

INVENTORY OF MECHANISMS TO DISGUISE CORRUPTION IN THE BIDDING PROCESS

by

Jean-Pierre Bueb and Nicola Ehlermann-Cache*

Public funds may be misappropriated to serve private interests in every country, across many sectors of activity. Given the amounts involved in public procurement, these contracts require particular attention to prevent the misappropriation of funds as well as, in case of misdeeds, the detection of wrongdoings.

It needs to be stated from the start that corruption is not the rule in public procurement. In most countries, corruption is caused by a limited number of dishonest public officials and business people seeking to obtain personal advantage. The potential risk of corruption may be greater in international procurement than in domestic procurement, especially because of the high value associated with the contracts and the number and variety of players which makes it more difficult to trace the money and the transactions. Finally, it may be noted that in many corruption cases, regulatory means have been deflected from their true purpose.

Various mechanisms used to camouflage corruption in public procurement are reviewed in this paper. Questions are raised at the end of the paper to encourage further reflection on the ways fraud and corruption is disguised.

I. Mechanisms used to disguise corruption in public procurement

Corruption may take place at any stage in the process of tendering for, awarding and performing public contracts for works, supplies or services. Various forms of corruption can be identified throughout the four principle stages of the public procurement process:

- a) Identification of needs.
- b) Definition of specifications.
- c) Awarding of the contract.
- d) Performance of the contract.

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1. Mechanisms used during the identification of needs

It has been observed that before a contract is put out to tender, during the phase of determining project needs, two methods may be used to favour one candidate over another. The first is to distort or falsify needs so that projects can be launched which are unnecessary or bigger than planned. The second method is to commission onerous or unjustified studies.

Modified or falsified needs

Changing or falsifying needs is a way of justifying purchases, works or services that are often unnecessary or disproportionate to actual needs. The initiators of the project outline the justifications of needs in an explanatory report. In many cases these project officials can only be reprimanded for benign "mistakes" such as wrongly estimating stocks, replacing equipment that could have been repaired or failing to look for alternative solutions. However, these justifications can conceal corruption.

Unnecessary, falsified or subjective studies

Studies are often essential in order to identify needs, but can also be used for corrupt ends. Examples include small-scale studies commissioned from a favoured firm without consultation or studies that are commissioned but never delivered or claimed, even though advances have been paid. In some cases, several organisations submit identical studies, simultaneously or over a period of time. For example, an initial study is commissioned from a competent organisation. The results of the initial study are then passed on to fictitious firms that plagiarise them, generating very substantial margins that can be shared with the decision-maker through a slush fund, using false invoices (see Annex 21.A.).

Instead of commissioning studies from independent organisations, the decision-maker can have them carried out in-house. Internal units may bias their studies. Deliberate omissions can then be used later to justify an award of contracts. Usually this leads to a negotiated procedure, which is generally unpublicised and is without competitive tendering.

2. Mechanisms used during the definition of specifications

It has been determined that there are many ways of concealing corruption in the process of drawing up specifications. However, they are not easy to identify, particularly when controllers are not familiar with the technical aspects of a given project. Claims, especially those made by unsuccessful bidders, must be checked quickly and thoroughly so as to ensure that controllers are not used unknowingly to eliminate a chosen candidate.

Misevaluated project estimate

The project estimate is a crucial and often complex element in the procurement process. In the most complex cases, the project is estimated in two stages: a summary estimate formulated at the same time as the initial study and a final estimate, drawn up together with the specifications. A contract estimate can be deliberately under- or overstated. Underestimation is frequent and can unduly facilitate the authorisation to begin a project. The necessary supplements will subsequently inflate the initial cost, because the winner of the initial contract will inevitably be the beneficiary of the supplements, which are rarely negotiable, generating substantial margins that facilitate corruption.

Purchases or works may be overestimated when the decision-maker is certain that a contract will be awarded. The awardee of the contract will thus have a comfortable margin, part of which may be returned to the decision-maker without increasing the initial cost. The decision-maker may even be perceived as a

good manager and re-elected for another term, since the project required neither re-evaluation nor supplemental costs.

