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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

Contribution from Germany

-- Session V --

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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

-- Germany --

1. Introduction: The Process of Public Procurement and its Review

1. Public procurement is a factor of key significance in the German economy, as in many developed as well as developing economies around the world. The volume of public procurement (all contracting authorities combined) in Germany amounted to almost 270 billion Euros in 2007, which constituted a share of roughly 11% of GDP¹. For the entire EU, the volume of public procurement is estimated at 1.500 billion Euros, which is a share of 16% of GDP.²

2. A contracting authority in Germany that places a call for tenders has to respect certain basic principles in the process leading to its procurement decision, namely and most importantly, transparency, non-discrimination and competition. The aim is, ultimately, to make sure that the contract is awarded to the economically most advantageous offer so that public funds are used in the most efficient way. Furthermore, procurement law is seen as an instrument for integrating the European market and for controlling the exercise of any market power by the state. The relevant principles are specified, in more detail, in the law governing public procurement.³ Among these principles are a timely announcement of the procurement procedure and non-discrimination in drafting the tender documents and in assessing the bids.

3. The contracting authority placing a call for tenders is obliged to make sure that its tendering procedure is in accord with these principles, and it is this entity which is responsible for assessing the submitted bids. In this process, the contracting authority is called upon to be aware of and look out for any possible anti-competitive behaviour of bidders and to exclude any such bid.

4. To ensure that the key principles of public procurement law are respected it is of great importance that, at least for procurement projects exceeding certain thresholds⁴, procurement procedures and decisions can be reviewed by an independent instance in an effective manner. Companies participating in a public procurement procedure have a right to demand that the contracting authority respects the relevant provisions of public procurement law. Therefore, under certain conditions, companies can request a formal review of the procurement procedure and decision. Such a formal review of a procurement decision, under public procurement law, can only be triggered by a company that can demonstrate its interest in the relevant public contract. This implies, in particular, that a review cannot be initiated *ex*

¹ The total value of public procurement stated is based on statistics of the Federal Office of Statistics (*Bundesamt für Statistik*) and the budget plans of ministries.

² Cf. http://ec.europa.eu/youreurope/business/profitting-from-eu-market/benefiting-from-public-contracts/index_de.htm and http://ec.europa.eu/internal_market/publicprocurement/index_de.htm.

³ The relevant legal provisions are to be found in Sections 97 – 129 of the Act against Restraints of Competition (ARC) for procurement above certain thresholds. For procurement below those thresholds, budgetary law is applicable (for thresholds cf. below, FN 4).

⁴ The thresholds differ according to the kind of procurement, ranging from 4,845,000 Euros in construction down to 193.000 Euros for other products and services. The thresholds are regularly adjusted.

officio. The relevant authorities in Germany to conduct the review initiated by a bidding company are the public procurement tribunals of the federal administration, as far as procurement projects of a federal contracting authority are concerned, and the public procurement tribunals of the federal states (*Länder*), for procurement projects of those contracting authorities under the jurisdiction of the federal states or municipalities.

5. The public procurement tribunals are independent in their legal review of procurement decisions. Their decisions can be appealed, typically, to the relevant Higher Regional Court (*Oberlandesgericht*). A request for the review of a procurement decision can be put forward by any company that has an interest in the awarding of the contract and whose rights have been infringed because the rules of procurement have been violated and that has therefore suffered, or will suffer, damages.

2. General Issues of Collusion and Corruption in Public Procurement

6. Collusion among bidders is, arguably, a perennial problem in bidding processes, and particularly so in tenders placed by government entities. Strategies of collusion can be executed in a number of ways, among them cover bids (i.e., submission of a bid that is known and designed, by the colluding firms, to be too high) or non-bidding (i.e., refraining from bidding or withdrawing a submitted bid). These strategies serve to make sure that, among the colluding firms, a specific company is awarded the contract. The underlying rule for allocating contracts among the colluding firms can be, e.g., rotation (i.e., over time each one of the colluding firms is awarded a contract), allocating customers (i.e., a specific customer is “reserved” for a specific cartel member) or allocating geographic markets.

7. Although bidding processes seem to be, on the face of it, particularly competitive procedures, they have certain weaknesses from an anti-collusion point of view. The fact that, at a given point in time and with a given deadline, interested firms are asked to submit bids for products or services according to precise specifications conveys information to market participants that is typically not available in non-bidding procurement situations. Collusion among potential contracting firms is facilitated if certain market characteristics prevail, e.g., a small number of market participants, little or no market entry, repetitive bidding.⁵

8. In the case of governmental tendering procedures, certain additional factors may further heighten the risk of collusion. Among these factors, in Germany, is typically a ban on re-negotiating a bid that has been submitted in a formal bidding procedure (*Nachverhandlungsverbot*).⁶ This may have the effect of stabilising a cartel, since the colluding firms – once they have executed their scheme of collusion and their bids have been filed – do not have to be concerned that any subsequent bilateral negotiation of the contracting authority with bidders will endanger the result. In this sense, a legal provision that aims at protecting the bidding companies *vis-à-vis* the contracting authority may have the unintended side effect of facilitating anti-competitive behaviour. Other specifics of public procurement may further facilitate collusion, e.g., systems of co-financing by different public entities which may necessitate an early enquiry about the product, giving firms more lead time for colluding.⁷

9. The system for review of public procurement, as described above, is designed to make sure that the intricate rules for bidding processes are respected and that individual bidders who see their rights infringed can have effective legal recourse. However, detecting bid-rigging is not the primary concern of a specific review procedure. This is not what the system is designed to do. In this context it is important to

⁵ Cf. OECD, Guidelines for Fighting Bid Rigging in Public Procurement, pp. 2-3.

