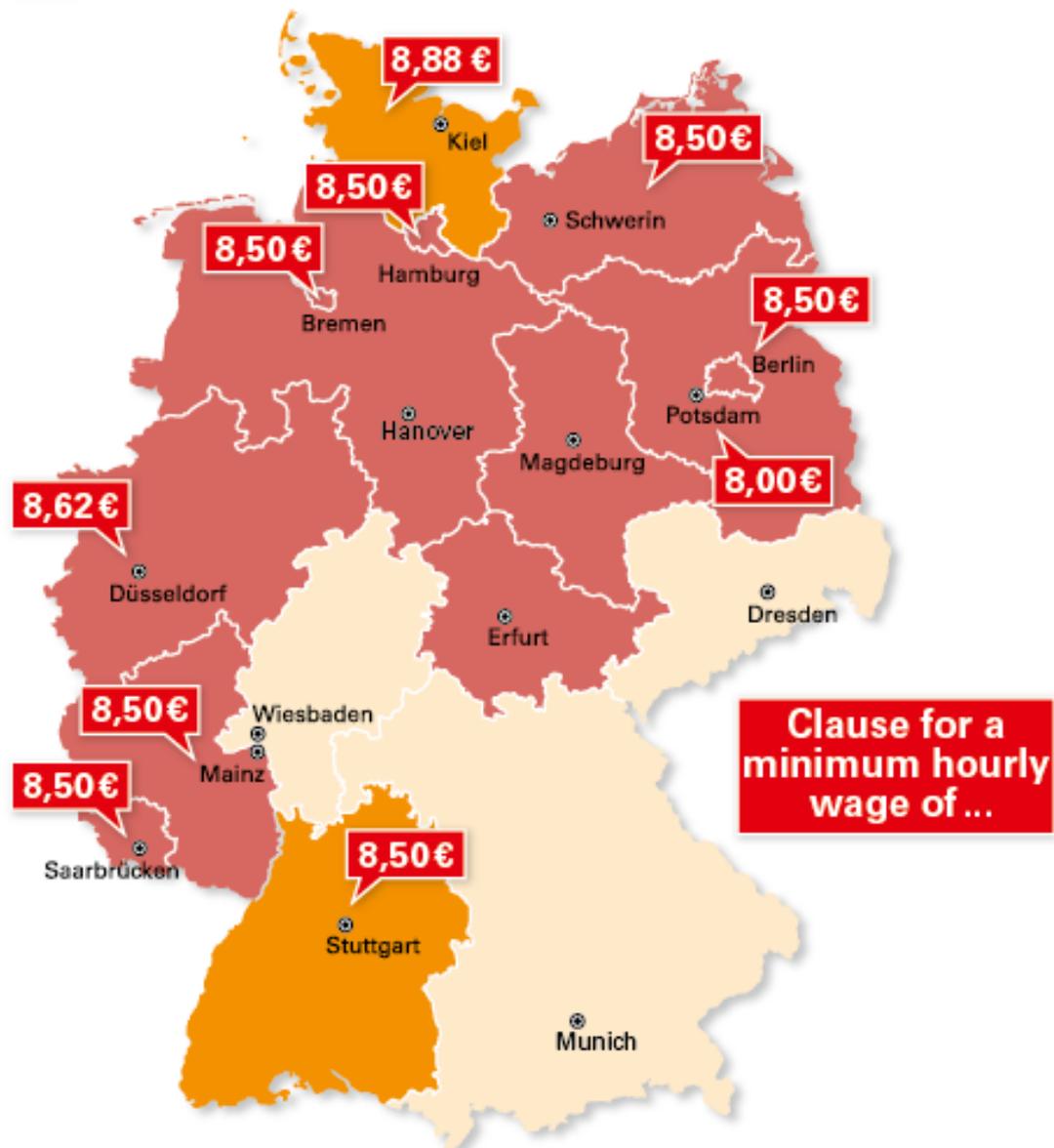
In order to determine social, and mostly also environmental, requirements for public procurement, since 2008 more and more German federal states have either revised their regional procurement laws in the aftermath of the Ruffert judgement or adopted completely new procurement legislation. By November 2012, 11 out of 16 federal states had concluded new regional procurement laws. Among them are the three city-states Berlin, Bremen and Hamburg as well as Brandenburg, Lower Saxony, Mecklenburg-Vorpommern, North Rhine-Westphalia, Rhineland-Palatinate, Saarland, Saxony-Anhalt and Thuringia. There are two further federal states (Baden-Wuerttemberg and Schleswig-Holstein) where in which governments have already presented draft bills for new procurement laws, so that 13 out of the total of 16 states will soon be covered by some legislation on socially-responsible procurement. For the moment, the only exceptions are Bavaria, Hesse and Saxony.

In comparison to the earlier legislation, the new procurement laws of the post-Ruffert-Era are in many respects more advanced, although they have had to consider the limitation set by the Ruffert case. While the older laws were often limited to a very few sectors, such as construction or public transport, the new laws usually cover public contracts in all sectors. The only exceptions are usually set by a certain minimum threshold for the value of the contract, which varies from 10,000 to 50,000 Euro. The new procurement laws also contain a much broader spectrum of social requirements, including not only pay clauses but also employment and gender equality issues (see also Annex 1 and 2 to this chapter). As a general reference to the application of local collective agreements is no longer allowed, following the ECJ’s judgment, the new public procurement laws contain three forms of pay clauses which, according to the German law makers, are still in conformity with EU law.

# Pay clauses in German public procurement law

Public procurement law in German Federal States

- with pay clauses,
- with plans to introduce pay clauses,
- with no pay clauses



Effective November 2012; Source: WSI Collective Agreement Archive 2012  
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*First*, in sectors where there are generally applicable collective agreements, companies are obliged to declare in their bid for the public contract that they pay their workers at least the pay rate laid down in these agreements. Although the extension of collective agreements is not very common in Germany, there are 13 branches (among them relatively important sectors such as construction, commercial cleaning, security services and care services) with collective agreements that set sector-wide minimum wages that have been declared to be generally binding on the basis of the German Posted Workers Act (see above Table 4.1). Although these collective agreements have to be considered anyway, their introduction into the procurement laws has been justified by the fact that this would ensure that they would receive more attention in the tendering process and create new opportunities for their control and enforcement.

*Secondly*, in the public transport sector companies operating under public contracts must accept the full provisions of locally prevailing collective agreements, even if these agreements are not generally applicable. Such special treatment of the public transport sector is permissible because it has a special legal status in EU law (TFEU, Article 90 -100), according to which the freedom to provide cross-border services is subject to some restrictions in that sector. Consequently, the Rüffert case does not apply to public transport (Denzin et.al. 2008). Moreover, there is a special EU regulation on public transport (EC No 1370/2007) which explicitly allows Member States to make reference to collective agreements in the tenders *“to ensure transparent and comparable terms of competition between operators and to avert the risk of social dumping”* (European Parliament/EU Council (2007: 3).

*Thirdly*, most German federal states have introduced a procurement-related minimum wage. Since Germany still has no national statutory minimum wage, the federal states have used the scope offered by public procurement law to ensure that all companies operating on public contracts are obliged to pay their workers a certain minimum rate. There have been some debates among German lawyers on whether or not such procurement-related minimum wages are in conformity with EU law, in view of the constraints imposed by the Rüffert judgement. A majority, however, has taken the view that these minimum wages are covered by the European Posted Workers Directive (Bayreuther 2008; Schmid and Rödl 2008; Oeter 2009; Rödl 2011). The latter has also been confirmed by the European Commission, which has stated in an answer to the European Parliament that the procurement-related minimum wage as laid down in Article 4 (3) of the Collective Agreement and Public Procurement Act of North Rhine-Westphalia (TVgG - NRW) *“is significantly different from the provision at stake in the Rüffert judgment ... (as it) sets a concrete minimum wage by law”* (Andor 2012).

Currently, six federal states (Berlin, Brandenburg, Bremen, Mecklenburg-Vorpommern, North Rhine-Westphalia and Rhineland-Palatinate) have introduced a procurement-related minimum wage, while there are four further states (Baden-Württemberg, Hamburg, Saarland and Schleswig-Holstein) which will introduce it in the near future. The amount of the minimum wages differs from state to state, ranging between 8.00 Euro and 8.50 Euro per hour. The highest minimum wage, with an hourly rate of 8.62 Euro, has been concluded in North Rhine-Westphalia which corresponds to the lowest pay grade in the collective agreement for the public sector. Following the same logic, the state of Schleswig-Holstein plans to introduce a procurement-related minimum wage of 8.88 Euro per hour, as the regional public sector collective agreement for that state provides for somewhat higher wages. Finally, some federal states have agreed to set up Minimum Wage Commissions composed of employers, trade unions and sometimes independent experts whose task is to advise the regional government on any adjustment or updating to be made to the procurement-related minimum wages. As a result of this, the government of Rhineland-Palatinate, for example, decided to follow the recommendation of its regional Minimum Wage

Commission and will increase its procurement-related minimum wage from 8.50 Euro to 8.70 Euro per hour in January 2013.

Procurement-related minimum wages are expected to have a particular effect on those sectors which are either not covered by any collective agreement or where collectively agreed wages are very low as, for example, in security services, gardening and landscaping, catering or parts of the postal services. For these sectors the procurement laws are intended to stop the payment of indirect subsidies to low wage earners in contracting companies. As the wages of workers under public contract have often been below the official subsistence level, these workers have the right to receive additional in-work state benefits. The latter has been often the case, for example, in the postal services where, after the liberalisation of the letter market, new postal companies paying extremely low wages often took over the delivery of official mail (Input Consulting 2009). This led to the rather absurd situation that the state could save some money through contracting to somewhat cheaper new postal companies on the one hand, while at the time having to spend more money on transfer payments on the other.

Apart from pay clauses, many of the new regional public procurements laws define further social criteria which have to be taken into consideration when choosing a contracting company. To different degrees the regional procurement laws consider

- measures for the promotion of equal opportunities and gender equality;
- the promotion of vocational training places;
- the employment of disabled workers;
- the employment of long-term unemployed;
- the promotion of equal pay and conditions for temporary agency workers

Furthermore, most regional procurement laws make reference to the eight core ILO Conventions (covering freedom of association and right to bargain collectively; prohibition of forced labour and of child labour, and non-discrimination in employment and occupation), according to which public authorities should ensure that purchased goods have been produced in observance with ILO core labour standards (CorA 2010).

## **Enforcement of pay and other social clauses in procurement**

In many federal states the adoption of pay and other social clauses in regional procurement laws took place in the face of resistance from employers' and business associations. They were also supported by some academics who regard social requirements as "factors extraneous to procurement" and who criticise such provisions for undermining an efficient tendering process and making public contracts more expensive (Bundesministerium für Wirtschaft und Technologie 2007; Prieß and Friton 2012). Furthermore, the opponents argue that including social award criteria would generate a great deal of bureaucratic effort that would overtax the capacities of the contracting authorities. Since the latter would often not be able to monitor social requirements, in practice these would often be simply ignored.

Since many of the new regional procurement laws in Germany have been adopted only quite recently, there is, as yet, only limited knowledge about the implementation and enforcement of these laws.<sup>19</sup> Moreover, there are also almost no studies on the implementation of the older procurement laws dating from the 2000s. The only exceptions are two evaluation

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<sup>19</sup> In November 2012 the Institute for Economic and Social Research (WSI) within the Hans Böckler Foundation started a three-year project on the implementation of the pay clauses in procurement in the federal states of Berlin, Bremen, North Rhine-Westphalia and Rhineland-Palatinate.

studies, one from North Rhine-Westphalia (Stefaniak and Vollmer 2005) and one from Hamburg (Hamburger Senat 2007). Both studies are based on surveys of companies and contracting authorities and cover mainly the construction industry.

First of all, both studies came to the conclusion that a great majority of the companies were supportive of pay clauses in procurement, which they saw as a reasonable instrument to prevent competition through mutual undercutting within the tendering process. In North Rhine-Westphalia, pay clauses, which referred to prevailing local collective agreements, were supported by 84 per cent of the surveyed companies (Stefaniak and Vollmer 2005: 35). The support was even greater in Hamburg, where only 3 per cent of companies said that the pay clauses were not useful. In fact, 80 per cent of the responding companies declared that they had directly gained from the application of this instrument. Contrary to the view of the critics, 90 per cent of responding companies said that the social requirements in the regional procurement law created no additional administrative work for them (Hamburger Senat 2007).

Regarding the control of pay clauses, however, the evaluation study from North Rhine-Westphalia found significant shortcomings. Nearly 80 per cent of the 139 surveyed contracting authorities declared that they were not able to control whether the contracting companies paid the appropriate wages (Stefaniak and Vollmer 2005: 31). Moreover, only 34 per cent of the surveyed companies said that the calculations in their tender documents were monitored by the contracting authorities (ibid: 42). According to the contracting authorities, the main reason for the low level of surveillance was the lack of sufficient qualified staff (ibid.: 27).

Somewhat different experiences regarding the surveillance of pay clauses were encountered in Hamburg. After the adoption of the regional procurement law, the governing authority of Hamburg established a new department for the control of wages in contracting companies. The so-called „Soko-Bau“ has ten employees, whose main task is to monitor employment documentation directly in the companies and at construction sites (Hamburger Senat 2007: 12). With the establishment of this new surveillance department, the governing authorities in Hamburg were able to carry out a large number of controls, which at the same time led to a high level of acceptance among the contracting companies affected (ibid: 14).

In addition to the two evaluation studies from the 2000s, there is also a lot of anecdotal evidence from media reports that there are still significant problems in enforcing the social requirements of the procurement laws. In October 2010, for example, the so-called FAIRgabe-Bündniss in Berlin – an alliance of trade unions and other NGOs dealing with procurement issues – found out that even after 100 days following the coming into force of the new procurement law for Berlin, there was still no reference to the new social requirements in tender documents (Berliner FAIRgabe-Bündniss 2010).

In order to improve the enforcement of pay and other social clauses most regional procurement laws contain detailed provisions on the right and sometimes even obligation of the contracting authorities to monitor contracting companies. The latter holds true in particular for the case of an “abnormally low offer”, usually defined as an offer which is at least 10 per cent below the next lowest offer. Some federal states (e.g. Bremen or North Rhine-Westphalia) decided to follow the example of Hamburg and create their own surveillance institutions for workers under public contracts. Finally, contracting companies, which offend against the social procurement requirements, have to pay a fine and can be excluded for a certain period (usually up to three years) from further tender processes.

Besides the surveillance by the state there is also a role for trade unions and other NGOs in supporting the enforcement of a socially responsible procurement policy. The United Services Union Ver.di, for example, is currently a campaign called “fairsenden“ (fair delivery) which aim to push pressure on public authorities to contract only with postal companies which provide fair wages (Ver.di 2011, see also: <http://psl.verdi.de/postdienste/fair-senden>).

In addition to that there are also many NGOs in Germany that are particularly active in the field of core labour standards and aim to convince public authorities when ever possible to purchase fair trade products (CorA 2010).

## **Conclusion**

Despite the Ruffert case, in recent years Germany has seen a major revival of pay and other social clauses in public procurement. There is a growing awareness that the more than 400 billion Euro spent every year for public contracts should be used in a socially (but also environmentally) responsible manner.

In practice, however, there are also still many public authorities which – in view of their financial constraints – simply follow the lowest-cost approach and do not care so much about social award criteria. There is obviously a need to improve the enforcement and control of the new regional procurement laws.

One special feature in German public procurement is also use the widespread use of pay clauses for workers under public contracts. Given declining collective bargaining coverage, pay clauses in procurement are also seen as one instrument to re-stabilise the German collective bargaining system. In this respect the Ruffert judgement has set some significant limits as it allows only references to universally applicable collective agreements (with some exceptions in the public transport sector). This is rather problematic as the extension of collective agreements is not very widespread in Germany,

In order to compensate the limits set by the Ruffert judgement, the public authorities have begun to adopt procurement-related minimum wages. This is, however, only a partial compensation for the limits imposed by the Ruffert judgment, as minimum wages only covers the lowest wage groups. If pay clauses in public procurement are to fully serve their intended role of securing fair wages and fair competition, it is essential that they should be allowed to make reference to locally prevailing collective agreements, regardless of whether they are legally declared to be generally binding. This is exactly the idea contained in ILO Convention 94, ratification of which has now been put on the agenda by the German trade unions in order to overcome the limits set by the Ruffert judgement (DGB 2012). After the Ruffert case, however, the relationship between ILO Convention 94 and EU laws has become rather uncertain and urgently requires clarification at EU level.

## Annex 1: German federal states with regional procurement laws

|                        | Regional procurement law  | Universally applicable collectively agreed minimum wages | Prevailing local collective agreements in public transport | Procurement related minimum wage in Euro per hour | ILO core labour standards | Other social requirements                              |
|------------------------|---|--|--|---|---------------------------|--|
| Berlin                 | <i>Berliner Ausschreibungs- und Vergabegesetz</i> from 8 June 2010                        | Yes  | Yes  | 8.50  | Yes                       | Gender equality, vocational training                   |
| Brandenburg            | <i>Brandenburgisches Vergabegesetz (BbgVergG)</i> from 21 September 2011                  | Yes  | Yes  | 8.00  | No                        | None   |
| Bremen                 | <i>Tariftreue- und Vergabegesetz</i> from 24 November 2009                                | Yes  | Yes  | 8.50  | Ja                        | Gender equality, vocational training, disabled workers |
| Hamburg                | <i>Hamburgisches Vergabegesetz (HmbVgG)</i> from vom 27. April 2010                       | Yes  | No   | 8.50*   | Ja                        | None   |
| Mecklenburg-Vorpommern | <i>Vergabegesetz Mecklenburg-Vorpommern (VgG M-V)</i> from 28 June 2011                   | Yes  | Yes  | 8.50  | Ja                        | None   |
| Lower-Saxony           | <i>Niedersächsisches Landesvergabegesetz (LVergabeG)</i> from 15 December 2008            | Yes  | No   | None  | No                        | None   |
| North Rhine-Westphalia | <i>Tariftreue- und Vergabegesetz Nordrhein-Westfalen (TVgG-NRW)</i> from 10. January 2012 | Yes  | Yes  | 8.62  | Yes                       | Gender equality, other issues possible                 |

\* draft bill for introduction is adopted

Source: WSI

**Annex 1: German federal states with regional procurement laws (continue)**

|                      | <b>Regional procurement law</b>  | <b>Universally applicable collectively agreed minimum wages</b> | <b>Prevailing local collective agreements in public transport</b> | <b>Procurement related minimum wage in Euro per hour</b> | <b>ILO core labour standards</b> | <b>Other social requirements</b>                           |
|----------------------|--|---|---|--|----------------------------------|--|
| Rhineland-Palatinate | <i>Landesgesetz zur Gewährleistung von Tariftreue und Mindestentgelt bei öffentlichen Auftragsvergaben (LTTG) from 17. November 2010</i> | Yes   | Yes   | 8.50   | Yes                              | Gender equality, vocational training, long-term unemployed |
| Saarland             | <i>Saarländisches Vergabe- und Tariftreuegesetz from 15 September 2010</i>   | Yes   | Yes   | 8.50*  | Yes                              | None   |
| Saxony-Anhalt        | <i>Landesvergabegesetz Sachsen-Anhalt (LVG LSA) from 18 October 2012</i>   | Yes   | Yes   | None   | Yes                              | Gender equality, vocational training                       |
| Thuringia            | <i>Thüringer Vergabegesetz (ThürVgG) from 15. April 2011</i>   | Yes   | Yes   | None   | Yes                              | Gender equality, vocational training                       |

Source: WSI

## Annex 2: German federal states with draft bills for regional procurement laws

|                    | Regional procurement law   | Universally applicable collectively agreed minimum wages | Prevailing local collective agreements in public transport | Procurement related minimum wage in Euro per hour | ILO core labour standards | Other social requirements |
|--------------------|--|--|--|---|---------------------------|---------------------------|
| Baden-Wuerttemberg | <i>Landestariftreuegesetz Baden-Württemberg</i> (LTTG) from 18 April 2012            | Yes  | Yes  | 8.50  | No                        | None                      |
| Schleswig-Holstein | <i>Tariftreue- und Vergabegesetz Schleswig-Holstein</i> (TTG) from 12 September 2012 | Yes  | Yes  | 8.88  | Yes                       | Possible                  |

Source: WSI

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## 5. Norway

*Kristin Alsos*

### Introduction

Public procurement in Norway amounts to NOK 400 billion (€ 50 billion) a year, and 70 percent of municipalities have outsourced services to private service providers. Norway takes part in the internal market as a party to the Agreement on the European Economic Area (EEA). Consequently Norway has to act in accordance with the EU regulations on public procurement.

