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**LATIN AMERICAN COMPETITION FORUM**

**Session III - Improving Effective Public Procurement: Fighting Collusion and Corruption**

**Background Note**

**18-19 September 2012, Santo Domingo, Dominican Republic**

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Contact: Ms. Hilary JENNINGS, Head of Global Relations, Competition Division  
Tel: +33 (0) 1 45 24 13 60; Fax: +33 (0) 1 45 24 96 95; Email: [hilary.jennings@oecd.org](mailto:hilary.jennings@oecd.org)

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## LATIN AMERICAN COMPETITION FORUM

-- 18-19 September 2012, Santo Domingo (Dominican Republic) --

### Session III – Improving effective public procurement: fighting collusion and corruption

#### Background Note by the OECD Secretariat

#### 1. Introduction

1. Public procurement is an essential government activity that affects a country's economy. The sheer volume of high value public procurement projects creates attractive opportunities for corruption and collusion. 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. Tensions between the sometimes competing approaches to the prevention of collusion and corruption within public procurement may necessitate trade-offs to achieve both effectively.

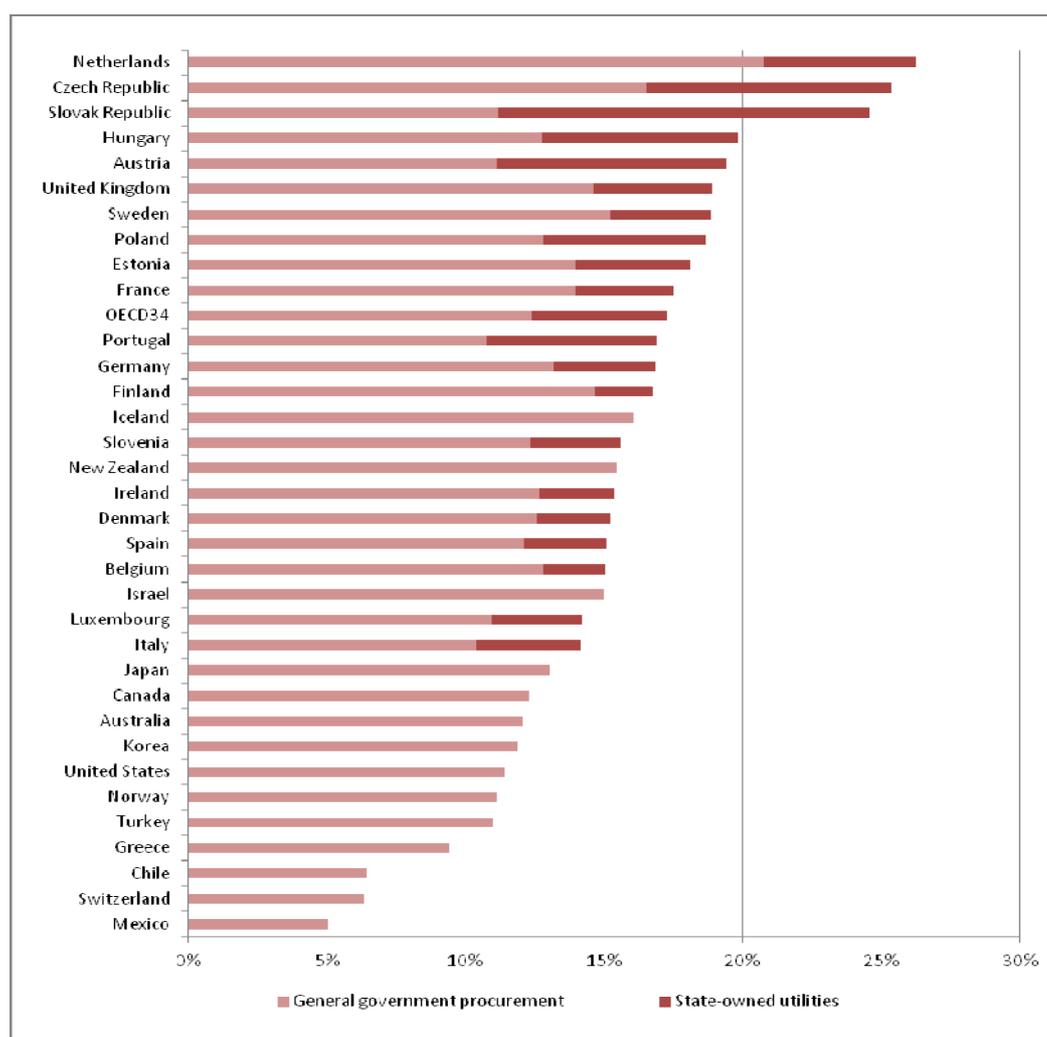
2. This paper will briefly discuss some of the complementarities and trade-offs that the fight against collusion and corruption presents to policy makers. These will be illustrated through country examples, notably from Latin America. The paper will consider the following points:

- The importance of effective public procurement systems in national economies and the relationship between collusion and corruption in public procurement;
- How the degree of transparency of the tender process may affect the likelihood of corruption and collusion;
- How the choice of bidding procedure can influence the likelihood that collusion or corruption could occur during the procurement process;
- The benefits that could be achieved by fighting collusion and corruption in public procurement in a co-ordinated way;
- Institutional frameworks that can facilitate the detection, investigation and prosecution of bid rigging and bribery in public procurement.