⁶ Cf. Section 24 VOB/A.

⁷ Cf. below.

stress that the review of procurement looks at an individual bidding process and considers whether the rules of public procurement have been adhered to. It is not intended to look at a sequence of tenders, which would be necessary to identify suspicious patterns of bidding that only become apparent over time. Furthermore, only a small percentage of procurement cases are potentially subject to formal review that can be initiated by one of the bidders. The value of most public tenders is below the relevant thresholds.⁸

10. Another problem area in public procurement, besides collusion among bidding firms is corruption, e.g., in the form that a person within the contracting authority calling for tenders engages in improper communication with one (or more) of the bidding companies and transmits crucial information that helps the companies design the winning bid. Collusion and corruption may go hand in hand in bid-rigging scenarios. However, the Bundeskartellamt has no statistics on the significance of these violations, and on the significance of both practices occurring jointly.

11. While the competition authorities in Germany are responsible for prosecuting undertakings engaging in bid-rigging according to the ARC, the persons involved in bid-rigging are, in principle, prosecuted by the public prosecutor's office according to criminal law. The competition authorities have no jurisdiction in corruption matters. This is the exclusive responsibility of the public prosecutor.

3. Cases of collusion in the practice of the Bundeskartellamt

12. The Bundeskartellamt has prosecuted cases of bid-rigging (collusion) – whether in procurement by public entities or non-public entities – in a wide range of sectors, and there is no strict focus on any sector or industry. Some of the sectors where bid-rigging has occurred are:

- Building materials (concrete);⁹
- High voltage power transformers;¹⁰
- Large steam generator vessels;¹¹
- Specialised vehicles;¹²
- Combat boots;¹³
- House-moving services for military personnel;¹⁴ and
- Waste collection services (*Grüner Punkt*).¹⁵

⁸ Cf. above, FN 4.

⁹ Cf. Bundeskartellamt, *Tätigkeitsbericht* (hereinafter: Activity Report) 2005/2006.

¹⁰ Ongoing procedure.

¹¹ Ongoing procedure.

¹² Ongoing procedure.

¹³ Cf. Activity Report 1999/2000, p. 42, p. 94.

¹⁴ Cf. Activity Report 2005/2006, p. 33, p. 149.

¹⁵ Cf. Activity Report 2007/2008, p. 153.

13. Cases were typically triggered by customer complaints, whistle-blowers, or by internal reviews conducted by contracting authorities. In one case, a news magazine that had been contacted by a whistle-blower informed the Bundeskartellamt about an ongoing cartel.

14. A case that is currently being prosecuted concerns bid-rigging in the procurement of certain specialised vehicles. In this case, it is suspected that the relevant producers operated a quota arrangement. The specific rules of public procurement in this sector may have been conducive to operating the cartel. Although the vehicles are ultimately procured by local authorities, they are typically subsidised by the respective federal state. This system entails that in the procurement process an initial round of market investigation takes place to determine the approximate price level in order to establish the amount of co-financing by the relevant state. This might give the producers additional lead time to operate the cartel. The Bundeskartellamt's investigation was triggered by several strands of information, among them one originating from the state authority involved in co-financing, another originating from a local contracting authority.

15. There is a good theoretical case to argue that collusion and corruption in bid-rigging cases go hand in hand. However, actual cases which provide empirical evidence are rather few and far between, in the Bundeskartellamt's experience.

16. One such case investigated by the Bundeskartellamt concerned the procurement of combat boots for the German Armed Forces. An employee of the Armed Forces Procurement Agency was bribed by colluding firms and passed on confidential information that facilitated collusion among producers supplying the armed forces with combat boots. An internal review by the procurement agency detected irregularities, and the state prosecutor's office prosecuted for corruption. The relevant information on collusion among the producers was given to the Bundeskartellamt. The investigations of the Bundeskartellamt confirmed the suspicion of quota agreements for four tendering procedures involving six companies. Based on the information that was revealed to them by the bribed official, the companies submitted their bids in such a way that the contracts had to be awarded according to the quotas that the companies had collusively agreed on. The Bundeskartellamt issued fines for infringing the ban on cartels against the companies and their chief executives.¹⁶

4. Conclusion

17. Although the system of public procurement is intended to be competitive, certain characteristics of public procurement may facilitate bid-rigging. With the rules on reviewing procurement decisions in place, the competitive nature of procurement procedures can be monitored at least to some degree. However, these review procedures by the procurement tribunals are not aimed, primarily, at identifying bid-rigging, and cannot accomplish this in a systematic way. The main responsibility for avoiding bid-rigging – e.g., by designing procurement procedures accordingly – and for being sensitive towards indicators of bid-rigging lies with the contracting authorities. The cases taken up by the Bundeskartellamt indicate the practical significance that this vigilance has for prosecuting bid-rigging.

¹⁶ Cf. Activity Report 1999/2000, p. 94.