The 2004 revision of the EU regulations on public procurement fell together with the enlargement of the EEA area eastwards. From May 2004 to August 2007, the Nordic countries had granted a total of more than 150 000 work permits to citizens of the New EU member states, in addition to more than 75 000 renewals. Nearly half of all first-time permits was issued in Norway (Dølvik and Eldring 2008). The high inflow of workers and service providers from NMS led to a demand in Norway on introducing new measures to combat social dumping, a stricter implementation of ILO Convention No. 94 being one of them.

The socialist/centrist coalition government has, since the enlargement, introduced two action plans against social dumping. The first, presented in May 2006 included measures as introducing identification cards in the building industry, improving the enforcement of generally applicable collective agreements, strengthening the sanctions at the disposal of the Labour Inspectorate, as well as implementing ILO Convention No. 94 for municipalities and county authorities. Further measures were introduced three years later when the second action plan was introduced. One of the key measures of this action plan was to develop a model for joint and several liability in areas where collective agreements are made generally applicable.

This paper will look at pay clauses in public procurement in Norway. That is, the implementation of ILO Convention No. 94 into Norwegian law, and the first part will focus on the Norwegian implementation and enforcement procedures (or lack of such). In the aftermath of the European Court of Justice's ruling in *Rüffert* (Case C-346/06) the European Surveillance Authority (ESA) has had a closer look at the Norwegian regulation, and their assessment will be described in the following section, as well as the Norwegian responses. Finally, this paper also aims to describe some bad and good experiences by the use of pay clauses in public procurement. However, first I will give a short introduction to minimum wage regulation mechanisms in Norway.

### Minimum wage regulation mechanisms in Norway

In Norway, as in the other Scandinavian countries, low-wage-regulation is mainly handled through collective bargaining, with minimum-wage floors established in collective agreements. No statutory (national) minimum wage exists. However, the EU enlargements in 2004 and 2007 have put pressure on the existing regulating regime, and revealed that the Norwegian regulation model lacked efficient systems to tackle low-wage competition, especially within some industries. A precondition for demanding an implementation of a collective agreement is that not less than ten percent of the employees in the enterprise within the agreement sector are organised in the trade union.<sup>20</sup> The trade union density in

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<sup>20</sup> See for instance the Basic Agreement 2010-2013 LO-NHO § 3.7. For enterprises that are not members of an employer organisation an implementation of an agreement requires consent. Consent

Norway is just above 50 percent, but with great diversity between public and private sector. 81 percent of employees in the public sector are members of a trade union, compared to only 40 percent of the private sector employees. The share of employees covered by collective agreements is higher, 100 percent in the public sector and around 55 percent in private sector, an average on 70 of all employees. Also within the private sector the differences are large between industries. 33 percent of employees of commercial service providers are unionised and only 15 percent of employees within the hospitality industry (Nergaard Aarvaag Stokke 2006). Combating low-wage competition through concluding collective agreements in these subsectors is obviously a very difficult task.

As Norway entered the EU internal market through the EEA agreement in 1994, the trade unions feared that this could lead to a high inflow of workers from southern part of Europe, and as a consequence increased low-wage competition. LO therefore initiated an act on general applicable collective agreements. The act<sup>21</sup> came into force at the same date as the EEA agreement. However, the scenario of a wave of southern European low-cost workers failed to materialise, and the act was inoperative until the EU-enlargement in 2004.

Compared to other countries with *erga omnes* measures, universally applicable collective agreements in Norway are not widespread. As for 2011 only three collective agreements are made generally applicable; covering the agricultural sector, construction and ship building and cleaning. Furthermore, only certain key provisions in the collective agreements are made generally binding, in particular minimum wage, supplements for overtime work or work time arrangements, travelling expenses, board and lodging expenses, and depending on the industry working time. The decision to make an agreement generally applicable is taken in the form of an administrative regulation, where the specific conditions are listed.

As a part of the government action plans against social dumping, several measures to enforce general applicable collective agreements have been introduced – many of these initiated by the Norwegian Confederation of Trade Unions (*Landsorganisasjonen i Norge*, LO). Firstly, the Labour Inspectorate Authority has been given new measures in order to enforce the legally extended collective agreements. This includes giving orders, halting of work and imposing coercive fines. Secondly, enforcement powers and duties have also been given to both trade unions and contracting companies. These enforcement measures include:

- a duty for the main contractor to ensure that generally applicable collective agreement is complied with,
- an obligation for the employer that engages the main contractor to give information on the applicable conditions,
- a right for the shop stewards of the main contractor to check whether conditions are applied with in sub-contracting companies, and
- joint and several liability where conditions are not complied with.

## **Pay clauses in public procurement**

Norway ratified ILO Convention No. 94 in 1996. Until the EU enlargement in 2004, the government did not see the need to adopt any specific regulations in order to comply with the convention. However, as the 2004 enlargement led to a massive inflow of Eastern European

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may be reached through industrial dispute, see Act of 5<sup>th</sup> May, 1927, No. 1 relating to labour disputes §6 (3).

<sup>21</sup> Act of 4 June 1993 No. 58 relating to general application of wage agreements etc. (General Application Act.)

workers and companies to Norway, and to some extent low-wage competition, the government decided to instruct central authorities to follow the regulations in the convention. In June 2005, a binding circular issued by the Ministry of reform (*Moderniseringsdepartementet*, now Ministry of Government Administration, Reform and Church Affairs, *Fornyings-, administrasjons- og kirke departementet*) was adopted (Moderniseringsdepartementet 2005). According to this circular contracts covered by the circular should include a clause ensuring workers' pay and working conditions that are not less favorable to what is normal for the relevant profession and place. The circular further put down enforcement measures, and a proposal on how clauses could be drawn up.

According to the circular all central authority's contracts included in the Public Procurement Act<sup>22</sup> were covered. That is procurement of goods, services and building and construction work above the threshold values, (NOK 1 million (€ 125 000) for central authorities).

As a part of the government action plan 1 to combat social dumping<sup>23</sup>, pay clauses in public procurement were extended to cover procurement by local authorities. This was implemented through an amendment of the Public Procurement Act in December 2007, giving the ministry authority to adopt administrative regulations on wages and working conditions in public contracts. Due to an ESA infringement case (see below), the regulation was amended in November 2011. In the following I will first present the regulation as it was originally adopted, before the amendments are presented.

In the reasoning for extending the regulation to local authorities it is stated:

*“After the EEA enlargement in May 2004 there has been a strong increase in the labour migration into Norway. There is a common agreement among the social partners and the government that the increase in the number of labour immigrants so far has contributed in a positive way to the Norwegian economy by meeting a need for labour force in several industries, the construction industry in particular.*

*However, there have been reports on increasing problems related to unscrupulous contractors and social dumping. There are a lot of examples on foreign workers been given unacceptable wages and working conditions, particularly in the construction industry. The problems seem above all to be related to service providers. ...*

*Thus, it is important that we have regulations that supports serious players and ensures that also foreign workers are entitled to decent conditions on the Norwegian labour market.” (Own translation) (Fornyings- og administrasjonsdepartementet)*

This objective was also referred to in the administrative regulation § 1, where it said that the regulation shall contribute to make sure that employees in undertakings that provide services and construction work on behalf of public authorities do not have wages and working conditions that are less favorable to those stated in a national collective agreement or otherwise established for work of the same character in the trade or industry concerned in the district where the work is carried out.

The regulation covers public procurement by the central government, counties, municipalities, bodies governed by public law, public supply enterprises and private enterprises that have been granted concessions in specific utilities sectors (oil companies). Call for tenders on service or construction contracts that exceed NOK 1 million (€ 125 000) for central authorities and NOK 1.6 million (€ 200 000) for other entities shall include a clause obliging the contractor and sub-contractors to ensure that employees have “Norwegian” wages and working conditions. The regulation reads:

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<sup>22</sup> Act of 16 July 1999 no. 69 on public procurements.

<sup>23</sup> St. meld. nr. 2 Revidert nasjonalbudsjett 2006.

*Contracting authorities shall impose as an obligation in their contracts a requirement that workers hired by the contractors and potential sub-contractors that contribute directly in fulfilling the contract, receive pay and working conditions which are less favorable than stated in the applicable nationwide collective agreement, or what is otherwise normal for the relevant place and profession. This applies also to work performed abroad. (Own translation)*

If there exists a generally applicable collective agreement this should be used as a basis. If several collective agreements exist in the same area, all agreements should be taken into account (Fornyings- og administrasjonsdepartementet 2008). Where no agreements are found, one should undertake a discretionary assessment of whether the conditions in the company in question can be said to be in accordance with work of the same character. In this assessment the public entities can look to open sources as information from trade unions or other available sources (Fornyings- og administrasjonsdepartementet 2007).

By wages and working conditions the Ministry understood provisions on pay and working hours. Pay is related to the minimum wage or normal wage rates fixed in the collective agreements, but could also include overtime payment, shift bonus and more. It was not expected that the entities shall define a fixed wage level, but rather assess whether the wage level in the company in question can be defined as “normal” when related to the geographical area and profession (Ot. prp. nr. 7 (2007-2008))

Furthermore employers may demand documentation to check the fulfillment of this clause. Public entities also have the right to sanction non-compliance with the clause. This may include detaining part of the remuneration, revocation of the contract and more.

### **ESA infringement case**

The EFTA Surveillance Authority (ESA) opened in July 2009 a case with regard to the Norwegian regulation on pay clauses.<sup>24</sup> The decision came as a consequence on the ECJ judgment in *Rüffert*, and was based on the provision obliging public entities to demand certain wage and working conditions. The enforcement provisions were not part of the case. ESA compared the Norwegian regulation to that in *Rüffert* and concluded that the Norwegian regulation was in breach of the posting of workers directive (PWD) as well as the EEA agreement article 36 (similar to article 49 EC). The decision was followed by a reasoned opinion by the ESA in June 2011, giving the Norwegian state two months to take necessary measures to comply with the opinion.<sup>25</sup>

Regarding PWD ESA finds that the Norwegian regulation is not constructed in a way described by the directive. The regulation does not itself fix any minimum rates of pay, and neither does it refer to collective agreements that have been made universally applicable in accordance to Article 3(8) of the directive. Moreover, the term “normal” does not correspond to the term “minimum rates of pay” in the directive. As for article 36 EEA, the provision was considered to constitute a restriction on the freedom to provide services that could not be justified:

*“However, Article 5(1) of Regulation No. 112/2008 applies only to public contracts and not to private contracts. As in Rüffert, Norway has not demonstrated why the objective of preventing social dumping, and consequently the protection of workers, is only necessary in respect of public contracts and not private contracts.”<sup>26</sup>*

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<sup>24</sup> Letter of formal notice to Norway for failure to ensure compliance with Article 36 EEA and Directive 96/71/EC. Event No. 501425).

<sup>25</sup> ESA, Reasoned opinion, Event No. 574000.

<sup>26</sup> Event No: 501425.

The Norwegian government argued as since Germany has not ratified ILO 94, ECJ had not had the opportunity in *Rüffert* to examine the obligations that the Convention imposes on Member States of the ILO who have ratified it. ESA did not find this argument very weighty, but stated that *implementing legislation required by such agreements must respect their obligations arising from the EEA Agreement.*<sup>27</sup>

## **The Norwegian response - amendment of the regulation**

The Norwegian government has responded to the Letter of formal notice by amending the regulation in November 2011. However, the main contents of the regulation is intact. The main amendments are:

- The regulation now makes it clear that it is the *minimum* rates of pay stemming from nationwide collective agreements that are to be complied with. This means that only minimum rates stated in the collective agreements are covered, and the public entities do not have to look to average wage levels. This is just a clarification of how this regulation was practiced earlier on. "Minimum rates of pay" does as before the amendment also cover overtime payment, shift bonus and more. However, this is now explicitly stated in the regulation.
- In sectors that are covered by regulations that declare collective agreements generally applicable, the regulation makes reference to the pay and working conditions that stem from these regulations. The condition related to *what is otherwise normal for the place and profession concerned* is thereby deleted.
- The regulation clarifies which types of pay and working conditions that must be applied, i.e. the conditions that follow from Directive 96/71/EC Article 3(1) first subparagraph (minimum rates of pay, working time and compensation for travel, board and lodging). This is in line with conditions that are usually covered by decisions on making collective agreements generally applicable in Norway.
- The contracting authorities have to make it clear in the call for tender and in the contract documents that these conditions are to be complied with.

By this amendment the government tries to meet part of the criticism by ESA. The amendments should make the required conditions more accessible for tenderers. However, when it comes to the differences between public and private contracts, the Norwegian government does not feel the need for revising the regulation. In the consultation paper regarding the amendments it says:

*Norway is opposed to the arguments by the ESA that in our opinion are based on a too narrow interpretation of EEA law. The result in Rüffert is not decisive as regards the judgment of the Norwegian provision. Firstly there are major differences between the Norwegian regulations and the German that was subject to hearing in Rüffert. Secondly, Rüffert only look at the relation to the posting directive. ECJ has in several rulings established that it is allowed to bring up social and environment considerations in public procurement. Thirdly Germany had not ratified ILO Convention No. 94, and the relation to this convention was therefore not considered. (Own translation) (Fornyings- og administrasjonsdepartementet 2007)*

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<sup>27</sup> Other arguments were also put forward by the Norwegian state, related to relationship between Directive 2004/18/EC and the PWD, where contracting authorities may lay down conditions concerning social considerations relating to the performance of a contract, and that the PWD was not meant to place any limits in this regard. However ESA referred to that public procurement principles are subject to the fundamental principles of the EEA Agreement, including the principle of freedom of establishment and to provide services.

The final warning issued by ESA in June 2011 was giving Norway a last chance to take corrective measures before ESA decides whether to bring the matter before the EFTA Court. ESA will now have to consider if these amendments are sufficient. Probably they will await the ongoing work in the EU regarding modernisation of public procurement. In the response to the ESA's reasoned opinion the Norwegian government says:

*In addition, the Government would like to refer to the European Parliament's resolution of 25 October 2011 on modernisation of public procurement (2011/2048(INI)), which calls for "an explicit statement in the [public procurement] directives that they do not prevent any country from complying with ILO Convention C94" and that the Parliament also "calls on the Commission to encourage all Member States to comply with that Convention".*

Regardless, the implementation of ILO 94 has been an important part of the government's action plan 1 to combat social dumping, and the Minister of labour, Mrs. Hanne Bjurstrøm, has announced that she will rather let the EFTA court have a saying rather than reverse existing policy solely based on the opinion of ESA.

The amendment has been accepted by LO, and is regarded as responding to the criticism made by ESA. The employer side, on the other hand, is not that impressed. The Head of the Labour Law department in The Confederation of Norwegian Enterprises (*Næringslivets Hovedorganisasjon*, NHO), Ms Nina Melsom, finds that the government has not been able to bring the regulation in accordance with EEA law. She points to the fact that the regulation does not solve the question of which collective agreement is applicable in cases where there are several agreements, as well as in cases where no collective agreements are established (Dagens Næringsliv, 28 November 2011).

## **Box 5.1: Administrative regulation on pay and working conditions in public contracts**

(Unauthorised translation by the author)

Adopted at 8 February 2008. Last amended 21 November 2011

### **Article 1 Objective**

The regulation shall contribute to make sure that employees in undertakings that provide services and construction work on behalf of public authorities do not have wages and working conditions that are less favorable to those stated in regulations that declare collective agreements generally applicable or a nationwide collective agreements.

### **Article 2 Definitions**

Definitions in regulation 7 April 2006 No. 402 on public procurement and regulation 7 April 2006 No. 403 on procurement in the supply sectors apply correspondingly.

### **Article 3 Entities covered by the regulation**

The regulation applies to governmental authorities, local and county administrations and public law entities.

### **Article 4 Contracts covered by the regulation**

The regulation is applicable to awarding of service or construction contracts exceeding NOK 1 million ex. VAT for governmental authorities and NOK 1,6 millions ex VAT for other entities.

The Ministry of Government Administration, Reform and Church Affairs may amend these threshold values.

### **Article 5 Contract requirements on pay and working conditions**

Contracting authorities shall impose as an obligation in their contracts a requirement that workers hired by contractors and potentially sub-contractors that contribute directly in fulfilling the contract, receive pay and working conditions in accordance to this article.

In areas covered by a regulation that declare collective agreements generally applicable contracting authorities shall require that pay and working conditions are in accordance with applicable regulations.

In areas not covered by a regulation that declare collective agreements generally applicable contracting authorities shall require that pay and working conditions are in accordance with applicable nationwide collective agreements for the industry. Pay and working condition are in this regard to be understood as provisions on minimum working time, pay, including over time payment, shift bonus and inconvenience payment, and covering of expenses to travel, board and lodging, so far as such provisions can be found in the collective agreement.

### **Article 6 Requirements regarding information**

Contracting authorities shall in the contract impose an obligation on the contractor and potentially sub-contractors on demand to document that requirements as regards pay and working conditions are fulfilled.

Contracting authorities shall in the contract secure the right to perform necessary sanctions if the contractor or potentially sub-contractors do not fulfill the requirements in article 5. Sanctions should be suitable for influencing the contractor or sub-contractor to fulfill the requirements.

Contracting authorities shall in the call for tender or the tender documents notify that the contract will include obligations regarding pay and working conditions, documentation and sanctions according to this regulation

### **Article 7 Control**

Contracting authorities shall undertake necessary control to see if the obligations regarding pay and working conditions are fulfilled. The level of control can be adjusted to the need in the concerned industry, geographic area and so on.

### **Article 8 Enter into force**

The regulation enters into force 1. March 2008.

