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Written contribution by

OECD

The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.

COMPETITION COMMITTEE



Competition and Procurement

Key Findings

With respect to the UNCTAD IGE 2012 Roundtable on “Competition and Public Procurement”, the OECD would like to draw attention to the attached paper which presents key findings from the extensive discussions on competition and procurement by the OECD Competition Committee, Working Party 3 and the Global Forum on Competition in recent years. The document is also available online at the OECD’s website at www.oecd.org/competition

Competition and Procurement

KEY FINDINGS

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FOREWORD

The OECD Competition Committee, Working Party 3 and the Global Forum on Competition have discussed competition and procurement extensively in recent years. Among the participants in these discussions were senior competition officials, leading academics and representatives of the business community.

This publication presents the key findings resulting from the roundtable discussions held on Collusion and Corruption in Public Procurement (2010); Public Procurement: The Role of Competition Authorities in Promoting Competition (2007); Competition in Bidding Markets (2006); and Competition Policy and Procurement Markets (1998). The key findings from each roundtable have now been organised into a cohesive narrative, putting the Competition Committee's work in this area into perspective and making it useful to a wider audience.

The full set of materials from each roundtable, including background papers, national contributions and detailed summaries of the discussions, can be found at www.oecd.org/competition/roundtables.

KEY FINDINGS

By the Secretariat

Introduction

- (1) *Public procurement is the process of purchasing goods or services by the public sector, the aim of which is to secure the best value for public money. Public procurement involves the expenditure of large sums of public money, and given its magnitude, can impact on the structure and functioning of competition in a market more generally. It is critical, therefore, to protect the integrity of the public procurement process, so as to maximise the resulting benefits for society and to protect competitive markets.*

Procurement is the process of purchasing goods or services. The primary objective of an effective procurement policy is the promotion of efficiency, i.e. the selection of the supplier with the lowest price or, more generally, the achievement of the best “value for money”. Both public and private organizations often rely upon a competitive bidding process to achieve better value for money in their procurement activities. Low prices and/or better products are desirable because they result in resources either being saved or freed up for use on other goods and services. However, the competitive process can achieve lower prices or better quality and innovation only when companies genuinely compete, that is, they set their terms and conditions honestly and independently.

Public procurement comprises government purchasing of goods and services required for State activities which accordingly aims to secure the best value for public money. Public procurement generally accounts for a large share of public expenditure in a domestic economy: in OECD countries, public procurement accounts for

approximately 15% of GDP. In many non-OECD countries that figure is even higher. Due to the magnitude of the spending involved, public procurement can have a market impact beyond the mere quantities of goods and services purchased: through its procurement policies, the public sector can affect the structure of the market and the incentives of firms to compete more or less fiercely in the long run. Procurement policy therefore may be used to shape the longer term effects on competition in an industry or sector.

- (2) *While collusive or corrupt conduct may occur during any procurement procedure, whether public or private, certain aspects of the public procurement process render it particularly vulnerable to distortion via anticompetitive conduct. On the one hand, the sheer volume of high value public procurement projects – many of which relate to sectors that have, historically, been prone to anticompetitive conduct – creates attractive opportunities for corruption and collusion. On the other hand, public entities are typically more constrained as to their range of permissible actions than private procurers, because of the highly regulated nature of public procurement, and therefore have limited strategic options available to address these threats.*

Collusion and corruption can arise in any procurement procedure, whether occurring in the public or private sectors. Yet, the distinctiveness of public procurement renders it particularly vulnerable to anticompetitive and corrupt practices, and magnifies the resultant harm. It is for this reason that the problems of collusion and corruption within the field of public procurement specifically have merited particular attention by the OECD Competition Committee in its work.

The competition concerns arising from public procurement are largely the same concerns that can arise in an “ordinary” market context: the reaching of collusive agreements between bidders during the tender process or across tenders. A key peculiarity of the public purchaser as compared to a private purchaser is that the government has limited strategic options. Whereas a private purchaser can choose his purchasing strategy flexibly, the public sector is subject to transparency requirements and generally is constrained by legislation and detailed administrative regulations and procedures on public

procurement. These rules are set as an attempt to avoid any abuse of discretion by the public sector. However, full transparency of the procurement process and its outcome can promote collusion. Disclosing information such as the identity of the bidders and the terms and conditions of each bid allows competitors to detect deviations from a collusive agreement, punish those firms and better coordinate future tenders. Moreover, regulatory requirements dictating particular procurement procedures can render the process excessively predictable, creating further opportunity for collusion. This lack of flexibility limits the opportunities for the public purchaser to react strategically when confronted with unlawful cooperation among potential bidders seeking to increase profits.

Other aspects of the public procurement process compound this particular vulnerability to anticompetitive and corrupt practices. Public procurement frequently involves large, high value projects, which present attractive opportunities for collusion and corruption. Certain sectors frequently subject to public procurement, including construction and medical goods and services, may be particularly prone to anticompetitive or corrupt practices. Finally, the sheer quantity of goods and services that are contracted by the State creates monitoring difficulties and increases the likelihood that the public procurement process may fall prey to collusion or corruption.

