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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

Contribution from South Africa

-- Session V --

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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

-- South Africa --

1. Introduction

1. Given that public procurement accounts for between 11 and 15% of GDP¹, the South African government actively utilises public procurement as a policy instrument to promote economic development to the benefit of those who had been discriminated against during apartheid.

2. The South African Constitution specifically provides that a preference system to advance previously disadvantaged individuals be located within a “fair, competitive, transparent and cost-effective procurement system”. Consequently, there has been a flurry of activity in policy-making and law-making to give effect to these principles. Although these policies and laws do not make specific references to bid rigging, in the antitrust sense, they are based on principles that recognise the value of competition in bringing down prices, improving quality and ensuring ‘value for money’, .

3. Collusive tendering is a *per se* prohibition in South Africa’s Competition Act (1998). In the recent past, the authorities have seen a significant increase in bid rigging cases. This is partly due to the prioritisation of enforcement in the construction sector, where the practice appears most prevalent.

4. There has also been greater use of the corporate leniency policy (CLP). During January 2010, the Commission was considering 66 applications for corporate leniency, 59 of which involved collusive tendering. A further 122 marker applications, the majority in construction, had been received. Three cases involving bid-rigging are currently being prosecuted before the Competition Tribunal. These, and a fourth case which was settled, are briefly discussed below. The next section will outline government policy and legislation on procurement, and the paper concludes with a discussion of the Commission’s advocacy work.

2. Government Policy and Legislation

- The *Green Paper on Public Sector Procurement Reform* (1997), still referenced today by policy makers, sets the framework for subsequent policy and legislation. The Green Paper emphasised continuous monitoring and vigilance by government departments to eliminate and counter corruption.
- The *Public Finance Management Act* (1999) seeks to ensure transparency, accountability and sound management in government spending. It designates the heads of government departments and agencies as “accounting officers” who are legally obliged to ensure good governance in financial management. Accounting officers are specifically required to put into place fair

¹ Department of Environmental Affairs and Tourism, United Nations, and United Nations Environment Programme. 2008. Final report of the national roundtable on sustainable consumption and production. Available from URL <http://www.environment.gov.za/Services/documents.html#>.

tendering procedures that safeguard against corruption. The *Municipal Finance Management Act* (2003) does same for local authorities.

- The *Preferential Procurement Policy Framework Act* (2000) sets out criteria and procedures to ensure transparency in awarding tenders using a preference points system that favours firms owned by previously disadvantaged individuals. Regulations to this *Act*, published for comment in 2009, include a signed declaration that the information in tender documents is true and correct; and requires bidders to provide proof on request.
- A *Policy Strategy to Guide Uniformity in Procurement Reform Process in Government* (2003) provides for Treasury to set standards and publish guidelines and practice notes to ensure uniform and competitive tender procedures at all levels of government.
- *General Procurement Guidelines* proclaims “Five Pillars of Procurement”: value for money, open and effective competition, ethics and fair dealing, accountability and reporting, and equity.
- The *Framework for Supply Chain Management* (2003) prescribes a governance framework for awarding government contracts and appointing consultants. It requires separate bid adjudication and bid evaluation committees in the tender process. Members of bidding committees have to declare conflicts of interest. Firms that appear on the list of restricted suppliers do not qualify as bidders and bids from firms who have engaged in corrupt practices may be rejected.
- Treasury publishes and manages a *List of Restricted Suppliers*. Accounting officers are required to check the prohibition status of bidders prior to awarding contracts. Treasury also maintains a *List of Tender Defaulters*, which is a statutory obligation in terms of *The Prevention and Combating of Corrupt Activities Act* of 2004. This act provides that companies convicted of tender fraud may be restricted from doing business with the public sector for up to 10 years.
- In July 2009, the government established a *Ministerial Task Team* to “scrutinise public expenditure trends and propose cost-cutting measures as part of the government’s response to the economic meltdown and the negative impact of the current recession on the national fiscus.” Its objectives include preventing fraud and corruption, although it makes no specific mention of bid-rigging. The task team includes representatives from the National Treasury, Receiver of Revenue, Auditor General, Special Investigations Unit, and the Financial Intelligence Centre.

3. Competition Commission Cases

3.1 Concrete Infrastructural Products

5. A CLP application revealed a cartel in the supply of pre-cast concrete infrastructural products to mainly government institutions and municipalities. The Commission found² that cartel members coordinated their quotations and agreed to share and allocate contracts amongst themselves to maintain agreed-upon market shares not only in South Africa but also for the Southern African region. There was also evidence of collusive tendering for contracts with two state owned entities, namely, Portnet, which controls commercial ports, and Gautrain, a government initiative to introduce a rapid rail link system in the Gauteng province of South Africa. In one instance, competitors sought to share the market by collectively

² The Competition Commission vs Rocla, Infraset, Empowa, Grinaker-LTA, Southern Pipelines, Concrete Units, Craig Concrete, Cobro, Cape Concrete, DND Concrete, Concrit Walls and Grallio (Case number: 2008Mar3595).

bidding through “the railway sleepers’ joint venture” in circumstances where they could have bid independently

6. The holding company of one of the parties, Aveng, settled with the Commission with an administrative penalty of ZAR46.3m (€4,1m). It also undertook to put into place a compliance programme and agreed to co-operate with the Commission’s investigation. The case against the remaining members of the cartel is currently pending before the Tribunal.