Source: (in Norwegian): <http://www.lovdاتا.no/cgi-wift/ldles?doc=/sf/sf/sf-20080208-0112.html>

## **Enforcement**

Enforcement issues can both be related to whether public entities actually complies with the regulations, and how contract clauses should be enforce in order to ensure compliance by the main contractor and sub-contractors. However both these issues are mainly left to the public entities to handle.

Whether the public entities include this kind of clauses in their contract is not systematically controlled by anyone. Companies tendering for public contracts may submit a complaint about infringement of the public procurement law to the Norwegian Complaints Board (KOFA), but this will depend on the tenderer's knowledge of the legal framework. Furthermore, if the clause is included in the tender, but not enforced in the contractual relationship, competing tenderers will not be in a position to complain. Compliance therefore depends on how this is dealt with by the public entities in question. The Labour Inspectorate has no authority in this respect. The obligation on the employer to check that the clause is complied with can be undertaken by random samples. However, the scale of controls should be adjusted dependent on industry, geographical area and so on (Fornyings- og administrasjonsdepartementet 2008).

This issue was discussed when the regulation was prepared. The Ministry then concluded that although enforcement could be more efficient if it was placed in other hands than the employer's, the Labour Inspectorate Authority did not have the necessary experience in controlling wages. As pay has been fixed in collective agreements or individual employment contracts, the enforcement has also been left to social partners and/or individual employees. However, since the first decision on making collective agreements generally applicable (see above), the Labour Inspectorate Authority has, through enforcing these regulations, gained experience in this field that they did not have a few years ago. Thus, a white paper from the Ministry of Labour published in August 2011 suggests giving the Labour Inspectorate enforcement power in this area:

*Many things indicate that the enforcement and sanction instruments that the Labour Inspectorate Authority has today, are not sufficient. ... It is the opinion of the Ministry that the Labour Inspectorate should have the competence to supervise with regard to the administrative regulation on wage and working conditions in public contracts. Even within areas of generally applicable collective agreements, where the Authority can make contact with each employer, and further has the right to control if the main contractor has fulfilled its duty to give information and ensure compliance, it would be expedient to be able to turn to the public entities to control whether they have pursued their responsibility according to the regulation. (Own translation) (Meld. St. 29 (2010-2011))*

The Ministry point to the fact that the Labour Inspectorate Authority in the later years has gained much experience in this field, and will therefore send a suggestion to give the Labour Inspectorate enforcement authority in this area out for consultation. If this is decided the Labour Inspectorate would probably be entitled to use their ordinary enforcement instruments, including issuing orders, imposing coercive fines and halt the work of the main contractor until the order has been complied with by the public entities.

## **Pay clauses in practice: Does they work?**

The pay clause in public procurement is only one among several regulations that procurement entities have to pay attention to. Especially in minor entities, it can be challenging to comply with the legal framework. And as will be outlined below, existing evidence indicates shortcomings when it comes to compliance with the regulation – both among small and big public entities.

In a survey among public entities buying cleaning services, only 9 out of 20 had included a clause concerning wages and working conditions in the contract (Trygstad et al 2011).<sup>28</sup> Trygstad et al (2011) finds that only 4 out of 20 public entities buying cleaning services have monitored the compliance of the clause, and many of the undertakings find it difficult to undertake such controls. The Confederation of Norwegian Enterprises (*Næringslivets Hovedorganisasjon*, NHO) claims that the regulation is a symbolic provision that the public employers do not take seriously (NHO, undated).

This is partly confirmed by Berge and Sønsterudbråten (2011). A survey among shop stewards in the service sector documented that even though the public entities includes this clause in the tender documents, most often the service procurers do not control whether the clause is fulfilled. They are primarily focused on the price of the service, and they seldom monitors if the clause is actually lived up to. This is especially the case in cleaning and private security.

### **The Adecco Case – staffing companies and nursing homes**

However, during 2010-11 the mass media have focused on poor wages and working conditions among employees in private service companies, especially within the health care sector. These cases have led to an increased focus on public entities responsibility. The attention was first raised by disclosures concerning a health care subsidiary of the staffing company Adecco that was running five nursing homes in Norway on behalf of municipalities.

Adecco Health (*Adecco Helse*) admitted in February 2011 that they had breached the Working Environment Act (*arbeidsmiljøloven*) provisions on working time. The confession came after serious violations of the law was disclosed by the Norwegian Broadcasting System (NRK) in one of their nursing homes in Oslo. Employees had worked 84 hours a week without over time compensation and slept in bomb shelters. Internal investigations showed that the violations on working time provisions could also be found at other homes drifted by Adecco Health, and Oslo and other municipalities revoked the contract with Adecco Health. Consequently Adecco decided to close down their nursing home operations. In June Oslo municipality requested Adecco Health to repay NOK 23 millions for having used unskilled workers in positions where the contract stated that skilled workers were to be used. This adds to NOK 11 million already withheld by the local authority for the same reasons. This case clearly demonstrated that the monitoring by the city administration was lacking.

Violation of the Working Environment Act has also been disclosed in public nursing homes. The City of Trondheim did through own initiated controls disclose a large number of violations of the Working Environment Act both concerning own employees and temporary agency workers. As regards temp workers, they found employees that had worked 41 days in a row, up to 104 hours a week. Three out of four of the agencies that provided services to the city of Trondheim were in breach of one or more provisions concerning working time. However, this was revealed in the audit made by the city itself, and one of the private service contracts was as a consequence of this cancelled.

### **Construction work – blind faith in main contractors?**

An audit in the municipal enterprise *Undervisningsbygg Oslo KF* uncovered that existing systems were insufficient in ensuring that public procurement regulations were complied with. The process leading up to signing a contract should in theory prevent social dumping, but written procedures concerning control as well as actual follow-up had failings.

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<sup>28</sup> The survey does not give information on whether the contract was over the threshold values. See.

*Undervisningsbygg* owns municipal school buildings in Oslo and is an important employer within the construction industry. It is the biggest property steward in Oslo and conducts construction work for NOK 2 billion a year.

The audit showed that the basic documents and routines for competition and contract included information and clause concerning wage and working conditions. These were used in all procurement processes, except in three cases. These three procurements were related to the same building project. However, *Undervisningsbygg* had not established routines for control of wage and working conditions, as they were contractually obliged to do. Such routines did not come into place until two years after the audit started. The audit showed that procedures and practice mainly left to the main contractor to evaluate whether there was a need for controls of the sub-contractors, as well as undertake such controls. This is not in accordance with the administrative regulation on public procurements. Neither did they have procedures for follow-ups in case of breaches of the contractual obligation.<sup>29</sup>

## Monitoring cleaning contracts

Berge and Søndstubråten (2011) analysed a case that can be considered a fairly *good example* on how to set up a monitoring system. The case study was made in a municipality that had bought cleaning services from a private provider. The municipality had used four different ways of monitoring the service providers:

- 1) By fixed quarterly controls
- 2) Intern audits that also covered service providers
- 3) Sample controls
- 4) Controls based on hints from users, employees or others

The municipality focused both at monitoring the quality of the service provided as well as working conditions on those working at the premises. Through sample controls, audits, or controls upon hints they sought to make sure that employees of the contracted cleaning companies as well as sub-contractors, got wages and working conditions in accordance with nationwide collective agreements or equal. In the written control procedures the following was examples of what could be controlled:

- If the contractor's system to monitor that the conditions are complied with, is observed.
- If the employees have a written employment contract, and if the agreed wage is in accordance with the minimum wage, and if paid wages are in accordance with what is agreed on.
- Agreement on overtime payment and how this is practiced.
- What kind of resting facilities that is available for the employees.
- Lodging.

Several of the persons interviewed in this case said that it is demanding to keep the necessary control with some of these conditions, not at least as the industry is characterised by employees that want or make demands on working more than what is allowed by labour regulations at the same time as the employer does not have money to pay for overtime work. Several employees had therefore volunteered to work more hours without overtime payment. Even if the municipal cannot accept this, it is hard to disclose.

The municipal acknowledges that it is probably not able to catch all unacceptable conditions. However, in the opinion of the municipal representative sample controls disclose some, and

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<sup>29</sup> [http://www.nyheter.doffin.no/index.php?path=2&resource\\_id=3738](http://www.nyheter.doffin.no/index.php?path=2&resource_id=3738)

as the contractors are aware of these controls, this makes them pay more attention to the conditions in their own company.

However, this case is however not only a good example. Even though this municipality undertook several control measures, the study found cases where the regulations were in breach:

*Even though we do not have information on to what extent this takes place or how many cleaners that are working under criticisable conditions, it illustrates how difficult it is to keep control with the conditions within the cleaning industry.*

The municipality referred to in this case study is considering whether they should develop the monitoring system to include other instruments of control. Among other things they are discussing what kind of documentation that should be demanded in order to check whether the contractual conditions concerning pay and working conditions are complied with. Furthermore they discuss how the qualification phase of a tender could ensure that potential bidders have satisfactory systems to handle working agreements wage, overtime, rosters, ID-cards and uniforms so those who do not have sufficient systems do not get to participate in the tender. Finally they assess whether the contract conditions should be stricter, e.g. if the municipality should demand that the tendering companies engage their auditor to look through contracts, rosters and paychecks.

## **Outlook**

The Norwegian regulation on pay clauses can be said to face two major challenges. Firstly, the future of this regulation will in many aspects depend on how ESA will go forward with its case. That is if the claimed infringement of EEA law is to be laid before the EFTA court. And in this respect how this court will solve the conflict between an ILO convention and EEA law. One tricky aspect in this respect is that the ILO convention No. 94 only addresses central authorities while the Norwegian regulation has a much broader scope. No matter how the Court assesses the relation between the EEA Agreement and ILO conventions it might prove difficult to argue for this broad scope.

If the Norwegian state is forced to amend its regulation further, one possibility is to link conditions in public procurement to general applicable collective agreements. As the number of general applicable collective agreements are very limited this would either limit the scope of the regulation considerably, or necessitate that more collective agreements are being made universally applicable. So far this option has not been considered in the ongoing debates.

Independently of what is the outcome of the ESA case, there seem to be a need for strengthening the enforcement instruments of the regulation. Given the Labour Inspectorate Authority increased power and resources this seems already to be in the pipeline. In addition, other initiatives on strengthening the enforcement of pay clauses have been taken by the trade unions. If employees do not receive pay and working conditions in accordance to what is intended by the regulation, they have no formal way of enforcing this. This is because the Public Procurement Act only makes demand on the public entities, and does not give any rights to the employees. As regards generally applicable collective agreements, the system is constructed differently. This regulation places a right on the employee and he or she can therefore make a claim on the basis of this regulation. To strengthen the right of the employees, there has also been implemented a joint and several liability for conditions made generally applicable. This means that employees can direct their claims not only to their own employer, but to all companies that are above their employer in the contract chain, the buyer excluded. A more efficient enforcement of pay clauses in public procurement can be to implement such liability in contracts covered by the administrative regulation, and where the public entities as the buyer also can be made liable.

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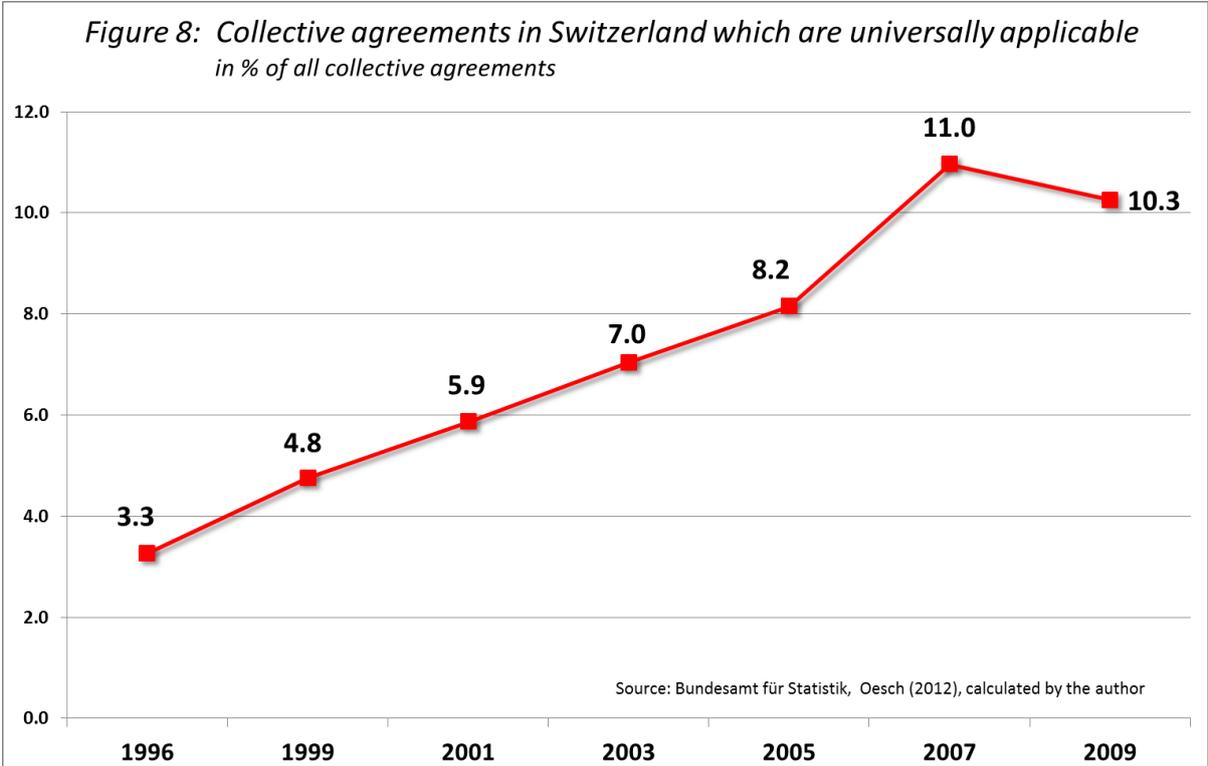
# 6. Switzerland

Thorsten Schulten

## Introduction

Social and labour issues have traditionally played an important role in public procurement in Switzerland. Procurement laws and ordinances at national and subnational level usually contain pay clauses, according to which contracting companies have to observe collective agreements or, if there are no such agreements, offer those wages and working conditions that are customary in the locality. As such, Switzerland belongs to the group of countries that “closely follows ILO Convention 94 on Labour Clauses in Public Contracts without having ever ratified it” (Baumann 2002).

The wage-setting system in Switzerland is rather diverse. Only about 50 per cent of all workers are covered by a collective agreement (Oesch 2011). In recent years, the number of collective agreements that have been declared generally binding has slightly increased. Nevertheless, they still represent only about 10 per cent of all collective agreements in Switzerland, so that the great majority of agreements are not universally applicable (Oesch 2012, Figure 2).



Against this background, pay clauses in public procurement play a major role in stabilising the Swiss collective bargaining system and in preventing downward wage competition in the tendering process. As public authorities in Switzerland spend around SFR 36 billion per year for goods and services, which corresponds to 25 per cent of overall public spending (Leduc 2010), the state can be seen to be actively using its market power to support collectively agreed wages and working conditions.

## Legal basis for Swiss public procurement

Up until the early 1990s, there was only limited regulation of public procurement in Switzerland, which created wide scope for public authorities to use public contracts for various political, economic and social purposes. The practice of procurement has been described as being rather discriminatory, as, in the absence of transparent tendering processes, contracting authorities, in particular at regional and local level, often privileged local companies (Felder and Podgorski 2009: 10). Some Swiss cantons even had protectionist procurement provisions that explicitly excluded foreign companies from public contracts.

The changes to Swiss procurement law were very much inspired by international procurement regulation, such as the 1994 WTO Government Procurement Agreement (GAP) and later the 1999 Bilateral Agreement on Procurement between Switzerland and the EU, which fostered a comprehensive liberalisation of Swiss procurement policy (Oesch 2010). In concluding these two agreements, Switzerland accepted the principles of transparent and non-discriminatory procurement procedures and – above a certain threshold – agreed to promote competition by opening the tenders to international bidders.

Procurement laws in Switzerland are determined both at national level and at the level of the 26 Swiss cantons (Stöckli and Beyeler 2012). At national level, the main legal principles are laid down in the 1994 Federal Act on Public Procurement (*Bundesgesetz über das öffentliche Beschaffungswesen, BöB*), which also introduced international procurement rules into Swiss law. Furthermore, the 1995 Ordinance on Public Procurement (*Verordnung über das öffentliche Beschaffungswesen, VöB*) further specifies the implementation of the federal procurement law. Both regulations are only valid for public authorities and companies at national level, representing only about 20 per cent of overall public procurement in Switzerland (Leduc 2010).

**Table 6.1: Legal framework of public procurement in Switzerland**

|                             |   |
|-----------------------------|---|
| <i>Supra-national level</i> | WTO Government Procurement Agreement (GAP) from 1994 (in force since 1996)  |
|                             | Bilateral agreement on procurement between Switzerland and the EU from 1999 (in force since 2002) ( <a href="http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:22002A0430(06):EN:HTML">http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:22002A0430(06):EN:HTML</a> ) |
| <i>National level</i>       | Federal Act on Public Procurement ( <i>Bundesgesetz über das öffentliche Beschaffungswesen, BöB</i> ) from 1994 ( <a href="http://www.admin.ch/ch/d/sr/1/172.056.1.de.pdf">http://www.admin.ch/ch/d/sr/1/172.056.1.de.pdf</a> )   |
|                             | Ordinance on Public Procurement ( <i>Verordnung über das öffentliche Beschaffungswesen, VöB</i> ) from 1995 ( <a href="http://www.admin.ch/ch/d/sr/1/172.056.11.de.pdf">http://www.admin.ch/ch/d/sr/1/172.056.11.de.pdf</a> )   |
| <i>Cantonal level</i>       | Intercantonal Agreement on Public Procurement ( <i>Interkantonale Vereinbarung über das öffentliche Beschaffungswesen, IVöB</i> ) from 1994 ( <a href="http://www.admin.ch/ch/d/as/2003/196.pdf">http://www.admin.ch/ch/d/as/2003/196.pdf</a> )   |
|                             | Regional procurement laws determined autonomously by the 26 individual cantons (see <i>Annex 1</i> )  |

Source: author's compilation

Given the strong political federalism that prevails in Switzerland, the bulk of public procurement is regulated by the regional procurement laws of the 26 individual Swiss cantons (see Annex 1). The latter are valid for both the cantons themselves and the municipalities within the respective cantons, which altogether represent 80 per cent of Swiss public procurement (Leduc 2010). Apart from cantonal-level procurement regulation, however, in an Intercantonal Agreement on Public Procurement (*Interkantonale Vereinbarung über das öffentliche Beschaffungswesen, IVöB*) concluded in 1994, all the cantons agreed on some common principles for procurement policy. The Intercantonal Agreement and its implementing regulations also had the task of transposing the provisions of the GAP and the bilateral agreement with the EU into regional procurement laws.