## 2. Collusion and corruption in public procurement

3. The performance of public procurement markets has significant implications for the effectiveness of governance in both developed and developing countries. Public procurement is one of the largest government spending activities in any country, representing on average 17% of GDP in OECD member countries.<sup>1</sup> The share of GDP is even higher in non-OECD countries. Moreover, procurement often involves goods and services with substantial economic and social significance, including transportation infrastructures, hospitals and health services, and education supplies

**Figure 1. General government and state-owned utilities procurement as a percentage of GDP (2008)**



Source: OECD National Accounts Database and Eurostat 2008

4. 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

<sup>1</sup> OECD (2011b), Government at a Glance 2011, Paris.

the long run. Procurement policy therefore may be used to shape the longer term effects on competition in an industry or sector.

5. The fundamental purpose of public procurement is to obtain goods and services at the lowest possible price or, more generally, achieve the best value for money. Ensuring that public procurement markets function effectively requires policy makers to address two distinct but inter-related challenges: (i) promoting effective competition among suppliers and (ii) ensuring integrity in administrative processes. Unfortunately, the potential for both collusion and corruption in public procurement exists in all countries and in all sectors. Moreover, collusion and corruption are often associated with other crimes, such as money laundering, accounting fraud, tax evasion and extortion.

6. In public procurement, the financial interests at stake, the volume of transactions and the close interaction between the public and the private sectors create multiple opportunities for private gains (through collusion and bribery) and waste at the expense of taxpayers.

7. The size of public tenders can generate strong competition but firms may seek to escape competitive pressures through collusion and bribery.

- *Collusion* is a horizontal relationship between bidders which restricts competition and, in public procurement, it harms the public purchaser. Through bid-rigging, the price paid by the public administration for goods or services is artificially raised. Generally, independent bidders in a procurement process ought to compete against each other to win the contract, and it is via this mechanism that the best value for money is achieved.
- *Corruption* involves a vertical relationship between one or more bidders and the procurement official.<sup>2</sup> It is first and foremost a principal-agent problem where the agent (the procurement official) enriches himself at the expense of his principal, the government purchaser (or the public more generally). Corruption arises in procurement when the agent of the procurer in charge of the procurement is influenced to design the procurement process or alter the outcome of the process in order to favour a particular firm in exchange for bribes or for other rewards. Corruption undermines growth and impedes development in the long run, creates political instability, and exacerbates inequalities.<sup>3</sup>

8. Collusion and corruption affect the efficient allocation of public contracts. By definition, they involve an allocation of contracts which would have been obtained through the competitive process. Collusion implies that public contracts are allocated to the firm chosen by the cartel. Corruption leads to the allocation of the contract to the firm who has offered the bribe. Thus, while fighting collusion and fighting corruption are separate policy challenges, they are often highly complementary. This is the case, for example, when the procurement official is paid to organise, enforce and monitor a bid rigging conspiracy.

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<sup>2</sup> In the context of public procurement markets, such abuses refer to conduct such as the awarding of contracts, the placing of suppliers on relevant lists or other administrative actions taken not for objective public interest reasons but for improper compensation or other reciprocal benefits (i.e. bribes).

<sup>3</sup> Brian (2000), *Holding public officials accountable in the international realm*, 33 Cornell International Law Journal, p. 4.

### Box 1. Examples of cases involving collusion and corruption

*Canada* – On 12 June 2012, the Canadian Competition Bureau announced that, together with the *Unité Permanente Anticorruption* in Quebec, it had brought 77 charges against 11 individuals and 9 companies in relation to a broad range of allegations that included corruption in municipal affairs. According to the Bureau, the case was the result of a two-year joint investigation. It uncovered evidence of a sophisticated collusion scheme giving preferential treatment to a group of contractors in the awarding of municipal contracts to provide infrastructure projects. The scheme reduced competition and led to a significant increase in costs for the affected cities. The consortium was able to inflate the cost of contracts by between 25 and 30 per cent and the fraud against taxpayers was valued at CAD 1 million. The scheme favoured a small number of contractors to the detriment of new bidders. Municipal officials facilitated bid rigging in exchange for gifts, tickets for shows and home improvements, while others accepted cash bribers for awarding contracts. Numerous criminal charges were brought for the corrupt conduct and bid rigging charges were also brought under the Federal Competition Act.