- (3) *Distortion of the procurement process via collusion or corruption typically has a particularly detrimental effect in the public sector context. The resulting failure to achieve best value for money has a negative impact on the range and depth of services and infrastructure that a State can provide. Moreover, corruption and collusion in public procurement can diminish public confidence in the government and the market, ultimately inhibiting a State's economic development.*

That public procurement is particularly vulnerable to anticompetitive interference is a state of affairs that is made all the more problematic by the fact that the harm caused by corruption and collusion has an especially detrimental impact in the public sphere. Effective public procurement determines the quality of public infrastructure and services and it impacts on the range and depth of infrastructure and services that the State can provide to its citizens. Public procurement is an issue of key importance for a State's economic development: (i)

the goods and services involved typically affect a large section of the population; (ii) public procurement often involves physical infrastructure or public health, which support other forms of economic activity; (iii) it impacts on international competitiveness; (iv) it can impact on the investment climate; (v) distortion of public procurement typically has the heaviest detrimental impact on the most disadvantaged in society, who rely on public services and infrastructure to the greatest extent; and (vi) public procurement often concerns “public goods”, and so government failures cannot be addressed by private market mechanisms.

The effects of collusion and corruption in public procurement are therefore arguably more problematic than in private procurement. Moneys lost because of subversion of the public procurement process represent wastage of public funds. The resulting loss to public infrastructure and services, whether in quality or range, typically has the heaviest detrimental impact on the most disadvantaged in society, who rely on public provision to the greatest extent. Collusion in public procurement may diminish public confidence in the competitive process, and undermine the benefits of a competitive marketplace. Moreover, distortion of the public procurement process is detrimental for democracy and for sound public governance, and it inhibits investment and economic development. In this way, deficiencies in public procurement impact on the wider economy in a way that does not occur with private procurement.

**Generic pharmaceuticals in Mexico:
Improved procurement securing better value for money**

Between 2003 and 2006, procurement of generic pharmaceuticals by the Mexican social security agency, IMSS, was on the basis of fragmented and wholly domestic (that is, reserved to national firms) tendering procedures: there were, on average, nearly 100 auctions per product per year, with each consuming area (region or general hospital) holding its own tenders separately and, in some instances, several times a year for the same product. Many of these auctions included multiple provision rules and relatively high reference prices.

In 2007, however, IMSS revised its procurement strategy. It began opening tenders to international bidders, consolidating purchases into only one or several annual national contracts per product, including aggressively low maximum prices based on market research, and eliminating multiple provision. As a result, evidence of collusion among bidders declined greatly, and winning tender prices for generic pharmaceuticals decreased dramatically: 18 of the 20 most important products, representing 42% of purchases, registered an average price decrease of 20%.

Collusion and Corruption in Public Procurement

- (4) *Collusion between firms that are bidding in a public procurement allows them to avoid the pressures of competition, with the result that the public purchaser gets less for its money, or pays more for what it gets. Bid rigging is the typical mechanism of collusion in public contracts, which leads to the predetermination of the outcome of the procurement process by its participants rather than the competitive process. Strategies for implementation of a bid rigging cartel include cover bidding, bid allocation, bid suppression and market allocation.*

Collusion involves a horizontal relationship between bidders in a public procurement, who conspire to remove the element of competition from the process. In the normal course, independent bidders in a procurement process compete against each other to win the contract, and it is via this mechanism that best value for money for the purchaser is achieved. Anticompetitive collusion occurs when businesses, that would otherwise be expected to compete, form a cartel; they secretly conspire to raise prices or lower the quality of goods or services for purchasers who wish to acquire products or

services through the bidding process, with the result that the purchaser gets less for its money.

Bid rigging is the typical mechanism of collusion in public contracts: the bidders determine between themselves who should “win” the tender, and then arrange their bids in such a way as to ensure that the designated bidder is selected by the purportedly competitive process. Bid rigging is an illegal practice in all OECD member countries and can be investigated and sanctioned under the competition law and rules. In a number of OECD countries, bid rigging is also a criminal offence.

Although individuals and firms may agree to implement bid-rigging schemes in a variety of ways, they typically implement one or more of several common strategies. These strategies are not mutually exclusive and may be used in tandem by firms. Use of these strategies in turn may result in patterns that procurement officials can detect and which can then help uncover bid-rigging schemes. *Cover bidding* (also called complementary, courtesy, token, or symbolic bidding), occurs when firms agree to submit bids that involve at least one of the following: (i) a bid that is higher than the bid of the designated winner, (ii) a bid that is known to be too high to be accepted, or (iii) a bid that contains special terms that are known to be unacceptable to the purchaser. *Bid-suppression* schemes involve agreements among competitors in which one or more companies agree to refrain from bidding or to withdraw a previously submitted bid so that the designated winner’s bid will be accepted. In *bid-rotation* schemes, conspiring firms continue to bid, but they agree to take turns being the winning bidder. Alternatively or additionally, competitors may carve up the market – *market allocation* – and agree not to compete for certain customers or in certain geographic areas.