Both the Swiss federal procurement law as well as the Intercantonal Agreement refer to the “economically most advantageous offer” as the main criterion for awarding public contracts (BöB, Article 1, c.; IVöB, Article 13, f.). According to Article 21 of the federal procurement law, the “economically most advantageous offer” has to be calculated by considering a broad range of factors and “in particular, deadlines, quality, price, profitability, operating costs, customer service, expediency of the service, aesthetics, environmental sustainability and technical value.” The criterion of the lowest price is only accepted for the purchase of standardised goods. Apart from that, Swiss procurement law adopts a more comprehensive approach that takes into account several short- and long-term cost dimensions, including social costs.

### **Pay and other social clauses in Swiss public procurement**

Consideration of social aspects has a long tradition in Swiss public procurement. Before the liberalisation of procurement policies in the 1990s, public authorities were had extensive scope to use public contracts for social purposes. Moreover, in some Swiss cantons regional procurement laws had long contained provisions on working conditions of workers under public contracts. The regional procurement ordinance of the canton of Solothurn, dating from 1932, for example, determined that “all contracting companies are obliged to provide their workers prevailing working conditions, in particular, regarding pay and working time” (quoted from Felder and Podgorski 2009: 16).

From the mid-1990s, the liberalisation of Swiss public procurement became part of a larger policy package aimed at greater integration of the Swiss economy with the European Single Market (Mach et. al. 2003). The latter also included opening the Swiss labour market to EU citizens, which caused considerable concern regarding possible negative effects on wages and working conditions (Eldring and Schulten 2012). As the liberalisation of Swiss public procurement was also intended, in particular, to open tendering procedures to foreign companies, it also put the issue of pay clauses for workers on public contracts onto the policy agenda.

The 1994 Federal Act on Public Procurement (BöB) also introduced two core provisions dealing with labour issues. First, it determined more generally that the “*contracting authority will only award a contract for services in Switzerland to a tenderer who will guarantee compliance with health and safety regulations and the terms and conditions of employment of workers*” (BöB, Article 8, b.), underlining that “*the conditions applicable at the place of performance will be binding*” (ibid.). Secondly, the Federal Act on Public Procurement contains a special provision on gender equality according to which “*the contracting authority will only award a contract to a tenderer who guarantees the equal treatment of men and women providing services in Switzerland in respect of salary*” (BöB, Article 8, c.).

The more general provision on the commitment to require observation of locally prevailing working conditions was further specified by the 1995 Ordinance on Public Procurement (VöB). According to Article 7 of the VöB, public contracts should preferably refer to working conditions as laid down in locally applicable collective agreements. If there are no collective agreements, public contracts can also refer to so-called ‘standard work contracts’

(*Normalarbeitsverträge*), which are regulatory instruments that prescribe statutory minimum wages in some sectors. In practice, however, standard work contracts are not very widespread and exist only in a very few cantons and sectors (SGB 2011).

Where there are neither collective agreements nor standard work contracts, the public authorities are required to identify those working conditions that are customarily offered by local employers for relevant occupations, and these then serve as criteria that have to be met in order to be awarded a public contract. Moreover, for goods and services that have been produced or supplied from abroad, an amendment to the VöB, dating from 2009, indicated that public authorities are obliged to choose only from those bidders that can guarantee that the purchased goods have been produced in observance with ILO core labour standards (VöB, Article 7, 2, see also Steiner 2010).

For public procurement at regional and local level, the Intercantonal Agreement on Public Procurement (IVöB) also contains provisions that require that the award of public contracts should respect prevailing working conditions and the equal treatment of men and women in the contracting companies (IVöB, Article 11, e and f.). Furthermore, all regional procurement laws or ordinances of the 26 Swiss cantons include more or less the same pay or labour clauses that oblige contracting companies to consider health and safety standards, to guarantee equal treatment between men and women, and to provide certain working conditions (Felder and Podgorski 2009: 39ff., see also Annex). Finally, some cantons also consider the provision of apprenticeship places as additional award criteria (Steiner 2010).

Regarding wages and working conditions, most cantonal procurement laws determine that companies under public contract have, first of all, to comply with collective agreements. The procurement law of the canton of Basel-Stadt even states that “usually public contracts may be awarded only to employers which are *covered* by a collective agreement” (Article 5, Annex 1, authors’ emphasis). In contrast to that, cantonal procurements laws usually require not that companies under public contracts be directly and legally covered by a collective agreement but only that they observe its basic provisions.

While some cantons demand the observance of locally applicable collective agreements, others require only the observance of any valid collective agreement in Switzerland. This allows Swiss companies with their principal office in one canton, but which deliver public contracts in another, to apply collective agreements from their place of origin. As there are sometimes rather significant regional differences in collectively agreed pay, this might lead to an important competitive advantage. The fact that the ‘place of origin’ principle can put pressure on firms with ‘more expensive’ collective agreements has led to its being strongly criticised by Swiss trade unions, which have called for only those collective agreements applicable at the place of performance to be considered acceptable (SGB 2008, Blank 2010).

If there are no collective agreements, the public contract can also refer to the statutory minimum wages as defined in standards work contracts, although these exist in only a very few sectors and cantons. For the case that there is neither a collectively agreed nor a statutory regulation of working conditions the most regional procurement laws determine that workers under public contracts have to receive locally and professionally prevailing wages.

### **Enforcement and control of pay clauses in procurement**

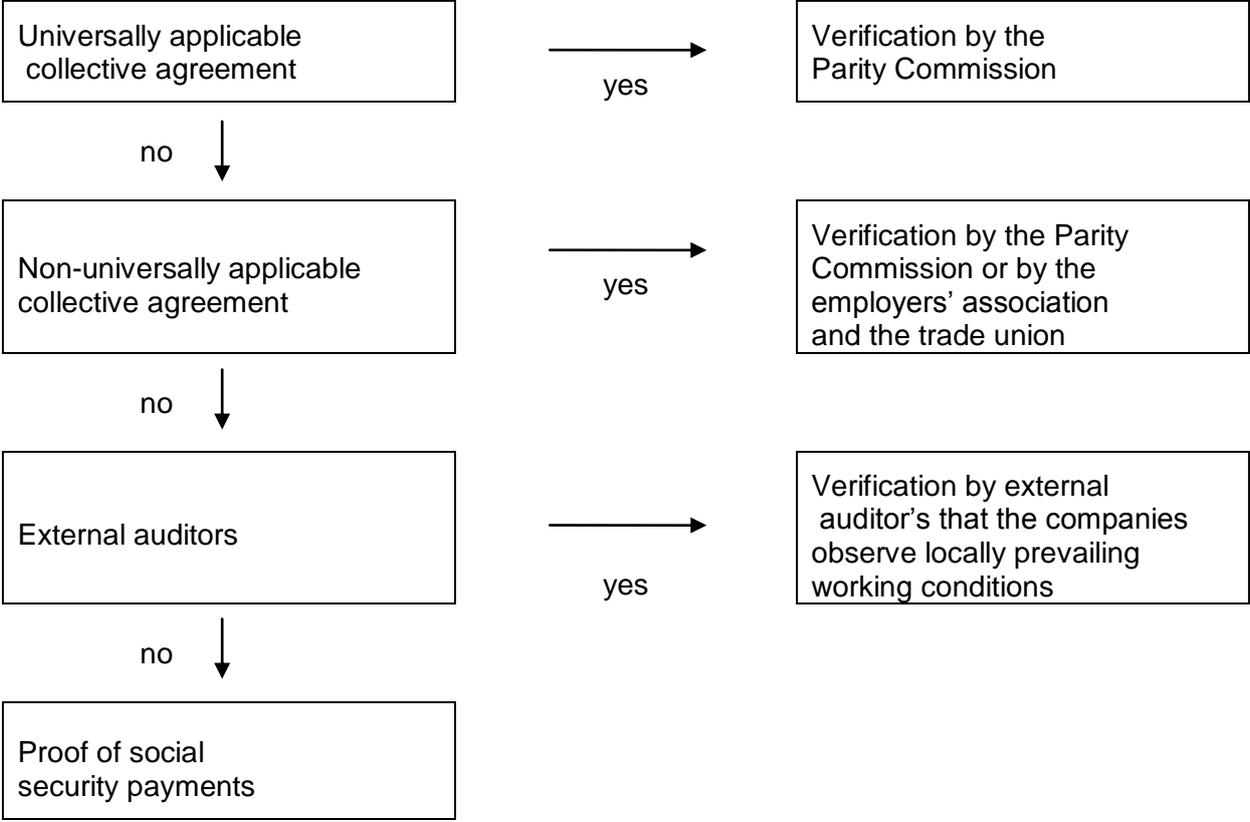
According to Swiss procurement laws at national and cantonal level, the contracting authorities have the right to ask tendering companies to provide evidence that they observe applicable working conditions and equal treatment of men and women. In most cases such proof can simply be constituted by self-declaration on the part of the companies. Regarding the observance of collective agreements, contracting authorities can ask for verification from the so-called parity commissions (composed of employer and trade union representatives) that have signed the agreement. Moreover, as a kind of pre-qualification system, some cantons (such as, Thurgau or Valais) publish a list of companies for which it has been confirmed that they fulfil the requirements of the regional procurement law (including

observance of working conditions). Should a company carrying out a public contract commit a breach by not applying any specified working conditions, it has to pay a fine and can be excluded from further tendering processes.

The system and scope of control in procurement depend very much on the ordinances at regional and local level, and show significant variations. One of the most advanced control systems exists in the city of Berne,<sup>30</sup> which exemplifies the strong involvement of both employers and trade unions in local procurement policy. Berne has established a local public procurement commission in which delegates from local business and trade unions are equally represented. The commission meets once a month, discusses all new draft public contracts, and gives recommendation to the contracting authorities. The commission also considers and reviews the application of any sanctions that may be imposed on companies for contravening the procurement laws.

In addition to that, the city of Berne has also established a comprehensive verification system, according to which tendering companies have to prove that they comply with the required employment conditions (Figure 9). In principle, there are four possibilities. First, where the public tender is issued in a sector where there is a collective agreement that is universally applicable, the tendering company has to submit a certificate obtained from the parity commission (composed equally of employer and trade union representatives) that signed the agreement.

Figure 9: Verification of the observance of working conditions in tendering companies in the city of Berne



Source: City of Berne ([http://www.bern.ch/leben\\_in\\_bern/arbeit/ausschreibungen/angebotende/nachweise/bestatigung\\_einhaltung\\_arbeitsbedingungen.pdf](http://www.bern.ch/leben_in_bern/arbeit/ausschreibungen/angebotende/nachweise/bestatigung_einhaltung_arbeitsbedingungen.pdf))

<sup>30</sup> See for the following: [http://www.bern.ch/leben\\_in\\_bern/arbeit/ausschreibungen/beschaffungswesen](http://www.bern.ch/leben_in_bern/arbeit/ausschreibungen/beschaffungswesen)

Secondly, if there are collective agreements in the branch in question, but these have not been declared generally binding, the tendering company can obtain verification either from the parity commission, or, where there is no such commission, directly from the responsible trade unions and employer association. Furthermore, where a tender is issued in a sector where there is no collective agreement at all, the tendering company has again two options for confirming its observance of locally prevailing working conditions: either this can be certificated by an external auditor or the company can publish its social security payments

If the tender concerns a sector that is not covered by collective agreements at all, one of the most difficult tasks is to determine the “locally” and “occupationally” prevailing working conditions which, in that case, should be the reference point for employees working on public contracts. One major source for identifying prevailing wages is the Swiss Earnings Structure Survey, which is carried out by the Swiss Federal Statistical Office every two years and contains the most detailed data on wages by region and occupation in Switzerland.<sup>31</sup> On the basis of this survey, the Swiss Confederation of Trade Unions (*Schweizerischer Gewerkschaftsbund*, SGB) runs an online wage indicator portal (<http://www.lohnrechner.ch>) which provides comprehensive data on prevailing wages for seven major regions and about 50 sectors in Switzerland. Similar internet tools are also offered by some of the Swiss cantons.

There are almost no studies on the actual control and enforcement of pay clauses in public procurement in Switzerland. One exception is a recent study on behalf of the Federal Office for Gender Equality, which analysed controls in companies under public contracts on the issue of equal pay for men and women (Trageser et. al. 2011). The study, based on the evaluation of 14 in-depth company cases, concluded that in 10 cases the companies had a significant pay gap that could not be justified by different objective characteristics of the workforce (qualification, age etc.) but was based on pay discrimination against female workers.

There are also regular reports by the State Secretariat for Economic Affairs (SECO) about controls regarding the observance of collective agreements, although these have no particular reference to public procurement. The growing importance of company controls and monitoring is part of the so-called ‘flanking measures’ that have been introduced in Switzerland in parallel with the adoption of the principle of free movement for workers who are EU citizens. This also includes greater involvement of trade unions and employers’ association through the establishment of bi- or tripartite commissions at sectoral and cantonal level (Eldring and Schulten 2012). In 2011, nearly 35,000 establishments have been controlled of which about 29 per cent have shown some incidence of non-compliance with collective agreements (Staatssekretariat für Wirtschaft SECO 2012). Given this rather high proportion of offences, the Swiss Confederation of Trade Unions has recently called for more and stronger controls in order to increase compliance with collective agreements (Rechsteiner 2012).

## Outlook

Pay clauses are a well-established element in Swiss public procurement. Against the background of the particularities of the Swiss collective bargaining system, in which only a small minority of all collective agreements are generally binding, pay clauses usually refer to locally prevailing agreements that are not universally applicable. The Swiss system of pay clauses in procurement is, therefore, rather similar to the German system, as it was established in the 2000s before the Ruffert judgment of the European Court of Justice (ECJ).

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<sup>31</sup> See at the webpage of the Swiss Statistical Office:  
<http://www.bfs.admin.ch/bfs/portal/en/index/themen/03/04/blank/data/00.html>

In contrast to Germany, Switzerland has been able to continue with that system, because as a non-EU member, and also a non-member of the European Economic Area, it is not directly affected by EJC judgements (Epiney and Mosters 2009).

However, with the adoption of the bilateral agreements with the EU, Switzerland has aimed at adapting its procurement regime to EU standards. Moreover, Switzerland has also taken over the basic economic freedoms of the Single European Market. Therefore, the ECJ's Rüffert judgement has prompted calls to change the provisions on pay clauses in Swiss public procurement law (Baumann 2008). In 2008, the Swiss government produced a draft for a fundamental revision of the Federal Act on Public Procurement, according to which – in line with the Rüffert judgement – pay clauses would be limited to the application of generally binding collective agreements. After strong resistance from the Swiss trade unions and the more leftist political parties, however, the Swiss government held back from that proposal and has continued with the established system (Hartwich 2011).

Nevertheless, some legal uncertainties regarding the conformity of the current regulation on pay clauses with the bilateral agreements with the EU remain. This is all the more so, as there is also an inconsistency between Swiss procurement law and the Swiss Posted Workers Act, as the latter only refers to collective agreements that are universally applicable. Therefore, it is rather likely that political pressure to change the current Swiss procurement regime will continue.

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## Annex: Pay clauses in regional procurement laws of Swiss cantons

|                        |   |
|------------------------|---|
| Aargau                 | <p><b>Ordinance on procurement from 1996:</b></p> <p><i>“Contracting authorities award public contracts (...) only to companies, which</i></p> <ul style="list-style-type: none"> <li>• <i>provide locally applicable health and safety standards and prevailing working conditions</i></li> <li>• <i>guarantee equal treatment of men and women, in particular regarding equal pay” (Article 3)</i></li> </ul> <p><a href="https://gesetzsammlungen.ag.ch/frontend/versions/1284">https://gesetzsammlungen.ag.ch/frontend/versions/1284</a></p>  |
| Appenzell Innerrhoden  | <p><b>Ordinance on procurement from 2001:</b></p> <p><i>„Contracting authorities may award public contracts only to companies which observe applicable health and safety standards and working conditions as laid down in collective agreements or standards work contracts.</i></p> <p><i>If the latter do not exist public contracts should refer to those employment conditions that apply to the occupations in question.”</i></p> <p>The main contracting company must ensure through the conclusion of a contract that subcontracting companies observe applicable working conditions. (Article 10).</p> <p><a href="http://www.ai.ch/dl.php/de/45dab7a0baa1f/726.010.pdf">http://www.ai.ch/dl.php/de/45dab7a0baa1f/726.010.pdf</a></p>   |
| Appenzell Ausserrhoden | <p><b>Law on procurement from 2000:</b></p> <p><i>“Contracting authorities may award public contracts only to companies that respect health and safety standards and observe working conditions as laid down in collective agreements or , in the absence of such agreements, those conditions that customarily apply locally and occupationally” (Article 3).</i></p> <p><a href="http://www.ar.ch/fileadmin/user_upload/Departement_Bau_Umwelt/Depsekreteriat/Gesetz_Beschaffung.pdf">http://www.ar.ch/fileadmin/user_upload/Departement Bau Umwelt/Depsekreteriat/Gesetz Beschaffung.pdf</a></p>   |
| Basel-Land             | <p><b>Ordinance on procurement from 2000:</b></p> <p><i>“1. Bidding companies that are covered by collective agreements have to include in the tender documents a written acknowledgement from the so-called Parity Commissions (composed of employer associations and trade unions) which must confirm observance with the collective agreement, in particular as regards working time, wages, bonuses and social insurance contributions.”</i></p> <p><i>2. Bidding companies which are not covered by a collective agreement have to obtain confirmation that collective agreements are observed through written acknowledgement from one of the following institutions:</i></p> <ul style="list-style-type: none"> <li>• <i>Parity commission</i></li> <li>• <i>Procurement administration of the canton</i></li> <li>• <i>An auditor or fiduciary services agency that is independent of the supplier (...) (Article 1)”</i></li> </ul> <p><i>“Bidding companies have to declare that they provide equal treatment for men and women” (Article 2)</i></p> <p><a href="http://www.baselland.ch/fileadmin/baselland/files/docs/recht/sgs_4/420.11.pdf">http://www.baselland.ch/fileadmin/baselland/files/docs/recht/sgs_4/420.11.pdf</a></p> |
| Basel-Stadt            | <p><b>Law on procurement from 1999:</b></p> <p><i>“Usually public contracts may be awarded only to employers covered by a collective agreement.”</i></p> <p>Tendering companies have to guarantee for goods and services produced in Switzerland</p> <ul style="list-style-type: none"> <li>• their observance of collective agreements in full and over time,</li> <li>• their observance of the principle of equal treatment of men and women.</li> </ul>   |

|            |   |
|------------|---|
|            | <p>For Swiss companies the relevant collective agreement is that which is applicable at the location of the registered head office of the company.</p> <p><i>“Foreign provider companies in Basel-Stadt must observe collective agreements in full or in the absence of such agreements, those conditions that apply locally and occupationally”</i> (Article 5).</p> <p><a href="http://www.gesetzessammlung.bs.ch/frontend/versions/1084">http://www.gesetzessammlung.bs.ch/frontend/versions/1084</a></p>  |
| Berne      | <p><b>Ordinance on procurement from 2002:</b></p> <p>Companies shall be excluded from the tendering procedure, <i>“if they do not provide working conditions as laid down by law or collective agreements of the respective sector, and in particular wages, equal pay for men and women and social insurance contributions.”</i> (Article 24, f.).</p> <p><a href="http://www.sta.be.ch/belex/d/7/731_21.html">http://www.sta.be.ch/belex/d/7/731_21.html</a></p>  |
| Fribourg   | <p><b>Ordinance on procurement from 1998:</b></p> <p><i>“Contracting authorities have to ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>oblige sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to be of equal force.”</i> (Article 6a)</p> <p><a href="http://bdlf.fr.ch/frontend/versions/1130/download_pdf_file">bdlf.fr.ch/frontend/versions/1130/download_pdf_file</a></p> |
| Geneva     | <p><b>Ordinance on procurement from 2007:</b></p> <p>Contracting companies and their subcontractor have to ensure that their workers are employed under the locally prevailing working conditions (Article 20)</p> <p><i>“With the application documents the companies must confirm and declare</i></p> <ul style="list-style-type: none"> <li>• <i>that they are covered by a collective agreement valid in Geneva (...)</i></li> <li>• <i>that they provide equal conditions for men and women”</i> (Article 32)</li> </ul> <p><a href="http://www.ge.ch/legislation/rsgf/rsg_l6_05p01.html">http://www.ge.ch/legislation/rsgf/rsg_l6_05p01.html</a></p>  |
| Glarus     | <p><b>Law on procurement from 1997:</b></p> <p>Companies might be excluded from the tendering procedure, or have a contract revoked, if they fail to respect health and safety standards, do not ensure equal treatment of men and women, and do not comply with working conditions as laid down in collective agreements or standard work contracts. In the absence of the latter, public contracts should refer to locally prevailing conditions. (Article 12)</p> <p><a href="http://gs.gl.ch/pdf/ii/g_s_ii_g_2_1.pdf">http://gs.gl.ch/pdf/ii/g_s_ii_g_2_1.pdf</a></p>   |
| Graubünden | <p><b>Law on procurement from 2004:</b></p> <p>Bidding companies have to make an explicit declaration that they</p> <p><i>“observe applicable health and safety standards and working conditions oblige subcontractors to observe applicable health and safety standards and working conditions”</i> (Article 10)</p> <p><i>„Working conditions refer to collective agreements or standard work contracts, or in the absence of these, to those conditions typically applicable locally and occupationally</i> (Article 11, 2)</p> <p><a href="http://www.gr-lex.gr.ch/frontend/versions/1226">http://www.gr-lex.gr.ch/frontend/versions/1226</a></p>   |