3.2 *Pharmaceutical Supplies to Public Hospitals*

7. The Commission initiated an investigation³ into collusion over State Tender Contract RT299, for the supply of large volume intravenous solutions and related products to public hospitals across South Africa. One of the parties subsequently applied for corporate leniency and provided detailed information about its role and the role of its competitors in the collusive tendering. The competitors had collaborated and agreed on prices prior to the submission of their respective tenders. The firms also agreed that winning firms would cede portions of their business arising from Contract RT299 to one or other of the losing firms in certain proportions.

8. All the members of this cartel have settled with the Commission with admissions of guilt and administrative penalties totalling ZAR55m (€4,9m). In addition the parties have agreed to implement compliance programmes.

9. This case drew the attention of the Department of Health to the losses it could incur through bid-rigging. The department’s representative at the Tribunal hearing was keen to claim damages in terms of the Competition Act, but this has not been pursued. The experience did, however, prompt the department to review its procurement processes.

10. Contract RT299 was put to tender again in 2009, and interestingly the Department of Health allowed members of the cartel to bid. The department’s view was that the exclusion of the firms would have been counterproductive as it would dampen competition in an oligopolistic market. One of these firms, which subsequently won part of the tender, voluntarily informed the Commission of measures it had taken, in terms of its compliance programme, to ensure an independent bidding process.

3.3 *Buyers of Scrap Metal*

11. The Commission initiated an investigation⁴ into possible collusion in the scrap metal industry following its prohibition of a horizontal merger in the industry in February 2006. The merger documentation implicated parties in anti-competitive behaviour in the collection and supply of ferrous and non-ferrous scrap metal. The Commission found evidence of collusive tendering in the 2007 auction of wagons, coaches, and tankers by state owned rail transport entity, Spoornet (now known as Transnet Freight Rail).

12. There was a general understanding amongst competitors to not push up the purchase prices at local auctions or to bid against each other. The evidence indicated that the cartel had also enlisted the co-operation of an insider in Spoornet.

³ The Competition Commission vs Adcock Ingram Critical Care (AICC), Tiger Food, Fresenius Kabi South Africa (FKSA), Thusanong Health Care (Thusanong) and Dismed (Criticare) (2005Jan1404 and 2007Nov3376).

⁴ The Competition Commission vs The New Reclamation Group (Reclam), Aberddac Group, Amalgamated Metals Recycling, Ben Jacobs Metals, Power Metals, SA Metal and Universal Recycling (2007Aug3121).

13. The acquiring firm to the merger that triggered the investigation, Reclam, has since settled with the Commission, with an administrative penalty of ZAR146m (approximately €13m), representing 6% of its annual turnover in the affected markets. Reclam also agreed to implement a compliance programme and co-operate in the Commission's prosecution of the remaining members of the cartel. This case will be referred to the Tribunal for adjudication.

3.4 *Plastic Pipes for Water and Sanitation*

14. Another collusion case⁵ which emerged from a merger review was in the market for plastic pipes used mainly by municipalities in the provision of water and sanitation. The acquiring firm to the merger has also since applied for corporate leniency and has furnished the Commission with evidence of the existence of collusion in the markets for the pipe products. The alleged collusion involved price fixing, collusive tendering and the allocation of markets or customers. In allocating contracts between themselves, the cartel considered pre-existing market shares and their pre-existing relationships with customers. This matter was referred to the Tribunal for adjudication in February 2009 and the hearing is pending.

4. Interaction with Government

15. The Commission has engaged in advocacy at various levels of government to create awareness of bid rigging. It works closely with National Treasury which is the custodian of policy for public procurement. The Commission has made submissions to National Treasury proposing the incorporation of a *Certificate of Independent Bid Determination* (CIBD) in its procurement processes. This is currently under consideration.

16. The Commission has also held workshops with state owned electricity utility, Eskom, which had identified bid rigging as one of its key risks. Eskom is currently undertaking a major infrastructure expansion programme. On the Commission's recommendation, Eskom is now using CIBDs in its tender processes.

17. Several presentations and workshops to identify, detect and report bid rigging have been held with a total of 235 procurement officials and bid adjudicators from national and provincial government departments. The Commission plans to expand its advocacy work with government departments, including a joint project with the OECD.

⁵ The Competition Commission vs DPI Plastics, Petzetakis Africa, Marley Pipes System, Swan Plastics, Amitech South Africa, Flo-Tek Pipes & Irrigation, Macneil Agencies, Andrag and Gazelle Plastics (Case number 2008Mar3596).