- (5) *Certain sector characteristics facilitate collusion (bid rigging) between firms, and therefore make it more likely to occur successfully. These include market conditions that allow firms to reach agreement on a common course of anticompetitive conduct, to monitor adherence (or cheating) by other firms to the agreement, and to punish firms that have deviated from the cartel.*

In order for firms to implement a successful collusive agreement, they must agree on a common course of action for implementing the

agreement, monitor whether other firms are abiding by the agreement, and establish a way to punish firms that cheat on the agreement. Although bid rigging can occur in any economic sector, there are some sectors in which it is more likely to occur due to particular features of the industry or of the product involved. Such characteristics tend to support the efforts of firms to rig bids.

Sector characteristics that are likely to facilitate collusion include: (i) a small number of companies operating in the market; (ii) little or no new entry into the market; (iii) certain market conditions, insofar as while a constant, predictable flow of demand from the public sector tends to increase the risk of collusion, at the same time during periods of economic upheaval or uncertainty, incentives for competitors to rig bids increase as they seek to replace lost business with collusive gains; (iv) the presence of industry or trade associations, which although in many instances perform legitimate and precompetitive functions, can in other circumstances be subverted to illegal, anticompetitive purposes; (v) repetitive bidding by firms; (vi) identical or simple products or services; (vii) few if any substitute products or services available; and (viii) little or no technological change in the sector.

- (6) *Public procurement may furthermore be subverted by corruption of the public official(s) with responsibility for organisation of the procedure and selection of the winning bid. The key facilitating factor for corruption in public procurement is a lack of transparency of the process.*

Corruption occurs where public officials use public powers for personal gain, for example, by accepting a bribe in exchange for granting a tender. While usually occurring during the procurement process, instances of post-award corruption can also arise. Corruption constitutes a vertical relationship between the public official concerned, acting as buyer in the transaction, and one or more bidders, acting as sellers in this instance.

As with bid rigging, corruption of a public procurement procedure means that the purchaser fails to achieve the best value for money, because the winning firm has been protected from the full rigours of competition by its interference in the competitive process. A lack of transparency within the procurement process is considered to be the key facilitating factor for corruption of procurement officials – with

the result that, historically, public procurement rules have put a strong emphasis on transparency of process. Corruption is generally prohibited by the national criminal justice rules, legislation on ethics in public office or by the specific public procurement regulations.

- (7) *Collusion and corruption are distinct problems within public procurement, yet they may frequently occur in tandem, and have mutually reinforcing effect. Thus, they are best viewed as concomitant threats to the integrity of public procurement with a need to accommodate avoidance of both within any strategy to protect the procurement process.*

Both collusion and corruption prevention are necessary aspects of any overall strategy aimed at protecting the integrity of the public procurement process. While collusion and corruption constitute distinct problems in the area of public procurement, ultimately these discrete offences have the same effect: a public contract is awarded on a basis other than fair competition and the merit of the successful contractor, so that maximum value for public money is not achieved.

There is empirical evidence that corruption and collusion can occur in tandem, and certainly, these offences have a mutually reinforcing effect. Where corruption occurs in a public contract, collusion between bidders – for example, in the form of compensatory payments or the granting of subcontracts – may be necessary to ensure that losing bidders do not expose the illegal conduct to the public authorities. Equally, economic rents derived from collusion may foster corruption, while collusion is also facilitated by having an “insider” in the public agency that provides the bidders with information necessary to rig bids in a plausible manner and may even operate as a cartel enforcement mechanism. Moreover, as these problems are mutually reinforcing, reducing the likelihood of one offence will also decrease the risk of the other.

Given that tackling collusion and corruption are not mutually exclusive goals, there is a need to accommodate both in order to better protect the public procurement process. Collusion and corruption are typically pursued under separate but largely compatible legal frameworks. Nonetheless, approaches to the prevention of collusion and corruption within public procurement diverge significantly with respect to the role of transparency, and the resulting tensions between

these sometimes competing positions may necessitate trade-offs to achieve both effectively.

Protecting the Integrity of the Procurement Process: Design of the Procurement Procedure

- (8) *Preventing the distortion of a public procurement procedure through collusive or corrupt behaviour begins at an early stage in the process, with the selection of the bidding model, and continues through to the post-award phase. Procurement tenders, by their nature, are more susceptible to anticompetitive practices than ordinary posted-price markets. Nonetheless, by careful tender design, procurement officials can minimise the risks of collusion and corruption in the process. The OECD’s Guidelines for Fighting Bid Rigging in Public Procurement provide procurement officials with a comprehensive framework for procurement design, from the initial selection of the procurement model, through the running of the procurement procedure, to detecting anticompetitive conduct during the tender process.*

Because their formal rules reduce “noise” and make communication among rivals easier, public procurement via tender can promote collusion, compared with ordinary posted-price markets. Choices about procurement design can therefore affect how susceptible the tender process is to collusion or corruption, or how widespread is participation in the tender. Designing procurement tenders with competition in mind – in particular, careful consideration of the various features and their impact on the likelihood of collusion – allows the creation of an environment where the bidders’ ability and incentives to reach collusive arrangements are significantly reduced, if not eliminated. Two fundamental prescriptions for effective procurement design follow from the theoretical literature: induce bidders to truthfully reveal their valuations by making what they pay not depend entirely on what they bid, and maximize the information available to each participant before he bids.