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| Jura         | <p><b>Ordinance on procurement from 2006:</b></p> <p>Public contracts should refer to working conditions as laid down in collective agreements or, in the absence of these, to locally prevailing working conditions. All regulations in Switzerland are deemed to have equal force (Article 28 and 51).</p> <p><a href="http://rsju.jura.ch/extranet/groups/public/documents/rsju_journal_off/journal_off_2006_19.pdf">http://rsju.jura.ch/extranet/groups/public/documents/rsju_journal_off/journal_off_2006_19.pdf</a></p>   |
| Lucerne      | <p><b>Ordinance on procurement from 1998:</b></p> <p><i>“Public contracts are awarded only to companies which guarantee (...)</i></p> <ul style="list-style-type: none"> <li>• <i>that they comply with applicable Swiss health and safety standards and working conditions, in particular the conditions determined by collective agreement,</i></li> <li>• <i>that they provide for equal treatment of men and women.”</i> (Article 4, b. and c.)</li> </ul> <p><a href="http://srl.lu.ch/frontend/versions/454?locale=de">http://srl.lu.ch/frontend/versions/454?locale=de</a></p>   |
| Neuchâtel    | <p><b>Law on procurement from 1999:</b></p> <p>Public contracts must respect locally prevailing working conditions. All regulations on working conditions in Switzerland are deemed to have equal force (Article 7)</p> <p><a href="http://www.lexfind.ch/dta/9376/3/60172.pdf">http://www.lexfind.ch/dta/9376/3/60172.pdf</a></p>  |
| Nidwalden    | <p><b>Ordinance on procurement from 2004:</b></p> <p><i>„Contracting authorities have to ensure contractually that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>obliges sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force.”</i> (Article 7)</p> <p><a href="http://www.nw.ch/de/online/main/dienstleistungen/?dienst_id=2701">http://www.nw.ch/de/online/main/dienstleistungen/?dienst_id=2701</a></p> |
| Obwalden     | <p><b>Ordinance on procurement from 2004:</b></p> <p><i>„Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>obliges sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force”</i> (Article 7)</p> <p><a href="http://ilz.ow.ch/gessamml/pdf/975611.pdf">http://ilz.ow.ch/gessamml/pdf/975611.pdf</a></p>   |
| Schaffhausen | <p><b>Ordinance on procurement from 2004:</b></p> <p><i>„Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>obliges sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or</i></p>  |

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|            | <p><i>standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force</i>" (Article 7)</p> <p><a href="http://www.sh.ch/fileadmin/Redaktoren/Dokumente/Hochbauamt/BeilageVergaberichtlinien.pdf">http://www.sh.ch/fileadmin/Redaktoren/Dokumente/Hochbauamt/BeilageVergaberichtlinien.pdf</a></p>  |
| Schwyz     | <p><b>Ordinance on procurement from 2004:</b></p> <p><i>"Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>obliges sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force</i>" (Article 7).</p> <p><a href="http://www.sz.ch/documents/430.130.pdf">http://www.sz.ch/documents/430.130.pdf</a></p>  |
| Solothurn  | <p><b>Law on procurement from 1996:</b></p> <p><i>"Contracting authorities shall award public contracts only to companies which</i></p> <ol style="list-style-type: none"> <li>a. <i>observe applicable health and safety standards and working conditions (especially regarding wages, working time, social insurance contributions ...)</i></li> <li>b. <i>observe the principle of equal treatment of men and working conditions especially regarding equal pay</i>" (Article 9).</li> </ol> <p><a href="http://bgs.so.ch/frontend/versions/592">http://bgs.so.ch/frontend/versions/592</a></p> <p><b>Ordinance on procurement from 1996:</b></p> <p>The working conditions considered in public contracts are those <i>"determined by collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally</i> (Article 3)</p> <p><a href="http://bgs.so.ch/frontend/versions/593">http://bgs.so.ch/frontend/versions/593</a></p>   |
| St. Gallen | <p><b>Ordinance on procurement from 1998:</b></p> <ol style="list-style-type: none"> <li>1. <i>"Contracting authorities shall award public contracts only to companies, which respect statutory health and safety standards and prevailing working conditions as laid down by collective agreements or standard work contracts</i></li> <li>2. <i>If there are no collective agreements or standard work contracts, the conditions applicable to the occupations in question by custom and practice shall apply;</i></li> <li>3. <i>If the contract is to be performed abroad, the company must confirm that ILO core labour standards have been observed."</i> (Article 10)</li> </ol> <p><i>"The main contractor has to secure that subcontractors are obliged to observe</i></p> <ol style="list-style-type: none"> <li>a. <i>health and safety standards and working conditions</i></li> <li>b. <i>equal treatment of men and women</i>" (Article 11)</li> </ol> <p><a href="http://www.gallex.ch/gallex/8/fs841.11.html">http://www.gallex.ch/gallex/8/fs841.11.html</a></p> |
| Thurgau    | <p><b>Ordinance on procurement from 2004:</b></p> <p><i>"Public contracts ... shall be awarded only to companies which observe applicable health and safety standards and working conditions as laid down in collective agreements or standard work contracts or in the absence of these, those conditions that typically prevail locally and occupationally"</i> (Article 36).</p> <p><a href="http://www.rechtsbuch.tg.ch/pdf/700/720_21e2.pdf">http://www.rechtsbuch.tg.ch/pdf/700/720_21e2.pdf</a></p>  |

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| Ticino | <p><b>Ordinance on procurement from 2001:</b></p> <p><i>“Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>oblige sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force” (Article 6).</i></p> <p><a href="http://www3.ti.ch/CAN/ri/program/books/rst/htm/07_37.htm">http://www3.ti.ch/CAN/ri/program/books/rst/htm/07_37.htm</a></p> |
| Uri    | <p><b>Ordinance on procurement from 2004:</b></p> <p><i>“Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>oblige sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force.” (Article 8).</i></p> <p><a href="http://www.lexfind.ch/dtah/61710/2/3-3112.pdf">http://www.lexfind.ch/dtah/61710/2/3-3112.pdf</a></p>                      |
| Valais | <p><b>Ordinance on procurement from 2004:</b></p> <p>The tender documents must establish that companies under public contracts have to observe health and safety standards and working conditions as laid down in collective agreements or standard work contracts. In the absence of these , locally prevailing conditions have to be observed. (Article 2, 2)</p> <p><a href="http://www.vs.ch/public/public_lois/de/LoisHtml/frame.asp?link=726.100.htm">http://www.vs.ch/public/public_lois/de/LoisHtml/frame.asp?link=726.100.htm</a></p>  |
| Vaud   | <p><b>Ordinance on procurement from 2004:</b></p> <p>Companies under public contracts have to observe applicable health and safety standards and working conditions as well as equal treatment of men and women. Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or, in the absence of these, <i>those conditions that typically prevail locally and occupationally</i> (Article 6)</p> <p><a href="http://www.vd.ch/themes/economie/marches-publics/cadre-legal/">http://www.vd.ch/themes/economie/marches-publics/cadre-legal/</a></p>  |
| Zug    | <p><b>Ordinance on procurement from 2005:</b></p> <p><i>“Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"> <li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> <li>▪ <i>oblige sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li> </ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force” (Article 7)</i></p> <p><a href="http://bgs.zg.ch/frontend/versions/788/pdf_file">http://bgs.zg.ch/frontend/versions/788/pdf_file</a></p>                    |

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| Zurich | <p><b>Ordinance on procurement from 2003:</b></p> <p><i>“Contracting authorities must contractually ensure that the supplier</i></p> <ul style="list-style-type: none"><li>▪ <i>observes applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li><li>▪ <i>obliges sub-contractors to observe applicable health and safety standards and working conditions as well as equal treatment of men and women</i></li></ul> <p><i>Working conditions are defined as conditions laid down in collective agreements or standard work contracts, or in the absence of these, those conditions that typically prevail locally and occupationally. All regulations in Switzerland are deemed to have equal force” (Article 8).</i></p> <p><a href="http://www.zh.ch/internet/de/rechtliche_grundlagen/gesetze/erlass.html?Open&amp;Ordnr=720.11">http://www.zh.ch/internet/de/rechtliche_grundlagen/gesetze/erlass.html?Open&amp;Ordnr=720.11</a></p> |
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Source: Authors' composition and translation

## 7. United Kingdom

*Pete Burgess*

### **Introduction: Pay clauses in UK procurement**

The UK has a history of regulating employment conditions in public procurement that extends back to the final decade of the nineteenth century. In 1893 the 'Fair Wages Resolution', which provided for minimum wage standards for public contracts, was adopted by Parliament (Bercusson 1978). The resolution took the form of an opinion issued by the House of Commons, rather than statute law, after hearings into the 'sweating system', the super-exploitation of workers mostly engaged in sub-contracting. This was the culmination of campaigns conducted from the mid-nineteenth century, but was added to following concerns about the deterioration in wages during the 'long depression' (1870-1890). One concern was that contractors were so eager to become suppliers to the government that competition for contracts was especially intense. 'The consequence is that there is extreme competition, tenders are cut down to the lowest possible point; and, under present conditions, the profit is made very much at the expense of the labourer' (Buxton cited by Denman 1947: 163). The aim of the provision was to 'secure the payment of such wages as are generally accepted as current in each trade for competent workmen'. In some cases the benchmark was the relevant collectively-agreed rate, in others it was the local rate under custom-and-practice. Where no comparator could be found, a rate might be inserted – although the government generally sought to stand aside from prescribing wage rates. The Fair Wages Resolution was complemented by the system of 'Wage Boards', introduced in 1909 and expanded over the next few decades, and renamed Wages Councils. These specified not just minimum wages in weakly-organised industries but also pay grades.

The resolution was amended several times and also influenced the wording of ILO Convention (No. 94) on labour clauses in public contracts, which, based on a comparable principle, also required wages, working hours and working conditions in public contracts to be no less favourable than prevailing legal, agreed or customary provisions. The UK ratified the Convention in 1950. The Fair Wages Resolution had a considerable influence on the wages of many employees in that it symbolised the aspiration for government to be a 'good' employer and contractor. Contractors had to declare that they complied with the resolution, and compliance was a contractual condition. Support for the institution of collective bargaining by government also had a wider political impact. Both aspects fell victim to the deregulatory approach of the Conservative Government (1979-1997), starting with the denunciation of Convention No. 94 in 1983 and the abolition of the Fair Wages Resolution in the same year. These represented some of the earliest instances of market-centred neo-liberal deregulation pursued by the Thatcher administration (Robertson 1986: 278f). Wages Councils were largely abolished in 1993, with the last remaining example, for agriculture, removed in 2011 (Burgess 2006: 27ff.).

The use of provisions on pay and other social matters in public procurement in the UK is currently constrained by EU and UK law, due both to the limits imposed by the legal framework and the lack of clarity of these stipulations. In addition, some notable features of the UK system of labour market regulation militate against using collectively-agreed industry-level arrangements as a regulatory mechanism: for example, collective agreements are not legally-binding on the signatory parties, single employer bargaining is the dominant form of collective bargaining, and there is no form of statutory extension of collective agreements.

Official guidance on social provisions issued in 2006 sought to make use of the options in the EU framework, especially on non pay-related issues. In addition, a number of public

authorities have introduced Living Wage policies for suppliers (see below and Appendix: Living Wage incidence). Discussion around the issue of a Living Wage has acquired a high profile in recent years, driven forward by campaigning based on the gap between the statutory National Minimum Wage and assessed needs. November 2012 saw the holding of a 'Living Wage' week, centred on the raising of the rate at which the Living Wage is calculated (see below), and the opposition Labour Party has committed itself to develop a Living Wage policy in the coming years.<sup>32</sup>

The Ruffert judgment had little direct impact in the UK as no public body in Britain had sought to rely on a similar constellation of collective provisions to prescribe minimum wage levels in public contracts. As outlined further below, the UK government's policy of transposing the Posted Workers Directive in a way that excluded the option of considering industry-level agreements in construction has also meant that UK public authorities may only insist on compliance with *statutory* minimum wage levels for employees working in Britain. Moreover, outside of the construction sector there are virtually no industry-level collective agreements in the UK, representing a further barrier to the use of *erga omnes* mechanisms. UK trade unions saw the Ruffert judgment as reinforcing the ECJ's narrow interpretation of the Directive, in which statutory protection were seen as a 'ceiling rather than a minimum', in which no consideration was given to the Procurement Directives, and in which the court 'did not consider the issue of the increasing use of public procurement as a means for achieving social benefits'.<sup>33</sup> By stating that the restrictions imposed by the contracting authority in the Ruffert case were not justified, the case emphasised the caution in the UK over imposing Living Wage requirements: as yet, local authorities that have developed Living Wage policies in respect of their contractors have done this on a voluntary basis, albeit with slightly differing emphases and interpretations of EU procurement law.<sup>34</sup>

The UK government's response to the Commission Green Paper on Modernising Public Procurement has focused on advocating simpler procurement processes, with easier access to public procurement for employee-led organisations, SMEs and mutuals.<sup>35</sup> The government also asked the Commission for 'clarification and clearer guidance on how social and environmental issues can be taken into account, and how they can help to achieve value for money' (Cabinet Office 2011) and argued for a substantial rise in, and indexation of, the value threshold for goods and services procurement.

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<sup>32</sup> The next parliamentary elections in the UK are scheduled for June 2015.

<sup>33</sup> GMB European Briefing, April 2008 (<http://www.gmb.org.uk/pdf/Ruffert%20Case%20-%20April%2008.pdf>)

<sup>34</sup> Keith Ewing noted, in commenting on the Ruffert judgment, that: "The contested collectively agreed terms in Laval and Ruffert were challenged by the companies (or those acting in their stead) in circumstances where an attempt was made to impose them on foreign contractors (from Latvia and Poland respectively). It does not follow – and it is highly improbable - that a domestic contractor could bring a similar challenge under the PWD in such circumstances" (Fair Pay Network 2009: 18).

<sup>35</sup> This is in line with UK government policy on SMEs, under which the government aspires to move to 25 per cent of procurement being placed with SMEs with more management of state provision to be transferred to mutual undertakings. The UK government has asked that such organisations be given a three-year period before being subject to competition. As noted below on the abolition of Codes of Practice on public sector contracting, the promotion of SMEs can clash with the principles of requiring good employment practices in public procurement.

## Wage setting in the UK

The setting of mandatory minimum wages in the UK is achieved through a national hourly minimum wage (NMW). This applies to virtually all employment relationships. Any clause in an employment contract that provides for a rate below that specified as applying to the employee is void, and employees may claim the difference between this and the NMW.

There are different rates, applicable by age. As from 1 October 2012:

- the adult minimum wage for workers over 21 is £6.19.
- the 'development rate', which covers workers aged between 18 and 21, is £4.98.
- the rate for 16-17 year-olds is £3.68.
- for apprentices aged under 19 or 19 or over and in the first year of apprenticeship: £2.65.

As discussed below, the NMW raises a number of areas of difficulty: the level is insufficient on its own to secure an adequate standard of living, and needs to be supplemented by in-work benefits, such as tax credits;<sup>36</sup> enforceability remains a problem, despite recent efforts to improve the inspection and sanctions regime; the NMW does not reflect the wide variation in living costs between high-cost London and other regions. In the field of public procurement this has triggered campaigns to establish a Living Wage, dealt with in greater detail below.

There is no other form of legally-enforceable pay minimum in the UK. Collective agreements are not legally-binding, unless expressly stated to be so by the parties (virtually never), and there is no extension of collective agreements to non-signatory parties.

Sectoral collective agreements outside the public sector are rare, although there is an agreement for the Engineering Construction Industry (concluded between UNITE and GMB and the Engineering Construction Industry Association, ECIA, and other employer bodies) that has significance for public sector procurement. The agreement was renewed in November 2009, in the wake of a series of disputes about the recruitment of non-UK employees in refinery construction, and included an Appendix ('Appendix G') that covers employment and industrial relations issues where contractors propose to employ labour or use sub-contractors from outside the UK. This notes that all 'in-scope' labour employed on such projects (that is, by member companies) is directly subject to the terms of the agreement (pay, holidays expenses etc.).<sup>37</sup> The ECIA has committed itself to ensure compliance with this aspect. In addition, the agreement sets out measures that employers should take to ensure that vacancies are advertised locally through appropriate public agencies (Job Centres). This agreement, as well as elements not expressly included in it, were enforced on some employers through industrial action in 2009 in the Lindsey Refinery Dispute, prior to the renegotiation (Broughton 2009).

Machinery that stipulated pay minima, including the application of specific pay grades as well as a base minimum, to entire sectors was largely abolished by the Conservative Thatcher-Major governments by the early-1990s. The last remaining institution to set industry-level wage minima, the Agricultural Wages Board, has no direct application to the field of public procurement. Moreover, in summer 2011 the government announced that it intended to

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<sup>36</sup> The situation as regards the design and levels of in-work benefits is in flux, pending the current Conservative-Liberal coalition's proposal to introduce a 'Universal Benefit' from 2013. This would replace a range of existing benefits, and be phased in over several years. For an outline, see Morgan (2012).