*United States and Mexico* – On 10 July 2012, the United States Securities Exchange Commission (SEC) charged Texas-based medical device company Orthofix International with violating the Foreign Corrupt Practices Act (FCPA) when a subsidiary (Promeca) paid routine bribes, referred to as “chocolates”, to Mexican officials in order to obtain lucrative sales contracts with Mexico’s government-owned Institute of Social Security (IMSS). From 2009 to 2011, contracts to Promeca were awarded by IMSS officials under exceptions to the public tenders procedures. The use of these exceptions is permitted, for example, when there is only one supplier in the market. Promeca, however, paid bribes to IMSS officials in order to avoid international public tenders. The bribery scheme lasted from 2003 to 2010 and generated nearly USD 5 million in illegal profits for the Orthofix subsidiary. Orthofix agreed a USD 5.2 million settlement with the SEC and entered into undertakings, including monitoring its FCPA compliance programme and reporting back to SEC for a two-year period. As a result of the US SEC’s investigation, Mexico’s Secretary of Public Administration (SFP) and the Federal Attorney Office (PGR) in Mexico commenced an investigation into IMSS’s corrupt practices on 13 July 2012.

*United States* – From 2010 to 2012, the US Department of Justice’s Antitrust Division, with the assistance of the FBI and the Internal Revenue Service carried out an investigation related to re-insulation services contracts at the New York Presbyterian Hospital (NYPH). In 2010, a NYPH purchasing official pleaded guilty to conspiring to rig bids. Between October 2000 and March 2005 the official had conspired with others to create the appearance that contracts at the NYPH were awarded in accordance with NYPH’s competitive bid policy. The official admitted that he designated which company would submit the lowest bid on a contract, and which company or companies would submit higher bids, to ensure that his designated company would be awarded the contract, thereby creating the illusion of a competitive bidding process. In exchange for awarding the contracts to the designated bidder, the official received cash kickbacks from his co-conspirators.

*United States* – On 15 September 2011, the US Department of Justice announced that Bridgestone Corporation, a Tokyo-headquartered manufacturer of marine hose and other industrial products, agreed to plead guilty and to pay a \$28 million criminal fine for its role in conspiracies to rig bids and to make corrupt payments to foreign government officials in Latin America related to the sale of marine hose and other industrial products manufactured by the company and sold throughout the world. During the bid rigging conspiracy (from 1999 to May 2007) the cartel affected prices for hundreds of millions of dollars worth of marine hose (and related products sold worldwide). Bridgestone and its co-conspirators agreed to allocate shares of the marine hose market and to use a price list for marine hose in order to implement the conspiracy. Bridgestone and its co-conspirators agreed not to compete for one another’s customers either by not submitting prices or bids, or by submitting intentionally high prices or bids to certain customers. In addition to the bid rigging conspiracy, and in order to secure sales of marine hose in Latin America, Bridgestone authorised and approved corrupt payments to foreign government officials employed at state-owned entities. As a result of the investigation, nine individuals were convicted and sentenced to a total of 4,557 days in prison for their involvement in the marine hose conspiracy. Bridgestone Corporation was charged with conspiring to violate both the Sherman Act and the FCPA.

9. Distortion of the procurement process via collusion or corruption typically has a particularly detrimental effect in the public sector context. 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.

10. Moreover, corruption and collusion in public procurement can diminish public confidence in the government and the market, ultimately inhibiting a State's economic development. 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.

11. Some sectors tend to have relatively higher instances of bribery, corruption and collusion than others. Contributing factors include government and political intervention, large capital investments and complex multi-level approval systems, all of which create opportunities for corruption. The road and telecommunication sectors are common examples.

12. Between 2000 and 2010, the World Bank committed close to USD 56 billion for road construction and maintenance. Lending for roads constitutes a significant proportion of the World Bank's portfolio, and features heavily in its development programmes. However, the impact of fraud, corruption and collusion in such projects is an on-going concern for the Bank.

13. Allegations related to road projects and the corresponding data demonstrate that the road sector is particularly vulnerable to fraud and corruption risks. In response, the Bank's Integrity Vice-Presidency (INT), which investigates misconduct in Bank-funded projects, piloted an International Road Review, focusing on collusion among bidders and corrupt practices. INT reviewed 29 cases of misconduct in Bank-funded road projects to assess the incidence of various forms of fraud, corruption and collusion.<sup>4</sup> The types of misconduct most often found in these 29 cases were: collusion, false documentation and fraud in the implementation of a contract. The report considers these cases in light of developed country experiences with collusion in public procurement. It assesses measures taken by developed countries to curb collusion for their application in developing country contexts. The report also aims to inform the Bank's own policies for detecting, investigating and sanctioning such misconduct. It explores how the World Bank and

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<sup>4</sup> World Bank (2011), *Curbing Fraud, Corruption and Collusion in the Roads Sector*, World Bank Group, Washington DC.

developing nations can reduce losses from collusion and corruption in procurement and suggests measures to eliminate them<sup>5</sup>.