Preference for a single supplier

A single supplier may be favoured for a contract. Two methods are frequently used to justify awarding a contract to a given firm: choosing services covered by an exclusive right; or commissioning studies or specifications from an operator linked to a group, another of whose subsidiaries will then bid for the contract. In the second case, the subsidiary has exclusive access to information that other bidders do not have.

Inaccurate data

The intentional use of inaccurate data can conceal corruption. In this case, a favoured firm is told about incomplete or inaccurate information deliberately included in the specifications. The firm may discount a particularly onerous condition in its estimate and win the contract by making a bid that is lower than other bids but provides for a higher margin nevertheless. In another example, a firm makes a low overall bid to win the contract but charges high unit prices for the goods or services needed to continue the work, without a new tender. The additional work, carried out by the contractor and paid at the stated unit price, generates a substantial profit.

Excessive specifications

Imposing specifications that are much more rigorous than general standards can be another method to disguise corruption. In this technique, the official responsible for certifying the work is an accomplice. The official states that the work is in conformity with specifications, when in fact it is not. As long as the work meets generally accepted standards, safety certification agencies do not conduct further inspections.

Imposed requirements for maintenance

Some equipment and material need maintenance that can be provided only by an installer with an exclusive right. In such cases the purchase contract is negotiated on particularly advantageous terms, but the maintenance is later carried out under conditions imposed by the supplier. This technique is encountered particularly in contracts involving computers and office equipment.

Another technique along similar lines is the purchase of state-of-the-art equipment that is incompatible with the decision-maker's existing equipment. At some point, the decision-maker will be obliged either to make expensive modifications to make existing equipment compatible or to replace it completely.

3. Mechanisms used in the awarding of the contract

The most frequent offences in the awarding of contracts involve circumventing the application of regulations. The main techniques to conceal corruption are splitting contracts, reducing publicity, misusing procedure and skewing selection criteria.

Split contracts

This method consists of splitting a large contract into several smaller ones that are not subject to public procurement regulations. The same firm does all the work but the bills are submitted under different company names. In the case of several companies taken over by a competitor, this is very easy, as acquired companies maintain their own distinct identity.

Reduced publicity

Splitting contracts can also reduce competition, especially from foreign firms by circumventing the requirement for publication of calls for tender (in the Official Journal of the European Union, for example).

Fraudulent operators can reduce publicity in other ways, such as publication in a journal with limited circulation or in domestic journals only or by making false claims of urgency that requires a shorter tender period. Wrongdoers can eliminate publicity entirely by using as justification spurious legal grounds such as state secrecy, exclusive rights, research or experimental work or additional supplies.

Misuse of procedure

There are two types of misuse of procedure that deserve particular attention: an open but inconclusive call for tenders and a restricted call for tenders.

Given that it is difficult to know the outcome of an open call for tenders, and in order to reduce the risk of an unknown bidder beating a favourite, the tender procedure is replaced by a negotiated procedure. The reason generally put forward for not awarding a contract on completion of the tender procedure is that the bidders' prices exceed the total envelope available.

A restricted call for tenders is justified in principle by the technical complexity of the operation or by the existence of patents or exclusive processes. However, the procedure may be misused in order to eliminate rivals, since in some cases work is sub-contracted to firms that do not have the required qualifications.

This procedure may also give rise to conspiracies between candidates on a list of possible tenderers. It is a real danger, since mergers and acquisitions have reduced the number of specialists, whether for works, supplies or services. It can also be noted that it may be perilous to try to break up a conspiracy, since the claimed "victims" can bring a complaint against the decision-maker for favouritism.

Biased criteria

Some of the bid selection criteria contained in public procurement regulations may be deliberately chosen for their subjective nature, enabling the classification of bids to be changed. This is the case, for example, with the "architectural aspect" or "environmental appropriateness" of a project. The criteria may also be revised by the members of the awarding commission when the bids are opened, for example by creating or modifying weightings allocated to each criterion or by adding further criteria.

Inability or failure to apply penalties

In certain cases it may prove impossible to sanction failure to comply with specifications, either because the necessary clauses have been removed from the contract or because the decision-maker does not enforce them.