<sup>37</sup> The agreement allows some exemptions in the case of short-term maintenance carried out by non-UK employees: NAECI 2010-2012, Sect. 20:4.

abolish the Board and bring agricultural workers within the scope of the National Minimum Wage.

The pay terms of a collective agreement can only be enforced, by application of the individual employee to an Employment Tribunal, if they have been 'incorporated' into an individual contract of employment. The collective agreement itself has no *erga omnes* effect on employment relationships or potential employment relationships in its scope.

As such, the only form of generally applicable pay regulation that can be enforced in law in the UK is the National Minimum Wage. Other stipulations pursued by official bodies in procurement may only do so voluntarily by way of agreement with suppliers or as permitted in other stages of the tendering process or, where appropriate, in the performance of the contract.

In addition to pay, employers must comply with the law on working time and discrimination/equality. Since these have a legal foundation binding on all employments, they can be included in contracts for public procurement and also cover any workers posted to the UK. In principle, a supplier could be excluded from a tender at the selection stage on the grounds of non-compliance with EU law (and its transposing provisions) in the field of Posted Workers, and equality/equal treatment (where there is also a specific public duty: see below) or a record of litigation in the area. As noted in the short case-study of Oxford City Council below, questions on diversity are included in the prequalification questionnaire for tenderers.

The approach taken by the UK government when transposing the requirements of the European Posted Workers Directive (96/71) did not make use of the provisions of Article 3(8) that deals with the status of collective agreements in the construction industry in jurisdictions lacking an extension mechanism. As such, although the option exists in theory for certain qualifying collective agreements to apply, this is not the case in the UK: any minimum pay rates or other provisions in such an agreement cannot, therefore, be made a requirement of a public procurement contract.<sup>38</sup>

In local government, an agreement concluded in 2003 between the then Labour government and public service unions led to a policy to regulate employment terms and conditions when local authorities transferred staff to private firms that had secured contracts to provide services. The policy, enshrined in the Code of Practice on Workforce Matters in Local Authority Service Contracts (2003), required that where a private sector contractor recruited new employees to work alongside staff transferred from the public sector (and whose terms and conditions were protected by the Transfer of Undertakings Protection of Employment [TUPE] Regulations), the new employees should not have any less favourable terms and conditions of employment and 'reasonable' pension conditions. These principles were extended to other public sector contracts in 2005 under the Code of Practice in Public Sector Service Contracts. These codes were abolished in March 2011, in particular in order to support the current government's policy of promoting procurement for SMEs. Although the new 'Principles of Good Employment Practice' include broadly similar provisions to the previous code, the key difference is that the new 'Principles' are voluntary, and 'outside of the formal procurement decision making process' (Cabinet Office 2010).

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<sup>38</sup> For the implications of this for the engineering construction industry, the Lindsey Refinery dispute – which crystallised many of these issues – and an interpretation of EU law in this area, see below and Barnard (2009). Barnard argues that certain conceivable social clauses in an agreement, in this case the requirement to employ a set percentage of locally unemployed workers, might be compatible with EU law 'if the need to promote local employment is framed not solely in terms of national social rights but by reference to a range of other Community policies in related areas' (ibid.: 262).

As noted immediately below, public procurement regulation in the UK has incorporated a range of other social objectives considered compliant with European Union procurement requirements.

## **Public procurement and social requirements**

The official framework for public procurement was established through the Office of Government Commerce (OGC 2006). This body was established as an agency within the Treasury, but was moved to the Efficiency and Reform Group in the Cabinet Office following the June 2010 General Election that resulted in a Conservative-Liberal Democrat coalition administration. To quote the OGC's mission statement, the body exists to 'provide policy standards and guidance on best practice in procurement, projects and estate management, and monitors and challenges Departments' performance against these standards'. The focus of the ERG is to achieve 'best value' in procurement, subject to policy considerations deemed consistent with European law: this includes 'sustainable procurement', the promotion of equality, and support for SMEs.

In its response to the Green Paper on Modernising Public Procurement, the UK government noted that 'the underlying policy objective of public procurement is to get value for money and the achievement of complementary policy objectives should not compromise this'. In particular, additional requirements should remain 'relevant to the subject matter of the contract' (COM (2011) 15 final.).

On the issue of contract performance clauses that include requirements on labour standards, the government argued that 'contract performance clauses are the most appropriate stage of the procedure at which to include social considerations relating to the employment and labour conditions of the workers' but noted that the 'main issue' was to ensure that these were relevant to the contract. 'Clarification and guidance on this would be welcome' (ibid.: 19). As noted below, the Greater London Authority has adopted this approach, and includes Living Wage provisions in certain contracts as a contract performance condition.

Much of the focus of the current administration has been on environmental sustainability, and in particular energy efficiency and CO<sup>2</sup> reductions in government properties, as well as steady downward pressure on costs of all kinds. This has, in practice, led to downward pressure on wages by service providers to the state in sectors that already account for many low-paid workers, such as the care sector (where there are also allegations of pay rates below the NMW level).

The European Public Procurement Directives were implemented in Great Britain<sup>39</sup> through Regulations that came into force on 31 January 2006 (The Public Contracts Regulations, 2006: SI 2006/5, amended in 2009, SI 2009/2992). This included the provision, written through from the Directive, that a contracting authority may request an explanation for an 'abnormally low' offer for a range of reasons, including a request that the bidder should be able demonstrate 'compliance with the provisions relating to employment protection and working conditions in force at the place where the contract is to be performed' (Part 5: 30: 6 and 7). As yet, this clause appears to have only been applied, at least in terms of publicly-reported cases, where a contractor contended that a competitor's bid was well below the

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<sup>39</sup> Great Britain comprises England, Wales and Northern Ireland: separate Regulations were adopted in Scotland.

range of what might be expected and the public authority had not requested an explanation.<sup>40</sup>

The main dimensions of official guidance on social aspects of procurement were set out in OGC (2006). This document remains on the official website for procurement and can therefore be held to reflect official thinking, pending any review. It states that in order to comply with EU procurement law, any incorporation of social issues<sup>41</sup> must be: relevant to the subject of the contract; consistent with government policy on value for money, but not necessarily at lowest price; be approached from the point of the 'whole life' cost.

The main social areas identified were (OGC 2006: 1 and Appendix A):

- community benefits,
- core labour standards (ILO). The guidance notes: 'Use the selection stage of a procurement to identify any convictions or evidence of grave professional misconduct a tenderer may have. These might relate to a breach of the labour laws in the country in which a tenderer operates. Poor labour standards may also lead to poor performance on previous contracts of a similar nature which can be another reason for exclusion' (ibid.:, 34f.). It also notes that poor health and safety standards may have a negative impact on the quality of supplies.
- disability, race and gender equality (see immediately below),
- employment, skills and training: guidance expressly states that it is not permitted to require that suppliers employ local people; if included as a condition of the contract, as opposed to voluntary post-award, they must be consistent the basic principles noted above.
- 'Fair Trade': the guidance states that it is not permitted to specify Fair Trade only or the use of a Fairtrade logo. However, Fair Trade supplier applications may be 'welcomed' and contracts awarded on a value-for-money basis. Direct sales to staff under catering contracts are exempt from EU provisions in this area.
- SMEs, including enterprises owned by ethnic minorities, women and people with disabilities. These may be promoted and contracts may be framed (such as sub-division) to make them more accessible to such firms.

A procuring authority may consider an employer's past performance on these issues when selecting for a tender, provided such evidence is relevant to the contract (see also 'Equality' below). Social criteria may be used to select only if bids are broadly equal in terms of value for money.

Prequalification questionnaires are commonly used to raise issues with suppliers: in September 2011, the UK government announced that it would seek to eliminate such questionnaires entirely for all central government procurements under approximately £100,000 (the EU threshold), with procurers 'free to choose the best route to market for the individual circumstances' (Department for Business, Innovation and Skills 2011).

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<sup>40</sup> The bidder obtained an injunction to prevent the low bid being accepted, but the case was eventually resolved out of court (*Morrison Facilities Services Limited v Norwich City Council* [2010] EWHC 487 (Ch)).

<sup>41</sup> In a number of papers consulted for this study, the term 'social requirement' was used in preference to 'social clause' as the latter might be taken to mean a contractual condition rather than a broader approach that guides the selection of, engagement with and monitoring of suppliers.

## **The issue of equality**

Public authorities are subject to 'equality duties' that attach not only to the authority but also public services ('public function', defined in statute): under the Equality Act 2010 new provisions in this area came into force on 5 April 2011. Under these obligations, public authorities must:

- Eliminate unlawful discrimination, harassment, victimisation and other prohibited conduct.<sup>42</sup>
- Advance equality of opportunity between people who share a protected characteristic and those who do not, by removing or minimising disadvantages suffered by people due to their protected characteristics; taking steps to meet the particular needs of people from protected groups; and encouraging people from protected groups to participate in public life and other activities.
- Foster good relations between those who share a protected characteristic and those who do not.

Where a public authority contracts out a public function that is subject to an equality duty it must ensure that these obligations continue to be met by a provider in respect of this function, and this can be specified and enforced through specifications set out during the procurement process. Enforcement powers ultimately reside with the UK Equality and Human Rights Commission.

## **Local government – the National Procurement Strategy**

As far as local government is concerned, and for contracts that fall below the EU threshold, there are number of specific statutory requirements, and the legal position is complex: the OGC guidance also applies to local authority procurement.

The Local Government Act 1988 (Sect. 17: 5(a), much of which is still applicable, stated that local authorities could not include 'non-commercial' reasons in their grounds for deciding on which supplier receives a public contract. This included 'the terms and conditions of employment by contractors of their workers or the composition of, the arrangements for the promotion, transfer or training of or the other opportunities afforded to, their workforces'. The Local Government Act 1999, which introduced the current 'best value' regime, relaxed the restriction on including the terms of employment of contractors, provided these are relevant to achieving best value. However, this provision is not seen by local authorities as being sufficiently robust as a legal basis to allow them to require contractors to pay a Living Wage to their employees (see below).

The Local Government Act 2000 placed a duty on English and Welsh local authorities to prepare a community strategy for promoting or improving the economic, social and environmental wellbeing of their area and contributing to the achievement of sustainable development in the UK. This must, however, be consistent with best value requirements and EU law.

The 2003 UK government's National Procurement Strategy for Local Government also made explicit a requirement on local authorities to realise community benefits through procurement activities, but within the framework established by domestic and EU law, and hence subject to the OGC guidance noted above.

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<sup>42</sup> The protected characteristics are: age, disability, gender, gender reassignment, pregnancy and maternity, race, religion or belief and sexual orientation.

The 2012 Public Services (Social Value) Act, the result of a bill sponsored by an individual (Conservative) MP, includes a new duty on public authorities during procurement. Specifically, it requires public authorities to consider how 'what is being proposed to be procured might improve the economic, social and environmental wellbeing of the relevant area' and how the procurement process might secure such an improvement', subject to EU requirements on appropriateness and proportionality. However, the main additional 'improvements' included have been seen mainly collateral social gains in contracting, such as employing people with disabilities or reintegrating the unemployed through training. However, Newcastle City Council, in developing a Living Wage policy, noted that the Act 'provides an opportunity for the City Council to emphasise the local economic benefits of a Living Wage in its procurement processes' (Newcastle City Council, 2012: 12).

Overall, local authorities have some scope to assess the benefits of 'fair employment terms' (see below) when procuring contracts at the tender evaluation stage, but this must take place on a case-by-case basis. Different local authorities appear to differ in how they interpret the existing law, and what steps they would take, for example, not to select a supplier who refused to implement fair employment terms.

Further below, short case studies are included on the Greater London Authority, Oxford City Council, and Preston City Council.

### **Minimum wage and 'Living wage'**

Aside from the NMW there is no mandatory pay level in the UK. Public bodies may ask suppliers at prequalification stage to guarantee higher pay standards, such as the Living Wage (see below), but can only do this through exhortation, through identifying 'business case' benefits that relate to the product or service as a contract performance condition (such as lower staff turnover), or incentives, such as accreditation.

A Living Wage has been defined as 'a wage that achieves an adequate level of warmth and shelter, a healthy palatable diet, social integration and avoidance of chronic stress for earners and their dependants' (Family Budget Unit). The concept of the 'Living Wage' has been one of the main responses to the problems associated with the NMW – in particular:

- that it is too low to guarantee an adequate living standard for recipients,
- that it requires supplementary payments through in-work benefits such as Working Families Tax Credit, which pays a proportion of childcare costs<sup>43</sup>, to provide such a living standard,<sup>44</sup>
- and that living costs in London are much higher than the rest of England: it is estimated that 11 per cent of full-time and 46 per cent of part-time employees in London earn below a Living Wage.

This latter element has also led to the adoption of two levels of the Living Wage: one for London, and one for the rest of the UK (for calculation see further below). There are a number of campaigns, which have trade union involvement, and research institutes that have developed methodologies for calculating a Living Wage, and for propagating it.

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<sup>43</sup> This was 80 per cent, but has been reduced to 70 per cent in 2011, and is subject to income thresholds

<sup>44</sup> GLA Economics, which calculates the Living Wage for London, notes that without tax credits, the rate per hour that employers would need to pay to meet the living standard criterion would be £10.70 an hour (GLA Economics, 2012: 7).

The Living Wage campaign has its origins in the community organisation, London Citizens (then TELCO) in 2001. In 2003, TELCO worked with local unions to win a Living Wage for workers at four London hospitals. In 2004, London Citizens invited London mayoral candidates to commit themselves to support a Living Wage. Ken Livingstone (Labour), who won the 2004 election, created the Living Wage Unit at the Greater London Authority and this now calculates the London Living Wage (see below). In the 2008 campaign, London Citizens obtained a renewed pledge from Boris Johnson (Conservative) to implement and 'champion' the London Living Wage, and under his administration GLA has continued to calculate the wage. London Citizens has also established the Living Wage Foundation.

The Living Wage Foundation ([www.citizensuk.org/campaigns/living-wage-campaign/the-living-wage-foundation](http://www.citizensuk.org/campaigns/living-wage-campaign/the-living-wage-foundation)) operates a formal accreditation scheme for organisations in London under which organisations may apply for a licence to use the 'Living Wage' 'brand', for which there is a variable charge depending on the size of the workforce. Licensees must pay all employees aged over 18 (but excluding apprentices) not less than the London Living Wage, increase this rate within six months of any uprating (see below), and notify employees of the change. Licensees must also ensure that contractors providing sub-contracted staff who work on the licensee's premises must also be paid the Living Wage as if they were direct employees. Licensees must keep appropriate records, and make them available on request to the Foundation, which also stipulates that it must have independent access to employees and representative trade unions.

The Scottish Living Wage Campaign has broad civil society and trade union involvement, and was established in 2007 (Scottish Parliament 2012b: 5). The Scottish government has introduced a living wage for directly employed staff, staff in agencies (that is, official bodies that implement policy), and the NHS in Scotland. During 2012 there have been discussions within the Scottish Parliament about the prospects for promoting the adoption of a Living Wage in public procurement in Scotland (Scottish Government 2012). In preparing this, the Scottish Government sought guidance from the European Commission, which noted that any requirement imposed on contractors to pay a wage above the UK NMW 'is unlikely to be compatible with the Treaty on the Functioning of the European Union. In practice, this means that public bodies cannot address payment of a living wage as part of the award criteria for a public contract nor make it a condition of contract performance' (ibid. 2f.)<sup>45</sup> During 2012, there was a consultation, sponsored by an individual member of the Scottish Parliament, John Park MSP (Labour), to explore the prospects for a 'procurement-only' Scottish law requiring payment of a Living Wage in contracts.<sup>46</sup> To quote the consultation document, the bill 'would impose a contractual obligation on the successful tenderer to pay the living wage to workers employed on the contract. The obligation would be owed by the tenderer to the contracting authority and any breach would only be remediable by the contracting authority raising an action for breach of contract against the successful tenderer. There would be no individual right for workers on public procurement contracts under the employment tribunal system to raise an action for non-payment of the Living Wage' (Living Wage Scotland Bill, A

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<sup>45</sup> A legal opinion commissioned by the Scottish Parliament concluded that a living wage provision set out in a procurement-related statute could be lawful under certain conditions, and emphasised the need to stress the benefits to workers directly affected of a Living Wage in terms of protecting their human rights and dignity (Scottish Parliament, 2012a: 11ff).

<sup>46</sup> Under arrangements for devolved government in Scotland, employment rights remain the prerogative of the UK government. However, it was considered that there was scope for separate provisions on procurement.

consultation by John Park MSP, 2012).<sup>47</sup>

The Living Wage is supported, in principle, by Prime Minister David Cameron ('an idea whose time has come'). However, Living Wages are not implemented in central government procurement in England and Wales, and only one government department reportedly pays its staff the Living Wage. The government encourages adoption of the Living Wage on an entirely voluntary basis, mainly on 'business case' arguments, such as lower staff turnover.

During the course of 2011/12, the opposition Labour Party has moved closer to developing a formal Living Wage policy, and the proposal was strongly supported by shadow Cabinet ministers and the Labour Party leader, Ed Miliband, during 'Living Wage week' in November 2012. The policy is not yet fully formed, and would need to navigate the obstacles set by EU provisions. The policy ties in with the notion of 'pre-distribution', which is one of the responses to growing pay inequality in the UK and the limits to tax-based redistribution through the welfare system, with the Labour Party committed to not making further spending commitments in this area. As such, the policy aims to achieve savings in in-work benefits, currently tax credits, and make these available in other forms to companies and organisations that pay a Living Wage. Although this might redraw the boundaries between income through work and income via redistribution, it would not necessarily mean that there would be a net reduction in public spending.

Elements that have been suggested by various senior Labour Party figures include:

- Making the Low Pay Commission responsible for calculating the Living Wage (see too immediately below),
- Encouraging local authorities to secure employer agreement to pay Living Wages in public contracts, and using some of the savings from tax credits to create local skills funds to provide training for young people. Direct tax benefits to compliant firms.
- Exploring legal options to require local authorities to gain a commitment from suppliers to pay the Living Wage.

## Calculating the Living Wage

In London, the Living Wage is calculated by the GLA Economics, part of the Greater London Authority (see below). Outside London, it is calculated by Minimum Incomes Standards Project at the Centre for Research in Social Policy, Loughborough University.<sup>48</sup>

The 'Minimum Income Standard' is based on survey data for what is considered to be an acceptable level for different types of household. The MIS method then works out the wage needed to meet these costs. An alternative method, the 'Income Distribution' approach, calculates the rate that would be equivalent to 60 per cent of median income for London, the official poverty line. In 2011 the MIS figure was above the Income Distribution figure. Outside London, the base MIS figure plus a typical figure for housing costs and childcare totalled some £240 per week, or gross earnings of £287, equivalent to an hourly rate of £7.67 (based on an assumed 37.5 hour week). Most Living Wage requirements continue to be based on

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<sup>47</sup> In December 2012, John Park resigned from the Scottish Parliament to take up a senior strategic role in the UK trade union, Community.