**Box 2. Fraud, corruption, and collusion in the roads sector:  
Findings from the 2011 World Bank Report**

Road projects around the globe are plagued by fraud, corruption, and collusion. The Bribe Payers Index 2011, a Transparency International poll, ranked construction as the industry most prone to corruption, while a survey of international firms revealed that companies in the construction industry were more likely than firms in any other sector to have lost a contract because of bribery. World Bank-financed projects are not immune. Roughly one-fourth of the 500 plus projects with a Bank-funded roads component approved over the past decade drew one or more allegation of fraud, corruption, or collusion, according to the Bank's Integrity Vice Presidency.

***Evidence from World-Bank projects***<sup>6</sup>

"In *Bangladesh*, evidence showed that companies paid project officials up to 15 per cent of the contract value in exchange for contract awards. In *Cambodia*, INT investigators concluded that there were strong indicators that a 'well established cartel', aided by government officials, controlled the award of road contracts. In the *Philippines*, numerous witnesses independently informed ITN investigators that a well-organised cartel, managed by contractors with support from government officials, improperly influenced the Department of Public Works and Highways contracts awards and set inflated prices on projects funded by the Bank and others. In *Indonesia*, one Indonesian respondent explained that the Indonesian collusive system had been operating for 32 years, and many viewed the free market system as counter to the cultural norm of consensus and co-operation, a statement consistent with reports by Indonesia's competition law authority."

"In a project in *Eastern Europe* a World Bank procurement specialist alerted INT to a pattern in the bids on a street rehabilitation contract that suggested bid rigging. The cost figures in the bids submitted by the only two firms competing were virtually identical – down to the same typos in both. The only difference in the two bids was the total price: one was one per cent below the engineering cost estimate, and the other was one per cent higher. While INT could not substantiate collusion in this case, it did find that the high bidder had provided a false bid security"

"In *Latin America* three firms that submitted low bids on a contract were disqualified for reasons that INT suspected were aimed at keeping new entrants out, a common strategy for preserving a bid rigging scheme."

***Evidence from other projects***<sup>7</sup>

"Staff of the UK's Overseas Development Institute reported evidence on an industry-wide cartel to fix prices on roads contracts in *Uganda*. In *Tanzania*, a review by a former Prime Minister disclosed an industry-wide cartel in the road sector. In India, a deputy Government Secretary told participants at an international conference that cartels in the road sector operated in various Indian states. A joint study by the Government of *Nepal*, the Asian Development Bank, the UK's Department for International Development and the World Bank concluded that in recent years no tender in the Nepalese construction industry had been free of collusion. A statistical analysis of bids in road tenders by the *Lithuanian* competition agency strongly suggested collusion among firms there. A 2009 World Bank study of public procurement in *Armenia* noted widespread reports of collusion in tendering."

<sup>5</sup> The report recommends: customising techniques for analysing and reviewing collusive patterns in highway construction bids; making certificates of independent bid determination a prerequisite; standardising the use of high-tech equipment and machinery to test the quality of road-building materials; revisiting public tender rules and using e-procurement against collusion; greater use of independent oversight; legislating against cartels and prosecuting hard cases.

<sup>6</sup> World Bank, *supra* n.4 at 11.

<sup>7</sup> *Id.*

### 3. The role of transparency in public procurement

14. Transparency is crucial for sound procurement. Transparency is understood as the availability of information on the procurement decision-making process. It refers not only to the external publicity of the procurement event but also to the information that is disclosed to the bidders during the tender or after. Providing an adequate degree of transparency throughout the entire public procurement cycle is critical to minimising the risk of corruption and mismanagement of public funds, and to levelling the playing field for businesses, thereby promoting competition. The accessibility of information and stakeholder participation in key stages of the procurement process are essential to transparency and accountability in public procurement.<sup>8</sup>

15. The concept of transparency in government procurement – whether supporting open markets, integrity or other procurement goals, such as accountability and value for money – has four main aspects: i) ensuring adequate publicity for contract opportunities; ii) ensuring public availability and knowledge of the rules governing the award procedures; iii) providing the basis for a rules-based procurement system, by limiting the discretionary power of procurement authorities; and iv) providing opportunities for interested parties (including, but not limited to interested suppliers) to enforce and verify that the rules have been followed.<sup>9</sup>

16. The effect of transparency on the procurement process is two-fold:

- An opaque and complex procurement system provides an ideal environment for corruption to thrive. Transparency is therefore among the most effective deterrents to corruption. Transparent procedures allow a wide variety of stakeholders to scrutinise public officials' and contractors' decisions and performance. This scrutiny helps to keep officials and contractors accountable.
- Transparency alone, however, does not guarantee an efficient procurement process. Measures taken to enhance the transparency in the procurement process should be assessed to make sure they do not increase the scope for anti-competitive practices. A procurement system based on enhanced transparency can increase the scope for collusion, if it results 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.

#### 3.1 Relationship between transparency and corruption

17. Transparency requirements help to root-out and deter corruption by requiring information on the public procurement tender to be made publicly available. Procurement rules may increase the degree of transparency of the procurement system by requiring the basic facts and figures, award criteria and weights, the identities of the winning bidder and other bidders, and the terms offered by individual bidders, to be made publicly available.