Omission of mandatory clauses

Mandatory clauses are sometimes inexplicably omitted from the specifications or contractual documents, especially the general administrative terms. They are often penalty clauses for non-compliance with terms or conditions of the contract, such as missed deadlines, modification of equipment between order and delivery, obvious computational errors, etc. These omissions cannot be mere oversight, because the master documents used to draw up the contract contain all these clauses; and several deliberate steps must be taken in order to eliminate them.

Non-enforcement of penalty clauses

Where penalty clauses do exist, fraudulent intent may be revealed by the contracting authority's failure to take action against contractual non-compliance. If the amount of work has been wrongly estimated or essential services have not been provided, the fault generally lies with the contractor, design firm, technical controller, etc. and not with the contracting authority. Yet no steps are taken to sanction the initiators, despite the contractor's claims and the need for supplements to the initial contract. On the contrary, as the initiators' profits are proportionate to the volume of work, they are actually rewarded for their faults.

4. Mechanisms used during the performance of the contract

Many aberrations may occur during performance of the contract, though this no longer falls within the scope of public procurement procedure. Various methods may be used, whether in contracts for works, services or supplies, some examples of which are given here.

Misappropriation of supplies

Misappropriation in the delivery of supplies may take several forms and can occur, for example through discounts, changed orders, or through the return of equipment.

Discounts

Discounts, whether promotional, quantitative or other, can be paid to the buyer personally and not to the organisation the buyer represents. The technique is as follows:

- An account is opened with the supplier in the buyer's name and credited with discounts that have not been included in invoices. The buyer can use the credit to purchase what he or she wants. The goods concerned do not appear in any inventory because they have no legal existence.
- The discount is paid into an account that is not exactly that of the contracting authority but of an association linked to the buyer (the name of which is very similar to that of the authority), thereby providing parallel structures with money or equipment.
- Promotional products are delivered directly to the buyer: for example, if a fourth item is offered free for the purchase of three, three products are bought, paid for and delivered to the authority at the normal price while the fourth, which is free, is delivered later to another address.

Changed orders

Modifying orders is another way to misappropriate funds. A product is ordered and billed. Just before delivery, the supplier is asked to change the order for a less expensive product. The bill drawn up according to the initial order is sent to the authority. As the price is higher than that of the goods actually delivered, the supplier posts a credit equal to the difference to an account in a name similar but not identical to that of the authority.

Improper or undisclosed disposal of used equipment

Misappropriation can also occur in the return of computer or office equipment. Upon the purchase of new equipment, a buyer must dispose of used equipment. It is generally sold or taken back by the supplier in return for a small discount. If the equipment is still in working order, it is dismantled and taken to a

warehouse for destruction. The cost of dismantling and transporting the equipment is equal to the amount of the discount.

The firm to which the contract has been awarded thus finds itself in possession of goods that have no commercial value, as the acquisition price is equal to the cost of dismantling and transport, but are in working order. It can dispose of the equipment for cash, without leaving a paper trail, since this transaction would not appear in the accounts. This money can either be used to create a slush fund (see Annex 21.A.) or can be passed on to the buyer.

Irregular service provision

Aberrations can also arise in the provision of services. The mechanisms are generally more sophisticated than techniques used in the purchase of supplies. These techniques include modifying services or multiple payments for the same service.

Inappropriate changes

After a contract has been awarded, the decision-maker and the service provider may agree to reduce the services contained in the specifications so that a commission can be paid (see Annex 21.A.). The savings generated can then be returned to the decision-maker in cash or in kind (maintenance of a private residence, for example).

For intellectual services, the commissioner and the service provider may come to an oral agreement to limit the service provided. This can significantly reduce the amount of work while complying with the obligation to provide interim or progress reports which generally trigger the payment of advances.

Multiple payments

Another mechanism consists of ordering a study that already exists. This form of recycling is particularly profitable and generates substantial sums to be shared among those involved. This method is simple to use, can be used several times in succession, and is difficult to detect without prior knowledge of the original study, published under a different title.

Performance of works via multi-level sub-contracting

The involvement of a large number of firms, either members of a consortium that has won a contract or a group of sub-contractors, can multiply the possibilities for fraud. Cascade sub-contracting is an easy way to conceal fraud, and may occur at any stage of construction (groundwork, transport of materials, modified or incomplete work, etc.). Additional works covered by a supplement to the initial contract can radically transform the initial financial reckoning.