<sup>48</sup> The calculation was previously carried out by the Family Budget Unit, based at the University of York. This was dissolved in August 2011, and the role transferred to the Minimum Income Standards Project (MIS) at Loughborough University ([www.minimumincomestandard.org](http://www.minimumincomestandard.org)). The work to update the MIS annually is financed by the Joseph Rowntree Foundation (for the 2011 report see: Hirsch 2011).

the 'non-London' rate of £7.45 (as from 5 November 2012). The London Living Wage stands at £8.55 an hour, as from 5 November 2012.

This figure will vary as between household types and will also be affected by changes in tax rates and thresholds and benefits: for example, some childcare costs can be covered by the Working Families Tax Credit, but the rate was reduced from 80 to 70 per cent in 2011. As a consequence, the 2011 MIS update noted that 'the gap between the NMW and the wage needed to reach the MIS level has widened considerably, especially for families with children' (ibid.: 18).

## **The use of living wages - case studies**

A large and growing number of local authorities are pursuing Living Wage policies. As of 2012, this was around 20, of which nearly all are Labour-run administrations. However, what this means in practice is not always clear. In some cases, Living Wage policies have been adopted for council staff only; in others, there is an intention or practice of applying it to new contracts as they fall due. In other cases, policy is at an early stage of development. The three short case-studies below are intended to highlight the complexities of calculation and implementation in practice. Two local authorities were also visited: Oxford City Council and Preston City Council.

### *Greater London Authority (GLA) Group*

The GLA Group consists of the five bodies that represent the 'upper tier' of local government in London, providing a range of London-wide services. The 'lower-tier' consists of the 32 London Boroughs responsible for schools, social services, waste collection and roads. The GLA bodies are:

- Transport for London (TfL)<sup>49</sup>,
- Greater London Authority (GLA),
- London Development Agency (LDA),
- London Fire and Emergency Planning, Metropolitan Police Authority and Service.

The total annual volume of procurement is some £3.4 billion.

'Responsible Procurement' was a policy initiative begun during Ken Livingstone's office as Mayor of London (2004-2008), a position reintroduced by the Labour Government (1997-2010) following the previous abolition of all-London governance by Margaret Thatcher in 1986.<sup>50</sup> Within the GLA Group, each agency or authority has been responsible for its own operational implementation of the 'Responsible Procurement' policy (see also below).

'Responsible Procurement' covers wide range of policies and priorities, including supplier diversity and support for SMEs, environmental issues, skills development and community benefits, equality, and 'ethical sourcing', the core of which is the 'London Living Wage'. During the campaign for the Mayor's office in 2008, the Conservative candidate, Boris

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<sup>49</sup> TfL now owns all the undertakings that maintain and operate London Underground: from 2003-2011 these were public-private partnerships, but the consortia involved came back into public ownership following the collapse of one firm (Metronet) and the acquisition of the other Tubelines.

<sup>50</sup> Ken Livingstone ran in the 2000 campaign as an independent, following his expulsion from the Labour Party for standing against the official Labour candidate. He was readmitted just prior to the 2004 mayoral election

Johnson, committed himself to maintain a 'Living Wage' clause in GLA procurement, and the number of organisations committed to paying the London Living Wage has continued to increase.<sup>51</sup>

The London Living Wage currently stands at £8.55, compared with the adult rate of the statutory National Minimum Wage (from 1 October 2012) of £6.19, a difference of some 38 per cent. It is intended to offset the higher cost of living in London compared with the rest of the UK. For comparison, childcare is 23 per cent more expensive than the England average; housing costs are around 50 per cent higher than the national average; and transport in London is 63 per cent more expensive than in other large urban areas in the UK (Centre for Economic and Social Inclusion 2011). The rate is calculated by GLA Economics (now part of the GLA Intelligence Unit), using the FBU methodology, based on a 'Low Cost but Acceptable' Standard, termed 'Basic Living Costs' by GLA and an Income Distribution method (under which a rate is calculated to place a household on the 60th percentile of median income). For 2012, the Basic Living Costs method yields a figure of £7.10 per hour and the Income Distribution method a figure of £7.80 per hour. The average of these two figures is defined as the 'poverty threshold wage', equivalent to £7.45 per hour. This is supplemented by a 15 per cent 'margin' to allow for unforeseen events, giving a (rounded) £8.55 per hour. If employees in this section of the income distribution were not receiving a range of in-work benefits (tax credits, housing benefits and council tax benefits), the rate would need to be as much as £10.70 an hour.

The rate of the London Living Wage was increased by 5.7 per cent in 2011 over the 2010 figure, and 3 per cent in 2012, considerably more than the average rate of earnings growth in the UK in recent years. Since its inception in 2004 has been uprated by some 27 per cent, and its level above the NMW has risen from 33 to 38 per cent.

In order to comply with EU law, the GLA does not require compliance with the London Living Wage as a blanket condition: however, it has also moved further than simple exhortation.<sup>52</sup> The GLA's approach is to consider the scope for implementing the London Living Wage 'on a case-by-case basis for each contract, within the context of the Mayor's overarching commitment to promoting the London Living Wage... We consider the relevance and proportionality of London Living Wage provisions to the subject of the contract, its size and duration. Applying this case-by-case approach the GLA Group has implemented the London Living Wage across a number of support services, most notably cleaning, catering and portering contracts within the parameters of the EU Public Procurement Regulations and Best Value' (Mayor of London, 2009: 2). This is undertaken at the tender stage, both to save negotiation costs later in the procurement process and 'pre-prime' contractors about the

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<sup>51</sup> 'Paying the London Living Wage is not only morally right – with the potential to massively reduce child poverty in London – but also it makes good business sense. What may appear to a company to be an unaffordable cost in a highly competitive market is more appropriately viewed as a sound investment decision' (GLA 2011: 5). The consensus on this issue between Livingstone (seen as left-wing Labour) and Johnson (libertarian/neo-liberal Conservative) is interesting, and derives, arguably, in part from the unique social composition of London and the 'trickle down' economics of a global city with a large financial services sector – strongly supported by both.

<sup>52</sup> This has raised questions about the lawfulness of the GLA approach, highlighting the need for further clarification of EU law (Ross 2012). The GLA official consulted by the Scottish Parliament on the issue expressed themselves in 2012 in the following terms: 'There have been some contractual and legal difficulties about whether it is possible to specify the living wage in tender documentation. The office of Government commerce has been particularly concerned with a European Court case about whether it is legal for us to specify the living wage. I think that the law is still a bit uncertain on that point, but in practice we have had two fairly bullish mayors who have championed the living wage irrespective of that. As far as I am aware, no employer has ever taken any part of the GLA group to court, and we do not anticipate that anyone will do so. In that regard, the roll-out will continue' (Scottish Parliament, 2012b: 24).

Living Wage policy in order to allow them time to adapt. This document also notes that the GLA group's preferred approach is 'to link the introduction of [the] London Living Wage to increased performance objectives for contractors and staff training programmes to ensure contracted staff have the skills to warrant these improved performance requirements' (ibid., 6). Transport for London also noted that it considers the applicability of the London Living Wage at the start of the procurement process, and applies it only when 'relevant and proportionate', depending on factors such as the prevalence of low pay in the sector and location of staff working on TfL contracts. The London Living Wage is then included as a contract performance condition, 'with the requirement clearly set out in the invitation to tender documents and in the terms and conditions of relevant contracts' (Scottish Parliament, 2011: 2ff.). In some service areas, cost/benefit sharing models apply as between the authority and the contractor; in others, the supplier bears the additional cost alone. TfL has also undertaken research suggesting that lower turnover and reduced absence lower the net cost to employers. Monitoring is undertaken by contract managers, and contractors are required to warrant and verify that they pay the London Living Wage.

As of November 2012, nearly 200 organisations had committed themselves to implement a living wage policy (Greater London Authority 2012: 7). Rates paid by contractors are not changed when GLA announces an increase but are implemented 'as contracts allow' (Greater London Authority, 2012: 25). An accreditation by the Living Wage Foundation requires pay to be raised in line with changes in the Living Wage.

An estimated 9,000 families have benefited directly, including 3,000 employees working for companies with contracts for GLA organisations, including 700 cleaners on London Underground brought in during 2010.<sup>53</sup>

The following table sets out the increases in the calculation of the London Living Wage (LLW) in comparison with the National Minimum Wage (NMW), the difference between the two, and the required level of LLW without payment of in-work benefits, such as Tax Credits.

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<sup>53</sup> For calculations of the impact in London, see <<http://www.geog.qmul.ac.uk/livingwage/numbersandmoney.html>>. This role will pass to the Living Wage Foundation in the near future.

**Table 7.1: National Minimum Wage (NMW), London Living Wage (LLW) and LLW without benefits such as tax credits (in £, per hour)**

| Year | NMW  | LLW  | Difference between NMW and LLW | LLW without benefits |
|------|------|------|--------------------------------|----------------------|
| 2003 | 4.50 | 6.40 | 1.90                           |                      |
| 2004 | 4.85 | 6.50 | 1.65                           |                      |
| 2005 | 5.05 | 6.70 | 1.65                           | 8.10                 |
| 2006 | 5.35 | 7.05 | 1.70                           | 9.00                 |
| 2007 | 5.52 | 7.20 | 1.68                           | 9.15                 |
| 2008 | 5.73 | 7.45 | 1.72                           | 9.60                 |
| 2009 | 5.80 | 7.60 | 1.80                           | 9.85                 |
| 2010 | 5.93 | 7.85 | 1.92                           | 10.15                |
| 2011 | 6.08 | 8.30 | 2.22                           | 10.40                |
| 2012 | 6.19 | 8.55 | 2.36                           | 10.70                |

Source: Queen Mary University, Dept of Geography, London Living Wage Research <http://www.geog.qmul.ac.uk/livingwage> and GLA Economics, 2012: 7.

### *Oxford City Council*

The City of Oxford is recognised as a high-cost area, with house prices only just below London levels. The Oxford Living Wage had its origins in a local campaign ('Oxford Living Wage Campaign), which worked closely with low-paid workers in the city, including at Oxford colleges, on the need for an approach to offset high living costs. The campaign included local officials of the public sector union UNISON, as well as student groups and societies (Fair Pay Network 2010: 17).

In November 2007, Oxford City Council voted to become a 'Living Wage Employer' from April 2009. This would apply to all its own staff, including temporary workers and sub-contractors. This resolution also included a commitment to 'work together with living wage campaigners, low paid workers, trade unions and employers' to make Oxford a 'Living Wage City' 'in which every worker earns a living wage' (Motion adopted by Oxford City Council, November 2007). As well as taking action directly on implementing a Living Wage, the Council also voted that an implementation report should be prepared to explore the financial commitments entailed by becoming a Living Wage employer 'including redistribution of current salary levels within the Council structure' (ibid.). Steps were also taken to reduce the use of agency workers, with the effect that more permanent staff would benefit from the Living Wage policy.

The Living Wage was set at £7.00, as a figure mid-way between the then London rate of £7.20 and some other rates adopted in the British provinces (since updated). At that time, no methodology was used to calculate a specific Oxford rate based on local circumstances. For the future, it was decided that the council would increase the Living Wage in line with any pay increases negotiated for local government and also review the level of the Living Wage every two years, and adjust it in line with movements in the London Living Wage. Local officials of trade unions were consulted.

The City Council spends c. £50 million annually on bought-in goods, services and works, of which some 60 per cent is with local suppliers. Although, as noted above, the City Council

considers that it may not make it a condition of issuing a contract that a supplier complies with the stated Living Wage level or adopt a blanket policy of not considering tenders from contractors unwilling to implement such a clause in their employment contracts, the Council has stated that 'it is possible ... to take positive action through the tender process by exploring potential contractors' attitudes to the Living Wage alongside their approach to equal pay, fair employee relations and management on the basis that a positive approach is likely to produce improved outcomes' (Oxford City Council 2009).

It was decided that the City Council's procurement officials should introduce 'measures designed to allow appropriate consideration to be given to the sustainability of the offers received, such consideration to include the supplier's attitude towards the payment of the Living Wage, when considering the overall merits of the offers received ... All such considerations will form part of the process to determine the lowest or most economically advantageous offer received in accordance with the Council's contract rules' (ibid.).

This is carried out by including questions on these issues in the prequalification questionnaire that tenderers must complete, and from which the City Council gauges the their 'technical knowledge and experience, capability/capacity, organisational and financial standing to meet the requirement' (Oxford City Council 2011). As well as questions on diversity and equality, the questionnaire asks: 'The Council agreed a Living Wage Policy in 2009. The Council requests as part of any key contract or supply arrangement that the contract provider pays any employee over 18 a minimum rate of pay of £7.19 an hour (based on 2010/11 pay rates). Please confirm whether you accept this.' As yet, all potential suppliers have indicated that they would comply. Potential suppliers are also informed about the policy at 'Meet the Buyer' events. Some contracts have also had provisions on providing apprenticeship places agreed with suppliers.

The Council also checks the financial position of suppliers to ensure that it is able to comply. It would not be lawful for the Council to exclude a supplier on these grounds, but reputational reasons and a desire for a good relationship with the Council suggest that firms are willing to agree voluntarily.<sup>54</sup> Once a term of business, the requirement can be enforced as part of the contract. As yet, the Council has not attempted to apply 'business case' criteria to procurement decisions (such as reduced staff turnover), as suppliers have been willing to agree to pay a Living Wage.

At present, the policy only applies to first-tier suppliers, and all the high-value contracts for the Council are now compliant, including commodity contracts for building materials. Suppliers are checked annually in a contract management review. Members of the Council may seek to extend the policy further down the supply chain, although it is recognised this would create monitoring issues.

### *Preston City Council*

In 2008 Preston City Council began to consider the implications of becoming a Living Wage Employer, and a vote was passed in December 2008 confirming this. Initially, the City Council moved to ensure that its own direct employees and any contract (that is, agency) employees were paid the Living Wage. This also had an impact on the local authority wage agreement as it superseded a number of the lower grades.<sup>55</sup> In September 2011, following

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<sup>54</sup> Keith Ewing has also argued that a legal challenge by a UK-based supplier is unlikely (see Fair Pay Network 2009). This view was shared by some individuals consulted for this study.

<sup>55</sup> As yet, there does not appear to have been any reaction by trade unions either in Preston or elsewhere to the erosion of differentials and the clustering of pay around the Living Wage level, according to one union official consulted for this study.

local elections in which the Labour Party became the ruling party, the Council voted to secure the payment of a Living Wage in its procurement, and encourage and promote Living Wage principles to all employers in the city. Its intention is to operate within the current legislative framework to 'implement the Living Wage Policy in procurement practices on a case-by-case basis'. Preston has also been able to draw on the experiences of other authorities, such as Oxford to develop a policy that it considers to be legally compliant.

The rate is set at the non-London Living Wage rate (£7.45 from November 2012), as calculated by the Centre for Research in Social Policy at the University of Loughborough.

Preston City Council will initially operate its own accreditation scheme under which any company that wishes will be able to register as a 'Preston Living Wage Employer', and will be listed as such on a council website, provided they pay the Living Wage to all of their staff, broadly in line with the Living Wage Foundation's provisions. The Council will also initiate a Local Social Forum, to bring together civil society actors to promote quality employment.<sup>56</sup>

At the time of writing, commitments to pay a Living Wage had been obtained by developers on a major new site (the 'Central Business District') to cover construction and administration of the site. Commitments were also made on apprenticeships and traineeships. In part, this was possible because the investment was being made by a pension fund which had a mandate to promote local employment and used regeneration projects to make a social impact: as such the agreement was voluntary in nature. Further progress was expected through local higher education institutions and housing bodies. The City Council was also intending to implement its procurement approach with two impending contracts that would entail purely private sector firms: one for car parking and the other for security CCTV.

The legal opinions reflected in Preston's policy document illustrate the complexities involved in the UK. The approach will be to consult with tenderers to establish whether they are prepared to adopt the Living Wage, and the response will be 'taken into consideration' when selecting, and would include a value-for-money assessment.<sup>57</sup> Supplier consent would also be promoted by the 'additional consideration' given to suppliers at the evaluation stage if they paid the Preston Living Wage compared with those that did not. It is accepted that it cannot be a condition. The approach would not be applied to suppliers providing office supplies, but would be sought in areas of labour provision (cleaning, catering, grounds maintenance, social care).

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<sup>56</sup> Preston City Council has also drawn on the example of the Islington Fairness Commission, which was set up in May 2010: Islington is an inner-city district in London. The Commission included Professor Richard Wilkinson ('The Spirit Level'), senior figures from Islington Council, Islington Police, NHS, Homes for Islington, Islington Trades Council (local trade unions), Islington Chamber of Commerce, City and Islington College, Cripplegate Foundation, and London School of Economics. The Commission met in public and took evidence from the community on health, housing, family, community, social care, education, skills and training, employment, crime and safety, democracy, sustainability, environment and economy (Islington Fairness Commission 2011). Fifteen large employers in Islington currently pay the Living Wage.

<sup>57</sup> Preston City Council, Report to Cabinet, 'Living Wage', 31 August 2011. The Council states that business case arguments cannot be tested objectively for individual contract awards, and that any decision must be made on a case-by-case basis, 'with any impact on costs fully assessed and justified', and is likely to encounter 'some practical difficulty'. Service and price are expected to remain the 'key determinants'. In making its decision on selecting suppliers that paid the Living Wage as opposed to those that did not, the Council states it will be guided by 'normal principles of administrative law, including the requirement to act in a "Wednesbury reasonable" fashion' (ibid., 3.28). This term refers to an English legal principle established in case law: it might be roughly interpreted as 'proportionality'. The Council states that there are grounds for its policy within the parameters of its fiduciary duty to tax payers and 'obtaining best value'.

Once included in a contract voluntarily, it can be enforced. In addition, in order to ensure cost-neutrality for suppliers, the Council 'is prepared to pay a higher contract sum to compensate for the extra cost incurred in paying higher wages' (ibid.). It might also be the case that staff working on a Preston contract would have to be paid more than other staff in the same supplier working on other contracts: this could be a disincentive for suppliers, as they might face internal claims for pay equality. The Council accepts that it may need to wait for tenderer responses to establish whether such arrangements are attractive to suppliers, but hopes that the prospect of future contracts would be an incentive. The Council would monitor contracts for 12 months.

The City Council also operates a 'Fair Employment Policy', which promotes 'equality and fairness', non-discrimination and the combating of social exclusion, 'recognising the connection between service quality and the management of workforce issues'. This is implemented through engagement with suppliers, and a request to include fair employment clauses once a value-for-money has been made.

### **Trade union policies on public procurement**

Trade unions in the UK have faced dilemmas in the area of pay and social clauses in the EU context because of their reluctance to accept or argue for legally-binding collective agreements, based on long-standing voluntaristic traditions.

The TUC has called on the UK government to amend its approach to transposing the Posted Workers Directive by taking 'advantage of the provisions in the Directive which allow national governments to introduce measures to extend coverage to include sectoral or national collective agreements in companies operating in any sector' (Resolution at TUC Conference, September 2009). It considers that the pressures to cut costs in public procurement currently make it difficult to make headway with the type of provisions discussed in the 2006 OGC guidance. The TUC has argued that collective agreements should have 'legal effect' without their being 'legally binding' on the parties as civil law contracts.