18. Introducing transparency into the procurement process deters corruption in various ways:

- Publicised and transparent procedures allow scrutiny of public officials' decisions and, thereby, keep public officials accountable. A high degree of transparency reduces the information

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<sup>8</sup> OECD (2011b), *supra* n.1.

<sup>9</sup> Arrowsmith and Anderson (2011) *The WTO regime on government procurement: past, present and future*, in Sue Arrowsmith and Robert Anderson (eds.) *The WTO Regime on Government Procurement: Challenge and Reform*, Cambridge University Press, Cambridge, p. 15.

asymmetries and facilitates monitoring, supervision and control of the procurement process. It also favours public control when information is publicly available.

- Transparency makes bidders accountable and facilitates detection and punishment of malfeasance. Transparency also increases the likelihood that other bidders denounce corrupt activities, which sends positive signals about trust in the process.
- Transparency helps bidders to avoid the prisoner's dilemma in cases where it is not known if other bidders are bribing or not. Where the procedure is not transparent, the prevailing strategy would be to bribe or to leave the tender, both of which would result in a non-efficient procurement outcome.
- Finally, transparency also makes it easier for government auditors to uncover illegal conduct.

### **3.2 *Relationship between transparency and collusion***

19. Transparency-enhancing measures are, in general, consistent with the promotion of competition. They inform suppliers of opportunities to compete and give them confidence that bids will be assessed objectively on their merits – thereby enhancing their ability and incentive to bid. There are, however, circumstances in which transparency-enhancing measures can facilitate collusion among suppliers.

20. The issue of whether increasing transparency in public procurement markets helps achieve an effective and efficient procurement system deserves more attention. Improving transparency reduces the procurement official's discretion and allows the controlling bodies to monitor the process more easily, thus increased transparency is likely to diminish corruption. However, care must be taken that increasing transparency in order to decrease corrupt practices does not increase the scope for anti-competitive practices.

21. Transparency is one of the factors required for sustainable collusion. In order to reach terms of co-ordination, to monitor compliance with such terms and to effectively punish deviations, companies need detailed knowledge of competitors' pricing and/or output strategies. The artificial removal of the uncertainty about competitors' actions, which is the essence of competition, can in itself eliminate normal competitive rivalry. This is particularly the case in highly concentrated markets (which is the case with most public procurement markets), where increased transparency enables companies to better predict or anticipate the conduct of their competitors and thus to align themselves to it, expressly or tacitly. Transparency may also make a procurement procedure predictable, which can further assist collusion.

22. In the context of public procurement tenders, which are normally attended by a limited number of suppliers, the effects of information exchanges due to a transparent procurement process raises significant competition concerns. Information on the procurement outcome revealed by the procuring entity can facilitate collusion. The requirement that the name of each bidder and the amount of the bid be publicly disclosed allows the cartel to work more efficiently, because that information increases the ability of cartels to detect possible deviations from the bid rigging agreement. In other words, transparency makes it easier to police the agreement. In general, the less information provided on the tender outcome, the more difficult it is to rig bids successfully.

### **3.3 *Policy considerations***

23. Sound procurement design can go a long way towards achieving effective procurement and mitigating any trade-offs between the avoidance of collusion and corruption. In designing transparency rules and procedures, serious consideration should be given to establishing clear and precise disclosure

requirements for various types of information. Rules also need to address when and to whom the information is made available. A number of other methods could be used to make collusion harder, while safeguarding the need to reduce the risk of corruption:

- Only information on the winning bid should be released, while information on the losing bids could be made available only to issuers of tenders and controllers, and not to competitors generally.
- Because of the potentially destabilising effect of non-identifiable bidders on bid rigging, the procurement official might consider keeping the identities of the bidders undisclosed, perhaps referring only to bidder numbers, and the number of bidders remaining in the bidding process.
- The procurement official might allow bids to be telephoned or mailed in, rather than requiring that bidders turn in their bids in person at a designated time and place where all can observe.
- The procurement official might allow a bidder to submit more than one bid under different bidder numbers, or under different identities.
- The timing of the disclosure of sensitive information (such as the losing bidders' identity and their bids) could be delayed to ease the effects of such disclosure on collusion.

#### **4. Bidding procedures and the related risks of collusion and corruption**

24. The issues of the appropriate degree of transparency in the procurement process are closely related to the choice of bidding procedure. This is an important and delicate exercise as various bidding procedures have different degrees of transparency which may expose them to risks of either collusion or corruption. The choice of the "right" bidding model (or, better, the most suitable bidding model given the circumstances of the procurement) is therefore the starting point of any attempt to achieve efficiency in public procurement.