To the extent permitted by the regulatory framework, public procurement officials can behave strategically, choosing tender formats or practices that favour competition. It is important, therefore, that the legislative and regulatory framework on public procurement be designed to allow sufficient flexibility on the purchasing side. As a result, however, the design of a tender can become the object of

lobbying pressure, and excessive discretion granted to procurement officials can create opportunities for corruption in the procurement process. The OECD's Guidelines for Fighting Bid Rigging in Public Procurement provide public officials with a comprehensive overview of procurement design issues relating to collusion, including a checklist for designing the procurement process to reduce the risks of bid rigging.

- (9) *Selection of the tender procedure is the first pivotal first step in the fight against collusion and corruption in public procurement. A key policy question is whether to utilise an open tender procedure, which is more susceptible to collusion insofar as it creates opportunities for communication between bidders, or a sealed-bid procedure, which is more susceptible to corruption insofar as there is a lack of transparency in the process. The most appropriate procurement procedure depends, in large part, on market conditions*

There are numerous different forms of tenders that might be adopted in the procurement context, but not all bidding models are equal from the point of view of competition. Where there are enough firms in the procurement market to sustain reasonable competition, efficient procurement outcomes can usually be achieved through a simple tender process (either sealed or open bid). When there are not enough firms to sustain competition, more sophisticated arrangements may be necessary to achieve an efficient outcome. The choice of the most suitable bidding model given the circumstances of the procurement is therefore the starting point of any attempt to prevent collusion in public procurement.

Prior to selecting the tender process, procurements officials should first of all inform themselves about market conditions to the greatest extent possible. Collecting information on the range of products and/or services available in the market that would suit public requirements as well as information on the potential suppliers of these products is the best way for procurement officials to design the procurement process to achieve the best "value for money". In-house expertise should be developed as early as possible. Procurement officials, as well as competition authorities, should be particularly alert to the presence of those sector characteristics that indicate heightened risk of a collusive outcome in a procurement market. These factors may facilitate the

formation of a collusive outcome, although not all of these factors must be present for collusion to be likely.

When it comes to choice of the procurement process, open tenders are potentially more susceptible to collusion than sealed-bid tenders insofar as open tenders create opportunities for communication between bidders during the tender process and therefore make it easier for them to reach a collusive understanding. Sealed-bid tenders make the selection process more uncertain, so that deviation from coordination is harder to detect and cannot be punished immediately, thus inhibiting anticompetitive collusion. However, the resulting lack of transparency in the process makes corruption on the part of public officials more difficult to prevent or detect. Conversely, disclosing the identities of losing bidders helps bidders monitor possible collusion but makes it easier to identify possible corruption between bid-takers and bidders.

- (10) *The efficiency of the procurement process not only depends upon the bidding model adopted but also on how the tender is designed and carried out. The design of the precise features of the competitive bidding process can also have a strong influence on the efficiency of the outcome.*

Beyond the initial selection of the bidding model, the efficiency of the procurement process also depends upon how the tender is designed and carried out. Procurement procedures may even, inadvertently, make coordination easier. While procurement design is not “one size fits all”, the risk of collusion can be reduced when the procurement agency ensures that the procurement activity is designed and carried out to achieve three main objectives: (i) reducing barriers to entry and increasing bidders’ participation; (ii) reducing transparency and the flows of competitively sensitive information; and (iii) reducing the frequency of procurement opportunities.

Just as in non-bidding situation, more entry improves effective competition: where a sufficient number of credible bidders are able to respond to the invitation to tender and have an incentive to compete for the contract. The tender process should therefore be designed to maximise the potential participation of genuinely competing bidders. Participation in the tender can be facilitated if procurement officials reduce the costs of bidding, establish participation requirements that

do not unreasonably limit firm involvement, allow firms from other regions or countries to participate, or devise ways of incentivising smaller firms to participate even if they cannot bid for the entire contract. Entry could be subsidized, for example, by paying for proposals in an architectural competition. Or entry can be promoted by providing bidding credits or low-cost financing, or making resale easier. The cost of bidding could be reduced by, for example, providing centralised information about future bidding opportunities.