UNISON has argued for the introduction of a Living Wage for many years, both in terms of the appropriate level for the NMW and its own bargaining ambitions. In particular, it aims for a pay level that would reduce the level of in-work benefits paid to the low paid. UNISON supports the initiatives taken by local authorities noted above. UNISON has also supported a proposal outlined by Ed Miliband, during his successful campaign to become leader of the Labour Party in 2010, that companies that offer 'fair pay' should be eligible for a tax reduction on the grounds that this would reduce state subsidies in the form of tax credits and other in-work benefits. It also expects the Living Wage to figure more prominently in future collective bargaining, once the current public sector pay freeze ends. There is a strategic debate within UNISON about how best to go about this that is not yet completed: the main options are whether Living Wage issues should be brought up in local authorities or government departments, where local union organisation might be sufficient to make headway on either raising minimum pay levels or moving employees up existing scales; or whether there should be a national bargaining campaign around the issue. This also relates to public procurement as many outsourced services track the main public sector settlements. In its most recent submission to the Low Pay Commission, which advises government on the level of the NMW, UNISON advocated a rise in the minimum wage to £8.00 in order to provide a 'living wage'

The Public and Commercial Services Union (PCS) supports Living Wage initiatives, has initiated its own Living Wage campaign, based on the GLA figure, and has sought to make this part of its bargaining platform (for example, with Capita, the largest outsourcing company in the UK).

The RMT union, in the transport sector, has led a campaign for a Living Wage for cleaners working on London Underground, with a strike in summer 2008 by 700 cleaners. The RMT

has a 'Cleaners' Charter' that includes a call for a living wage, rising to £10 per hour. Some parts of the Underground count as direct public employment. Tubelines is a wholly-owned subsidiary of Transport for London (a part of the GLA: see above). From 1 July 2010, over 700 staff at Tubelines began to receive the London Living Wage, following its return to the public sector.

## Conclusions and assessment

The UK currently has access to a limited range of legal instruments to require compliance with any form of pay provision in public procurement above and beyond the National Minimum Wage. Although some recent high-profile industrial disputes have illustrated the difficulties created by the lack of legally-binding and universally-applicable collective agreements, there is no realistic prospect of the UK's legal position changing in this area in the near future to ensure that collective agreements have direct legal effect.

The legal position is complex and not always transparent: public bodies consider that there may be a 'significant legal risk'<sup>58</sup> to attempting to include pay and some social clauses, and the OGC advice has narrowed the range of possible social provisions and excludes any pay requirement, aside from the National Minimum Wage – which would apply in any event. Living Wage requirements must be agreed voluntarily, and public bodies may not require adherence with a Living Wage as a precondition for access to public procurement. However, different local authorities have interpreted this in a number of ways, as noted in the cases outlined above.

There is no mechanism that can currently specify a minimum rate for a particular skill level, and as such Living Wage requirements cannot effectively combat a clustering of pay at around or just above very low levels that have developed as a result of wider economic developments.

Living Wage provisions have been an important practical and mobilising tool that have enabled a growing number of public bodies to require compliance with pay levels above the National Minimum Wage, and to act as a benchmark for local campaigners. Campaigns have involved major efforts at grass roots organising, often led by civil society organisations and Labour Party councillors, but with a role for trade unions (see box). On balance, however, the civil society dimension is currently predominant, and is likely to remain so until Living Wage arguments figure more prominently in collective bargaining. A commitment by the Labour Party to develop policies to support the Living Wage could lead to further change in this area, should the party come to power in the future.

The coverage of Living Wage requirements is hard to judge, but remains limited. Nonetheless, there are demonstrable impacts, and in London it is estimated that 3,400 employees of the GLA have benefited directly and 11,500 employees overall. As Deborah Littmann from UNISON trade union put it (in April 2010): *"When the living wage campaign was launched less than a decade ago by London Citizens, with support from trade union UNISON, no political party or major employer dared go near it, much less claim credit for introducing it. What shifted the political landscape was the slow, painstaking work done in organising low-paid workers seeking a decent living standard. It meant building community support for their campaign and hammering on the doors of employers and politicians over and over again, using powerful stories and imaginative actions. Not only did this get across the message that this was the right thing to do, it showed that there was power – diverse, vocal and well organised – behind the demand for a living wage."*

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<sup>58</sup> The phrase used in a policy recommendation to Oxford City Council based on legal advice.

## **Appendix: Living Wage incidence**

The following is a selection of local authorities in the UK that are reported to have or be contemplating a living wage policy, either for their own staff or, where possible, for contractors.<sup>59</sup>

### **Camden**

Living Wage policy for contractors adopted in June 2011

<http://democracy.camden.gov.uk/documents/s3871/Item%2008%20-%20Workforce%20Standards%20in%20Outsourced%20Contracts%20OD%202011%2001.pdf>

### **Brighton**

Living Wage policy adopted in 2011: local Living Wage Commission exploring rate setting mechanism and levels

[http://www.brighton-hove.gov.uk/index.cfm?request=b1149084&action=show\\_pr&id=267105](http://www.brighton-hove.gov.uk/index.cfm?request=b1149084&action=show_pr&id=267105)

### **Ealing**

Living Wage policy adopted in 2007. London Living Wage paid to all in-house staff, and extension to contractors as contracts fall due on a voluntary basis.

### **Glasgow**

As from 2009, all council staff are paid the Glasgow Minimum Wage (2011: £7.20) and contractors are encouraged to pay this as part of council's sustainable procurement strategy

<http://www.glasgowlivingwage.co.uk/>

### **Greater London Authority**

Living Wage policy for contractors

<http://www.london.gov.uk/publication/fairer-london-2011-living-wage-london>

### **Islington**

Pays Living Wage to council staff, and intends to extend this to sub-contractors

<http://www.islington.gov.uk/Council/CouncilNews/PressOffice/2011/05/PR4412.asp>

### **Leeds**

Policy adopted in 2008. Not fully implemented for council staff by 2011.

<http://democracy.leeds.gov.uk/mgAi.aspx?ID=12653> and an update

<http://democracy.leeds.gov.uk/mgConvert2PDF.aspx?ID=9590&T=9>

### **Manchester**

Pays above NMW for its own staff: examining feasibility of a 'Manchester Living Wage' as of November 2011

[http://www.manchester.gov.uk/egov\\_downloads/EES\\_landO\\_November\\_2011.pdf](http://www.manchester.gov.uk/egov_downloads/EES_landO_November_2011.pdf)

### **Norwich**

Living Wage for own staff: not yet for contractors

### **Oxford**

Living Wage policy for contractors

<http://mycouncil.oxford.gov.uk/documents/s6943/Living%20Wage%20report.pdf>

### **Preston**

Policy in process of implementation

<http://www.preston.gov.uk/yourservices/jobs-and-volunteering/preston-living-wage>

Other examples include: Hackney, Newcastle, York, Birmingham, Cardiff, Southwark.

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<sup>59</sup> All references as of 27 November 2011

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## **Conclusion: Future of pay clauses in European public procurement**

*Thorsten Schulten*

Given the economic importance of public procurement, the state has always strategically used its market power to promote wider economic and societal goals. Today, social (as well as environmental) considerations are widely acknowledged as an integral part of a modern procurement policy (Kahlenborn et.al. 2011). Thus, in most European states procurement regulations encourage public authorities to accept not the *lowest-cost* but the *economically most advantageous* offer, taking into consideration further social and environmental costs. Under the financial constraints of tight budgets, however, public authorities often follow a more short-term policy and tend to choose the cheapest bids. As a consequence, a more encompassing inclusion of social award criteria will require legally binding provisions to be incorporated into procurement law.

The latter holds true, in particular, for the wages and working conditions of employees working on public contracts, as labour costs often represent the single most important cost factor in the process of competitive tendering. There are several countries in Europe that make use of pay clauses in public procurement, aiming to ensure compliance with certain minimum wages or collective agreements in public contracts. Among them are countries which have ratified ILO Convention 94 on Labour Clauses in Public Contracts, but also some countries which have *not* ratified it. As one of its major findings, this study has emphasised that pay clauses in procurement are of particular relevance in those countries which do not have an *erga omnes* system or where the extension of collective agreements is limited to a small number of sectors (see *Chapter 2*). In some respects, pay clauses in procurement can be seen as a substitute for legal extension mechanisms.

The active use of pay clauses in a couple of European countries confirms the position of the ILO Committee of Experts, which has concluded in its recent report on ILO Convention 94 that “*the basic motivation behind the adoption of the Convention in 1949 has not lost any of its relevance or persuasion.*” On the contrary, according to the ILO, current tendencies in public procurement still require a regulation of working conditions for workers under public contracts: “*Today, more than ever before, fierce competition for public contracts constrains tenderers to lower costs and as part of this process to economize on labour costs including workers’ pay and other costs related to working conditions. The incessant quest for ways to maximize profit by minimizing production cost, exacerbated by the forces of globalization, finds in this Convention a most compelling check. By proposing statutory regulation of the social aspects of public procurement, the Convention aims at counteracting extensive price competition based on costs of working conditions, skilled jobs and quality services. It introduces a truly level playing field for public procurement in so far as labour standards are concerned and puts tenderers on notice that there can be simply no “comparative advantage” at the expense of workers’ employment and working conditions.*” (International Labour Office 2008: 10).

In Europe, however, the use of pay clauses in public procurement came to a turning point with the so-called Ruffert judgment (C-346/06) of the European Court of Justice (ECJ), which stated that such clauses are only in conformity with EU law when they are backed by the European Posted Workers Directive (96/71/EC). In the ECJ’s interpretation, this is only the case when the pay clauses refer to statutory minimum wages or to universally applicable collective agreements. For all countries covered by this study, the Ruffert judgement has created some significant problems. It has either led to limitation in the scope and degree of the commitment of pay clauses or it has created major legal uncertainties, in particular

regarding the conformity of EU law with ILO Convention 94, which has been ratified by at least ten EU member states.

In *Germany*, which has been directly affected by the Ruffert case, most federal states have continued to include pay clauses in their regional procurement laws, while some of them have even brought in new ones. With the exception of the public transport sector, however, these pay clauses refer only to universally applicable collective agreements (which usually covers only the lowest pay grades of the agreements) or procurement related minimum wages. In comparison to the older procurement laws from the period before the Ruffert case, which referred to locally prevailing (and usually non-generally binding) collective agreements (including not only minimum wages but the entire pay scale), the scope and effectiveness of the new pay clauses is now rather limited.

Despite the Ruffert judgement, *Switzerland* continues with pay clauses in procurement that compel contracting companies to employ their workers under locally prevailing wage rates and working conditions as laid down in (often not universally applicable) collective agreements. Although Switzerland is neither a member of the EU nor of the European Economic Area, due to bilateral agreements with the EU it is obliged to implement – at least to a certain extent – EU procurement law. Consequently, after the Ruffert case there were also some political voices that demanded a change in Swiss procurement law in order to restrict pay clauses to universally applicable collective agreements. While such changes have not yet taken place, some legal uncertainties remain as to whether or not the current use of pay clauses in procurement is in line with the bilateral agreements between Switzerland and the EU.

In recent years the *United Kingdom* has seen a growing number of so-called “living wage” initiatives at local level that aim to establish a local wage standard above the national statutory minimum wage. One important instrument to enforce such living wages has been public procurement. However, all the living wage initiatives are based on a purely voluntary approach relying only on a political and moral commitment (Barnard 2011).<sup>60</sup> Attempts to make the payment of living wages a more binding award criterion have been rejected by referring to the Ruffert judgement: As the UK Office of Government Commerce has pointed out, “*this judgment means that imposing a contract condition requiring the payment of the London Living Wage to workers on a contract creates a risk of legal challenge against the UK, on the basis that it is restricting the freedom to provide services*” (OGC 2009: 4).

Finally, *Denmark* and *Norway*, which both have ratified ILO Convention 94, use pay clauses in public procurement that refer to prevailing (and not universally applicable) collective agreements. While in Denmark there is no possibility of declaring collective agreements universally binding at all, in Norway this is limited to a very few sectors. After the Ruffert judgement, in both countries questions have been raised as to whether the existing regulation on pay classes is in conformity with EU law. Norway has even been accused by the EFTA Surveillance Authority (ESA) that its procurement law would not be in conformity with the principle of freedom of services as laid down in Article 36 of the EEA agreement. In reaction to the ESA’s accusation Norway made some amendments to its procurement law in which it clarifies that workers under public contracts are only obliged to receive the minimum rates of pay as agreed in collective agreements. However, collective agreements that are not universally applicable continue to be a reference for pay clauses in procurement. The same holds true for Denmark, where the reference has now been specified to nation-wide collective agreements signed by the most representative bargaining parties (Danish Ministry of Employment 2012).

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<sup>60</sup> In contrast to that, in the United States many local living wage requirements have a legally binding character in procurement (Pollin 2008).

The cases of Denmark and Norway also raise the more fundamental question of the relation between ILO Convention 94 and the EU law. Before the Ruffert case, most lawyers took the view that there were no conflicts or contradictions between the two (e.g. Krüger et.al. 1998). Shortly before the Ruffert judgement this position was even confirmed by the ILO itself in its comprehensive report on Convention 94 (International Labour Office 2008: 85ff.). The Ruffert judgement itself did not mention ILO Convention 94 at all, as Germany as the defendant country from which the case originated has not ratified it. The content of the Ruffert judgement, however, is in marked contradiction to the ambition of ILO Convention 94 (Ahlberg and Bruun 2012; Bruun et al. 2010). This comes out very clearly, for example, in the refusal of the EFTA Surveillance Authority to accept Norway's attempt to defend itself by emphasising its ratification of Convention 94.

The future scope for using pay clause in public procurement urgently requires for there to be clarification to establish that ILO Convention 94 is not inconsistent with EU law. This was recognised by the European Parliament already in 2008 when – with regard to Ruffert case – it *“regrets that even judicial rulings fail sufficiently to take into consideration ILO convention 94.”* Moreover, the European Parliament has expressed its worry that the Convention *“might be in conflict with the application of the Posted Workers Directive”* and, therefore, *“calls on the Commission to clarify this situation as a matter of urgency and to continue to promote the ratification of this Convention in order to enhance further the development of social clauses in public procurement regulations”* (European Parliament 2008: 56). More recently, in its resolution on *“modernisation of public procurement”*, adopted in 2011, the European Parliament has confirmed its viewpoint and – with regard to the new European Procurement Directive – *“calls for an explicit statement in the directives that they do not prevent any country from complying with ILO Convention C94.”* Additionally, it *“calls on the Commission to encourage all Member States to comply with that Convention”* (European Parliament 2011). A similar statement has also been adopted by the European Economic and Social Committee (2011).

The need for a political clarification that Convention 94 is not inconsistent with EU law has also been expressed by various national political actors. The Swedish government, for example, asked in its comment to the EU Commission's Green Paper on Public Procurement for a legal clarification that EU member states still have the opportunity to ratify ILO Convention 94 (Regeringskansliet Socialdepartementet 2011). The background for this has been various motions put before the Swedish Parliament which demand the ratification of ILO Convention 94 (Vinterskog 2011).

A strong statement in favour of ILO Convention 94 has also been made by the EFTA countries within the EEA (Iceland, Liechtenstein, and Norway) which refer explicitly to the European Parliament and support its demand to include the convention in the new European Procurement Directive. Moreover the EFTA states have emphasised that *“it should be made clear that contracting authorities/entities have the possibility to set as a condition that the workers performing under the contract are subject to employment and labour conditions that are not inferior to those issuing from collective agreements or conditions that are normal for the place and profession. This should be the case regardless of whether the Member State has a statutory minimum wage or has made collective agreements generally applicable. This would make it possible for all Member States to fulfil the obligations stemming from ILO 94, without having to make substantial changes to their systems of wage formation”* (Standing Committee of the EFTA States 2012, my emphasis).

The necessity to ensure the compatibility between ILO Convention 94 and EU law has also been demanded by the European trade unions, which have additionally called for a more binding regulation to ensure *“that all the parties in a public procurement procedure are bound by national labour law and locally applicable collective agreements”* (ETUC 2012, see also EPSU 2011). One way in which this could be achieved has been developed in an expert opinion prepared for the German United Services Union (ver.di) which suggested introducing

the text of Article 2 of ILO Convention 94 into European procurement law (von Bechtolsheim and Charlier 2012: 94). The position of the European trade unions has been further supported by several national trade union organisations which, for example in Germany, Sweden or the UK, have called on their national governments to ratify ILO Convention 94 (DGB 2012, LO 2012, TUC 2008).

Apart from the new European procurement directive, which is currently under discussion, the debate on the enforcement of the Posted Workers Directive (Directive 96/71/EC) offers another opportunity to ensure the conformity of ILO Convention 94 with EU law.<sup>61</sup> A recent study on the enforcement of this directive, carried out on behalf of the European Commission, recommended removing “legal uncertainty with regard to the scope for Member States to include social clauses in public procurement contracts.” A clarification within the Posted Workers Directive seems to be appropriate “*not only in the light of the Ruffert judgment, but also taking into account the Public Procurement Directives which explicitly leave the Member States free to decide on how to integrate social policy requirements into public procurement procedures and ILO Convention No. 94*” (van Hoek and Houwerzijl 2011: 180).

Although there is a strong need for several European countries to confirm the conformity of ILO Convention 94 with EU law in order to ensure that pay clauses can be applied comprehensively in public procurement, the European Commission has failed to address this issue within both the draft directive on public procurement (European Commission 2011) and the draft directive on the enforcement of Directive 96/71/EC (European Commission 2012).

It seemed to be that there have been at least some discussions on the ILO Convention 94 within the Council of the European Union. In its revised draft for a European procurement directive (version from 14 November 2012), for the first time, the council has made even an explicit reference to ILO Convention 94 (Council of the European Union 2012a). However, this reference has again disappeared in the Council’s latest draft (version from 30 November 2012) (Council of the European Union 2012b).

According to the Council of the European Union it should now “*be possible to include clauses ensuring compliance with collective agreements in compliance with Union law in public contracts*” (ibid, No. 41a). The phrase “compliance with Union law”, however, already indicates some important limitations of that provision. The latter become even clearer when the Council further notes “*that award criteria or contract performance conditions concerning social aspects of the production process ... should be applied in accordance with Directive 96/71/EC ... as interpreted by the European Court of Justice and should not be chosen or applied in a way that discriminates directly or indirectly against economic operators from other Member States or from third countries*” (ibid., author’s emphasis). With the explicit reference to the EJC the Council has de facto limit the use of pay clauses in public procurement to the narrow scope determined by the Ruffert judgement while rejecting the much broader scope indicated by the ILO Convention 94. This is, however, quite the opposite of what has been demanded by both the European Parliament and a range of political organisations at European and at national level. Moreover, this stance completely ignores the needs that have arisen from the current use of pay clauses in procurement in several European states.

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<sup>61</sup> Interestingly, in the first draft for a posted workers directive from 1991 the European Commission made an explicit reference to ILO C94 (European Commission 1991). Later on, however, this reference disappeared (for a discussion of the history of the Posted Workers Directive see: Evju and Novitz 2012).

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