##### **4.1 *Dynamic or open tenders and sealed-bid tenders***

25. At a *dynamic (or open) tender*, bidders gather at the same time and in the same place to submit multiple competing bids. The contract is awarded by the procurement entity to the best bidder. In dynamic auctions, bidders can observe their competitors' bidding behaviour at the tender, which facilitates co-ordination at the tender and the monitoring of the agreed contract allocation. The longer a dynamic tender, the easier the co-ordination among bidders since they have a higher number of opportunities of agreeing on allocating contracts. Moreover, a bidding system where bids are publicly opened with full identification of each bidder's price and specifications is the ideal instrument for the detection of price cutting. It therefore provides the opportunity for colluders to punish firms which deviate from a collusive agreement.

26. If the risk of anti-competitive conduct is significant, the procurement official should preferably use a *sealed-bid tender* model which minimises the bidders' ability and incentives to collude. In sealed-bid tenders each bidder submits one single "best and final" bid in a sealed envelope to prevent its contents being revealed or known before the deadline for the submission of all bids to enhance competition. In a sealed-bid tender, a collusive outcome is possible but it is more difficult: effective prior communication between the conspirators prior to the tender is required and incentives to cheat on a collusive understanding are significantly higher because the ability to punish deviations is reduced, if not eliminated.

27. From an anti-corruption perspective, however, open bidding systems (such as dynamic tenders) are perceived as providing fewer opportunities for procurement officials to favour a specific firm. Normally, competitive processes are subject to various levels of supervision with external bodies evaluating bids for quality, specificity and value for money. Furthermore, firms that are not awarded a contract theoretically have the possibility of drawing public and judicial attention to their concern about potential irregularities.

#### 4.2 *Reverse auctions*

28. *The reverse auction* is another mechanism that has been recently implemented in various countries, including Brazil, Colombia, Ecuador, Mexico, Paraguay, Peru, the United Kingdom and the United States<sup>10</sup> A reverse auction is a competitive process in which a procuring entity solicits subsequent discount bids from suppliers during a defined period after the submission of their initial bids. In a reverse auction, bidders can submit one or more decreasing bids. Unlike a traditional auction, suppliers compete to sell a good or service by bidding lower than the price originally proposed in their bid submission without changing the specifications set forth in their technical proposal. The auction is typically done electronically.

29. This innovative auction format can have the following benefits<sup>11</sup>:

- Driving prices down: reducing the price the procuring entity pays for goods and services.
- Increasing the number of suppliers: the format encourages new entrants.
- Real-time market pricing for electronic auctions: suppliers can adjust their bids multiple times in response to other competitors' bids, meaning the first and the best offer can be improved to the benefit of the procuring entity.
- Time saving: the process compresses the negotiation time because suppliers simultaneously evaluate their pricing decisions when done electronically.<sup>12</sup>

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<sup>10</sup> Gazette of the Government of the State of Mexico, 3 September 2010, p. 10 and Wyld (2001), *Reverse Auctioning: Saving Money and Increasing Transparency*, Using Technology Series, IBM Center for The Business of Government, p.16.

<sup>11</sup> Wyld, *supra* n.10 at 6.

<sup>12</sup> In an electronic reverse auction the procuring entity posts the call for tender online, invitations to pre-selected suppliers are distributed automatically by email, interested suppliers place their bids, and the procuring entity can compare prices, qualifications, and other factors immediately. As a result, the time between creating the call for tender and choosing the supplier is considerably shortened.

### Box 3. Reverse Auctions – Country Examples

*United States* – The use of reverse auction mechanism by the Department of Veterans Affairs’ Hospitals (VHA) has generated savings of USD 2 million since March 2011. In addition to the cost savings, the reverse auction has also been helpful in facilitating entry by small business, as 64 per cent of the reverse auction awards on 2011 went to small business.<sup>13</sup>

*Peru* – The introduction of a reverse auction system in Peru generated significant savings. Government agencies pooled procurement of 165 essential medicines in 2010, saving approximately USD 14 million. Additionally the length of bidding processes was shortened from seven to two months.<sup>14</sup>

*Mexico* – The Secretary of Public Administration in Mexico announced that between September 2010 and June 2011, the Federal Government reported cost savings of USD 15 million from using reverse auctions. The reverse auction mechanism – *ofertas subsecuentes de descuento*, in Spanish – was included in the Federal and the State of Mexico procurement statutes on 28 May 2009 and 3 September 2010, respectively. However, the reverse auction mechanism in the State of Mexico is not yet in force.<sup>15</sup>

– The Mexican Institute of Social Security (IMSS) has achieved savings through streamlined and innovative procurement processes, including using reverse auctions.<sup>16</sup> It calculates that it has achieved savings of USD 2,838 million between 2007 and 2010. These savings essentially resulted from centralising the purchase of therapeutic goods, establishing maximum reference pricing and enhancing the use of *reverse auctions*. The table below provides detail on savings achieved by IMSS since 2009 through reverse auctions.<sup>17</sup>

**IMSS estimated savings from reverse auction (millions USD)**

Year	Category	Contract Value	Estimated Savings	%of estimated savings
2009	Medicines	605.6	64.9	10.7
2010	Medicines Health Material	185.3	4.7	2.5
	Mammography	3.6	0.9	27.4
	Vehicles	4.4	0.2	3.2
2011	Medicines	41.9	2.4	5.8
<b>Total</b>		<b>840.7</b>	<b>73.0</b>	<b>8.8</b>

<sup>13</sup> United States Department of Veteran Affairs at <http://www.va.gov/health/NewsFeatures/20111014a.asp>

<sup>14</sup> USAID, Deliver Project (2011) Presentation on *Improving Contraceptive Procurement by Building a South-to-South Exchange Network in the Latin American and Caribbean Region*, Dakar, Senegal.