It is important to design the tender process in a manner which reduces communication among bidders, and so procurement officials should be aware of the various factors that can facilitate collusion. Tender requirements should be defined clearly, but in a manner that avoids predictability. The drafting of the specifications and the terms of reference (TOR) is a stage of the public procurement cycle which is vulnerable to bias, fraud and corruption. Specifications/TOR should, as a general rule, be clear, comprehensive, non-discriminatory, and focus on functional performance, namely on what is to be achieved rather than how it is to be done. On the other hand, clarity should not be confused with predictability. More predictable procurement schedules and unchanging quantities sold or bought can facilitate collusion. By contrast, higher value and less frequent procurement opportunities increase the bidders' incentives to compete. Collusion is furthermore made more difficult where there is no advance notice of tender procedures.

The selection criteria for the evaluation and awarding of the tender affect the intensity and effectiveness of competition in the tender process, impacting not merely on the project at hand but also on the maintaining of a pool of potential credible bidders with a continuing interest in bidding on future projects. Qualitative selection and awarding criteria should therefore be chosen in such a way that credible bidders, including small and medium enterprises, are not deterred unnecessarily. Monitoring adherence to coordination can be made more difficult by having multidimensional criteria, thus making it harder to predict exactly how the winner will be chosen. However, decreasing transparency can facilitate corruption or collusion between the bid taker and some bidders, and so the advisability of decreasing transparency depends on the setting.

Vancouver Winter Olympics – “No Collusion” Clauses

Following discussions with the Canadian Competition Bureau, the Vancouver Organising Committee (“VANOC”) for the 2010 Vancouver Winter Olympics decided to include a “no collusion requirement”, similar to a Certificate of Independent Bid Determination (CIBD), in its tender documents for contractors. The “no collusion requirement” stipulated that bidders were required to arrive at their bids independently and that communications with other bidders must be disclosed. VANOC also reserved the right to request a formal CIBD, in addition to the “no collusion requirement”, if it had reason to suspect that bids were not arrived at independently.

- (11) *Strategies to address collusion and corruption in public procurement must address a fundamental tension: while transparency of the process is considered to be indispensable to corruption prevention, excessive and unnecessary transparency in fact facilitates the formation and successful implementation of bid rigging cartels. The extent to which transparency is a desirable aspect of a procurement process therefore depends on the circumstances, and may require trade-offs between best practice approaches to avoidance of collusion and corruption.*

At an operational level, best practice approaches to avoidance of collusion and of corruption in public procurement can differ. While a pattern of regular small tenders is seen to facilitate collusion, for example, large lumpy tenders can foster corruption. A significant difference is the role and importance of transparency in the procurement process. The principle of transparency – which relates to the availability of information on contract opportunities, the rules of the process, decision-making and verification and enforcement – is of critical importance in preventing corruption. In certain instances, however, transparency is inconsistent with the need to ensure maximum competition within the procurement process. Transparency requirements can result in unnecessary dissemination of commercially sensitive information, allowing firms to align their bidding strategies and thereby facilitating the formation and monitoring of bid rigging cartels. Transparency may also make a procurement procedure predictable, which can further assist collusion.

This may lead to tensions between the sometimes competing approaches to prevention of collusion and corruption within public procurement and require trade-offs in terms of how to achieve these objectives. While transparency of the process is indispensable to limit corruption, excessive or unnecessary transparency should be avoided in order not to foster collusion. There is some uncertainty, however, as to what information can facilitate collusion. Sound procurement design can go a long way towards achieving effective procurement and mitigating this trade-off. For example, procurement rules might require only information on winning bids to be released and not require bidder identities to be disclosed. Bidding procedures should not provide participants with sensitive information regarding the actions of others tenders, but, conversely, should allow for review of decisions of public officials by independent public agencies. Insofar as there is no single rule about the design of a procurement procedure, each one should be designed to fit the specific circumstances.

- (12) *Even the most robustly designed procurement procedure may not fully eliminate the risks of distortion via collusion or corruption. It is additionally necessary, therefore, to monitor and review the bidding process and performance of the contract constantly, in order to identify and penalise instances of anticompetitive conduct in the procurement procedure. Procurement officials should be aware of the telltale signs of bid rigging and/or corruption, which may indicate that the procurement procedure has been compromised. A number of more formal review tools also exist, including data analysis and auditing of the procurement procedure.*

Procurement design, even when in accordance with best practice standards, cannot alone eliminate the risks of collusion or corruption within the procurement procedure. In addition, it is important to monitor and review the conduct of the process itself, so as to identify instances of possible anticompetitive conduct. Given the covert nature of such practices, this is no easy task for procurement officials or competition authorities. Corruption is facilitated, and thus most likely to occur, where there is a lack of openness or transparency in the procurement process. Bid-rigging agreements are typically negotiated in secret, making them similarly difficult to detect. In industries where anticompetitive conduct is common, however, suppliers and purchasers may be aware of longstanding corrupt or collusive practices. In most industries, moreover, certain telltale signs may

indicate that the competitive process is not functioning normally and suggest the possibility of bid rigging or corruption.