<sup>15</sup> OECD (2012a), *Fighting Bid Rigging in Public Procurement in Mexico: An analytical report on procurement legislation, regulations and practices in the State of Mexico*, Paris, p 60.

<sup>16</sup> In January 2011, IMSS signed a Memorandum of Understanding (MOU) with the OECD and Mexico’s Competition Authority (CFC). IMSS’ goals were to obtain OECD support for the adoption of international best practices for fighting bid rigging and to have the OECD conduct a broad review of the integrity of IMSS’ procurement processes.

<sup>17</sup> OECD (2012b), *Public Procurement Review of the Mexican Institute of Social Security: Enhancing Efficiency and Integrity for Better Health Care - Highlights*, Paris, p.24.

### 4.3 *Direct negotiations and framework contracts*

30. From a competition perspective, there may be situations where it is not necessary to adopt some form of competitive bidding process to achieve the most efficient procurement outcome. These are situations where *individual negotiations* with a limited number of suppliers may yield the best value for money. This could occur, for example, in the following circumstances:

- If the costs of organising and holding a tender are high and outweigh its expected benefits.
- If the likely bidders and, indeed the likely lowest-cost bidder, may already be known to the procurer. In this context, it may be more efficient for the procurer to approach the least-cost bidder directly to negotiate a price (perhaps with the threat of competitive tendering if it is felt necessary).
- If it is not possible to contractually specify in advance all the elements of the services to be supplied, as may be the case with complex projects that are difficult to define in advance and where there is significant scope for adaptation as the project develops.
- If other policy reasons or other explicit reasons exist, which do not require the procurer to select the lowest-cost supplier, i.e. if diversity of supply is essential to ensure continuity of service.
- If secrecy considerations prohibit the public solicitation of bids; this may be the case where national security interests are at stake.
- If the number of potential bidders is very small and a single bidder may have very significant market power. In this case, a tender will not yield an efficient outcome and it may be appropriate to adopt more sophisticated contracting approaches to procurement.

31. From a corruption perspective, however, non-competitive procurement contracts are considered a source of concern because of their lack of transparency and democratic oversight. Procurement officials authorised to enter into such contracts have greater power over which company receives the most lucrative contracts. Without appropriate supervision, individual preferences can easily become part of the official's final decision. From the vendor's perspective, receiving lucrative contracts without being subject to the discipline of competition is highly desirable and firms can see benefits of eliminating the risk of losing the contract by influencing and/or bribing the procurement official.

32. A *framework agreement* can facilitate consolidated purchases. Procurement officials might find it more effective to use framework contracts as a basis for purchasing goods and services from pre-qualified firms meeting a number of quality standards. These standing agreements set out the general conditions of the contract to be performed over a defined time period, notably the conditions related to the price and quantities. Framework agreements can save time and resources by eliminating numerous bidding processes, thereby reducing the overall costs for procuring the goods or services.

33. Generally, a framework agreement is conducted in two stages: a first stage to select the supplier(s) or contractor(s) to be the party or parties to a framework agreement with the procuring entity; and a second stage to award procurement contracts under the agreement to one or more of the supplier(s) or contractor(s). An open framework agreement is an agreement that other suppliers or contractors can

join at any time after the initial stage.<sup>18</sup> It may be appropriate to use a framework agreement when a procuring entity has a recurring need for products or services over a period of time but does not know the exact quantities, nature or timing of its requirements, or the costs of organising and holding a tender are high and outweigh its expected benefits.

34. The use of framework agreements has been the subject of some criticism. For example, critics have argued that the use of framework agreements may undermine competition, if they result in false, if temporary, oligopolies, sheltering just a few select suppliers from ongoing competition.<sup>19</sup> However, certain elements can be introduced to make framework agreements more competitive and enhance their ability to promote, transparency, efficiency and accountability. For instance, framework agreements are normally open to new entrants, they can include fair opportunity to compete clauses; and remedy procedures can promote accountability in the case of wrongdoing by the procurement official.

#### **Box 4. Framework Agreements in Mexico<sup>20</sup>**

According to Article 14 of the regulations implementing the Mexican Federal Procurement Act, framework agreements are exempt from the application of the tender procedures outlined in the Act. But they must still respect the principles of “value for money”, effectiveness, efficiency, fairness and respectability in order to achieve the best results for Mexico. The Act states that at least five government agencies must be part of a framework agreement.