Indicators of a bid-rigging conspiracy may be found in the various documents submitted by bidding companies, and so documentation should be compared carefully to identify evidence that suggests that the bids were prepared by the same person or were prepared jointly. Bid prices also can be used to help uncover collusion. For example, a pattern of price increases that cannot be explained by cost increases may suggest that companies are coordinating their efforts. When losing bids are much higher than the winner's bid, conspirators may be using a cover bidding scheme. A common practice in cover pricing schemes is for the provider of the cover price to add 10% or more to the lowest bid. Bid prices that are higher than the engineering cost estimates or higher than prior bids for similar tenders may similarly indicate collusion. In addition, subcontracting and undisclosed joint venture practices can raise suspicions. When working with vendors, procurement officials should watch carefully for suspicious statements that suggest collusion, and be alert to suspicious behaviour at all times, for example references to meetings or events at which suppliers may have an opportunity to discuss prices, or behaviour that suggests a company is taking certain actions that only benefit other firms.

More formal mechanisms by which to protect the integrity of the procurement process include: (i) data analysis tools, such as comparisons of public databases to identify indicators of anticompetitive or corrupt activity, and (ii) auditing of public procurement procedure, whether conducted internally by a separate wing of the relevant public agency, or externally by an independent State body with specific powers of audit. Quantitative analyses of bid data can help procurement agencies (with the support of competition authorities) to identify up-front those sectors where infringements of the competition rules are more likely. In order to do so, it is crucial to examine the bids that have been submitted in the past to determine if the patterns are consistent with a fully competitive process. These analyses would allow procurement and competition authorities to maximise their efforts, optimising tender design in those industry sectors which are at risk and allocating law enforcement resources to the detection of collusion in those sensitive sectors. Retaining data from prior tenders may also help in any later bid-rigging prosecutions.

Where this is the case, knowing the data has been retained may have a deterrent effect, and thus help to discourage bid-rigging.

While bid rigging indicators identify suspicious bid and pricing patterns as well as suspicious statements and behaviours, they should not, without more, be taken as proof that firms are engaging in bid rigging. For example, a firm may have not bid on a particular tender offer because it was too busy to handle the work. High bids may simply reflect a different assessment of the cost of a project. Nevertheless, when suspicious patterns in bids and pricing are detected or when procurement agents hear odd statements or observe peculiar behaviour, further investigation of bid rigging is required. A regular pattern of suspicious behaviour over a period of time is often a better indicator of possible bid rigging than evidence from a single bid, and so all information should be recorded so that a pattern of behaviour can be established over time. A number of countries, as well as the OECD, have developed check lists to help procurement agencies to spot instances of possible collusion. While these check lists contain indications of potentially collusive conduct, they are not, in themselves, conclusive.

Korea's Bid Rigging Indicator Analysis System

In September 2006, the Korea Fair Trade Commission (KFTC) began using a bid rigging indicator analysis system, to monitor evidence of bid-rigging in public procurement. This system represents an evolution of the KFTC's earlier practice, begun in 1997, of analysing manually bidding data from public procurement procedures. The bid rigging indicator analysis system automatically and statistically analyses bid-rigging indicators based on data regarding procurement processes run by public institutions. Since 1 January 2009, under the amended Monopoly Regulation and Fair Trade Act, all public bodies have been legally required to provide this bid-related information to the KFTC. The data is delivered online to the KFTC, and the analysis system then calculates the probability of bid rigging by giving weightings to various indicators like bid-winning probability, the number of bidders, bid prices, competition methods, the number of unsuccessful bids and hikes in reserve prices, and transition into private contracts.

The analysis system helps the KFTC to identify bid-rigging activity by enabling it to monitor public sector tenders chronologically, and to conduct on-site investigations where there is significant evidence of bid rigging. The system is also considered to have a deterrent effect, insofar as it signals the constant oversight by the KFTC of the public procurement process.

Protecting the Integrity of the Procurement Process: Actors and Actions

- (13) *Procurement officials are the frontline defenders of the integrity of the public procurement process against the negative effects of collusion and corruption. In order to perform this role effectively, public officials require (i) education about bid rigging and how to identify it; (ii) the establishment of clear processes to be followed where suspected bid rigging has been identified; and (iii) mechanisms for cooperation with the competition authority. In order to avoid corruption, procurement officials should be made aware of the consequences for officials who themselves engage in corrupt practices.*

Equipping procurement officials – those at the frontline of the procurement process – with the skills and tools to identify, avoid and seek redress for collusion and corruption in public procurement is an indispensable element in the fight to protect the process from anticompetitive conduct. First and foremost, professional training of public officials at all levels of government is important to strengthen procurement agencies' awareness of competition issues in public procurement. Public procurement officials need to be made aware of the possibility and the harm caused by bid rigging; to be able to identify the signs of bid rigging; as well as to have a working understanding of the law on bid rigging in their jurisdiction. From the perspective of corruption prevention, education also serves as a warning of the likely consequences for officials who might otherwise be tempted to themselves engage in corrupt practices.

On the operational side, public agencies should establish internal procedures that encourage or require officials to report suspicious statements or behaviour to the competition authorities as well as to the procurement agency's internal audit group and comptroller. Agencies should, moreover, consider developing incentives to encourage officials to do so. Where bid rigging is suspected, there should be in a place a clearly defined procedure for public officials to follow, which will allow bid rigging to be uncovered and stopped. The OECD's Guidelines for Fighting Bid Rigging in Public Procurement advises procurement officials who suspect bid rigging to refrain from discussing their concerns with suspected participants; keep all documentation, as well as a detailed record of all suspicious behaviour and statements including dates, who was involved, and who else was present and what precisely occurred or was said; contact the relevant competition authority in the jurisdiction; and after consulting with the

public agency's internal legal staff, consider whether it is appropriate to proceed with the tender offer. Efforts to fight bid rigging more effectively can be supported by collecting historical information on bidding behaviour, by constantly monitoring bidding activities, and by performing analyses on bid data, in order to assist procurement agencies in identifying problematic situations.

Establishing a collaborative relationship between procurement officials and the competition authority is a worthwhile step. This might comprise, for example, setting up a mechanism for communication, as well as listing information to be provided when procurement officials contact competition authorities. Moreover, where competition authorities get involved in the procurement process at an early stage, they can help procurement agencies to identify signs of anticompetitive behaviour early on, thus increasing the effectiveness of competition law enforcement.

Procurement advocacy & outreach in Australia

Australia's national competition authority, the Australian Competition and Consumer Commission (ACCC), has developed an extensive education and advocacy programme for officials, at all levels of government, who are involved in public procurement. Efforts to promote awareness of competition issues among procurement officials have included:

- Development of education material for procurement officials, in particular a multi-media CD-ROM, which was provided to public sector procurement agencies, as well as private companies involved in procurement. The CD-ROM was interactive and allowed procurement officials to access a variety of different levels of information, including information on: how to identify cartel activity; the process for reporting suspected cartel or bid-rigging behaviour; the statutory provisions; and what a person should do if a cartel operation is suspected. The CD-ROM also included a checklist for procurement officials to determine whether or not there is any suspected cartel activity;
- Presentations by ACCC staff, at all levels, to procurement officials from Commonwealth, state and local governments; and

Advocacy efforts directed toward high level government officials, aimed at seeking support for the ACCC's education and compliance programme at the top levels within central and regional governments, and also in order to request all governments to examine their procurement frameworks and introduce measures requiring officials to take into account competition laws when designing their procurement policies and guidelines.

- (14) *Competition authorities play a variety of roles in support of public procurement processes. These range from education and technical assistance for public agencies running a procurement process, as well as advocacy efforts directed towards business and the wider community, through to competition law enforcement where bid rigging has been identified. Additionally, merger control presents an opportunity to shape competition in procurement markets more generally.*

The optimal strategy to tackle both collusion and corruption in public procurement appears to require a three-pronged approach: development of best practice rules for public procurement; extensive advocacy efforts; and vigorous enforcement action taken against any instances of corruption and/or collusion that are uncovered. The competition authority's role within the public procurement process therefore typically begins long before any discrete violation of the competition rules has been identified. Given the importance of educating public procurement officials about the risks of bid rigging and how to avoid it, many competition authorities are involved in advocacy efforts to increase awareness of the risks of bid rigging in procurement tenders, directed at public agencies. For example, some authorities have regular bid rigging educational programs for procurement agencies; others organise ad hoc seminars and training courses. This education effort includes documentation describing collusion and bid rigging, the forms it can take and how to detect it, as well as best practices for procurement design. The theory is that, through early intervention and smart procurement design, the necessity for *ex post* competition law intervention will be reduced. Similarly, advocacy efforts directed towards business, the media and the wider community can generate public support for enforcement efforts and promote a shift towards a "culture of compliance" by business. Education of public officials, business and civil society is perceived to be especially relevant in economies where rules against collusion and/or corruption in public tendering are relatively new or under-enforced.

Where bid rigging has already occurred, vigorous enforcement of the competition rules (either the general rules prohibiting cartels, or specific prohibitions prohibiting bid rigging) is needed, in order to punish the immediate violation and to deter future competition law violations.

Merger control is a further mechanism by which competition authorities can have an impact on procurement markets. When it comes to mergers in markets related to public procurement, the analysis is not significantly changed by the existence of a bidding process. Most of the instruments competition authorities use in merger analysis are robust and seem to provide good results in such markets, provided that account is taken of the specifics of the bidding process, in particular the fact that *ex post* market shares do not necessarily reflect the intensity of competition in the market during the bidding process. Quantitative techniques, such as frequency analysis or reduced form estimation, can be applied to data that come out of the bidding processes to identify competitive constraints.

The United Kingdom’s Construction Cartel: Case Management & Prioritisation

In 2009, the national competition authority in the United Kingdom, the Office of Fair Trading (OFT), issued an infringement decision imposing fines on 103 companies for involvement in a bid rigging cartel in the construction industry in England. The cartel involved cover pricing – whereby bidders colluded with competitors during a tender process to obtain prices that were intended to be too high to win the contract, thereby also inflating the “winning” tender price – and associated compensation payments – whereby the successful bidders paid agreed sums of money to the unsuccessful bidders. The infringements affected both public and private sector building projects across England worth in excess of £200 million, including building projects for schools, universities and hospitals.

One of the more challenging aspects of the case was the sheer amount of evidence uncovered, which implicated many more companies on thousands of tender processes. The OFT was forced to prioritise and focus its investigation to a more limited number of infringements by using objective prioritisation criteria, with a view to reaching a decision comparatively swiftly, while still ensuring that the scale and scope of the investigation reflected the endemic nature of the practices in question so as to maximise the deterrent effect of its investigation. In order to do so, the OFT narrowed the scope of the case by firstly categorising the initial evidence according to “evidential weight” in order to focus on those parties where evidence of bid rigging was greatest and strongest. Secondly, the OFT proceeded to investigate only those companies where there were reasonable grounds to suspect their involvement in bid rigging on at least five tenders. The eventual defendants in the case represented a broad spread of companies, both in terms of firm size and location. The OFT also made a decision to pursue both companies that had and companies that had not received leniency to ensure that companies are not deterred from coming forward as leniency applicants (with 70 companies that had not applied for leniency as well as the 33 that had applied).

- (15) *Cooperation between the various national enforcement agencies with jurisdiction over collusion and corruption in public procurement is paramount, in order to achieve a coherent overall strategy and ensure its full implementation, and additionally, to facilitate efficient prosecution of these offences.*

Incidents of collusion and corruption are typically investigated and sanctioned by separate national agencies: collusion generally comes within the remit of the competition authority, whereas corruption is pursued by public prosecutors or specialised anti-corruption agencies. Due to the mutually reinforcing nature of collusion and corruption plus the likelihood that such offences occur in tandem, however, the most effective approach requires cooperation between the various enforcement agencies, whether by means of a formal memorandum of understanding, notification requirements or other mechanisms.

The benefits to a coordinated approach are considerable. Evidence of collusion may come to light during a corruption investigation, and vice versa; having in place a knowledge-sharing policy ensures that this information is brought to the attention of the appropriate enforcement body. Evidence-sharing, where compatible with national evidentiary rules, also assists those enforcement agencies (typically, competition authorities) that have more limited evidence-gathering powers than the public prosecutor or other criminal justice agencies. The introduction of a formal cooperation policy can improve knowledge of misconduct in public procurement amongst enforcement agencies more generally. Cooperation between enforcers can go some way towards addressing the deleterious effects of cumulative attacks on public procurement through collusion and corruption. In certain jurisdictions, a single agency may have both collusion and corruption remits, thus internalising this cooperation. While a combined approach is not a necessary requirement of an effective strategy, whatever the structure of the cooperation mechanism utilised, it should ensure: (i) comprehensive coverage of all forms of malfeasance in public procurement, and (ii) efficient prosecution of any such offences that arise in practice.

- (15) *Sanctions for collusion and/or corruption in public procurement range from fines and imprisonment to more specialised penalties like debarment from participation in future public procurement procedures. A key factor to achieving deterrence is to ensure a*

credible prospect of detection and prosecution, coupled with a sufficiently severe penalty. However, generating a “culture of compliance” should be a key objective for enforcement agencies.

In fighting collusion and corruption in public procurement, there must be a credible threat of discovery and prosecution, coupled with strong sanctions upon conviction. Typical penalties imposed for corruption are fines and imprisonment, and dismissal within the employment context. Bid rigging is generally subject to the same penalties as other hard core cartels, meaning fines and, depending on the jurisdiction, imprisonment. Many countries have competition leniency programmes in place which grant immunity or reduced fines to firms that reveal the existence of cartels and participate in their subsequent investigation. A number of sanctions that are specific to the public procurement context may also be available. In many jurisdictions, a conviction for participation in collusion and/or corruption in public procurement leads to debarment from future procurement procedures for a certain period of time. Particularly in smaller economies, however, this penalty may have the paradoxical effect of reducing the number of qualified bidders to an uncompetitive level. In those jurisdictions that utilise Certificates of Independent Bid Determination (CIBD) in public procurement, prosecution for false statements in certification can provide a straightforward means of penalising collusion in tendering.

For some businesses, fines imposed for anticompetitive or corrupt behaviour are considered simply a cost of doing business. In certain situations, the adverse publicity and the possibility of disqualification from holding certain company offices may represent a greater harm and therefore function as a greater deterrent for firms. More generally, while eliminating collusion and corruption entirely is a very challenging goal for any legal system, the development of a “culture of compliance” is an important step towards reducing such behaviours. As competing firms are often best placed to identify irregularities in public procurement, getting business on board in the fight against collusion and corruption can reap benefits in terms of both deterrence and detection.