The Secretary of Public Administration (SFP) in Mexico is in charge of co-ordinating actions among the procuring entities who sign framework agreements. There are currently nine framework agreements administered by the SFP or federal entities which cover, among other things, airline tickets, uniforms, gardening, call centres, cleaning services and logistical services for public affairs events. In November 2010, the SFP approved a framework agreement for food stamps/vouchers, which they estimate has resulted in cost savings of USD 3.3 million.

Prior to entering into a framework agreement, the SFP (along with the participating agencies) is required to carry out a market study to determine: a) whether a national supplier can fulfil the conditions of the contract, in terms of quality and quantity; b) whether the supplier may be able to perform the contract, according to the requirements of the contracting authorities; and, c) the prevailing prices in the market.

Terms and conditions in framework agreements must be supported by the results of these market studies. Any supplier that meets the requirements set forth in a framework agreement can participate in that agreement. Procuring entities have the flexibility to purchase from the suppliers under a framework agreement or from another supplier, if they think, based on a new market study, that they could obtain better value for money. If the latter should occur, SFP is to consider the new information and to decide whether to amend the particular framework agreement or to cancel it.

#### **4.4 Policy considerations**

35. Given that the many different forms of procurement models are not all equal from the point of view of fighting collusion and corruption, it is important that procurement officials are aware of the risks attached to certain bidding models. Intuitively, *dynamic (or open) tenders* are more susceptible to collusion than *sealed-bid tenders*. Similarly, *private negotiations* and *framework agreements* with potential suppliers are less likely to lead to collusion than public tender processes. However, when it comes to fighting

<sup>18</sup> Horska (2010), *Curbing the World Bank’s Problem with Patronage and Corruption Through the Use of Framework Agreements*, Public Contract Law Journal, American Bar Association, Spring.

<sup>19</sup> Yukins (2008), *Are IDIQs Inefficient? Sharing Lessons with the European Framework Contracting*. 37 Pub. Cont. L.J. 545, 2008, p.9.

<sup>20</sup> OECD (2012a), *supra* n. 15 at 58.

corruption, sealed-bid and non-competitive procurement are considered to be a potential source of concern due to a lack of transparency, limited democratic oversight and a high risk of corruption.

36. The choice of the bidding model largely depends on the circumstances of the procurement. If the risk of collusion is limited (because, for example, there are many potential suppliers) an open tender would be preferable. If the risk of collusion is significant, then it would be preferable to use a sealed-bid system. If the risk of both collusion and corruption is significant, procurement officials should still consider using a sealed-bid tender, but make the tender “corruption proof”. In this case, electronic bidding or on-line bidding systems, for example, could ensure that both the risks of collusion and corruption are limited. Electronic bidding allows for a dynamic tender to take place, and at the same time ensures that a record is made of each bid and of each the person who had access to the bid. This prevents corrupt procurement officials from having had improper access to the bids before the bidding window is closed and the possibility of influencing the bidding process for personal gain. Similarly, to avoid improper manipulations, the sealed bids could be opened in public, after the closure of the bidding window, and a requirement that no bid can be destroyed and replaced could be foreseen. Alternatively, technology which makes it impossible for the procurement official to tamper with the bids could also be used.

## **5. Fighting malfeasance in public procurement – How to prevent and punish corruption and collusion?**

37. Public procurement laws and regulations are designed to promote competition between bidders and secure the best value for public money. The fight against bid rigging and bribery should be an integral part of this process. International experiences show that there are many ways to fight malfeasance in the procurement process, but in general this can be done in three broad ways: awareness raising for front-line procurement officials, establishing co-operation networks between enforcement agencies, and developing best practices rules alongside strong enforcement.

### **5.1 Awareness raising**

38. It is necessary to increase the awareness of public administrations and procurement officials on the risks of corruption and collusion in public procurement. Officials should be trained to apply adequate rules and control mechanisms to prevent and detect malfeasance. They need to be made aware of the possibility and harm caused by collusion and corruption. The use of guidelines and best practices can be particularly useful in this area where a multi-disciplinary approach can secure important results. Training should aim at improving understanding among officials of the costs that such practices have on public resources and on the benefits of ethics for the contracting authority and its officials. Training should focus on detecting signs of collusion or corruption, and giving public officials a working knowledge of the laws on collusion and corruption in their jurisdiction.

39. On the operational side, public agencies should establish internal procedures that encourage or require officials to report suspicious statements or behaviour to the competition authority, the anti-corruption body 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.

**Box 5. The OECD Recommendation on Fighting Bid Rigging  
in Public Procurement and the Guidelines**

On July 2012, the OECD Council adopted a Recommendation of Fighting Bid Rigging that calls for government to assess their public procurement laws and practices at all levels of government in order to promote more effective procurement and reduce the risk of bid rigging in public tenders. The Recommendation constitutes a step forward in the fight against collusion in public procurement that the OECD has been leading for a long time, notably through the issuing of the 2009 Guidelines for Fighting bid rigging in Public Procurement, and the work related to its dissemination worldwide.

The OECD has long recognised the vital roles that competition and procurement agencies play in fighting hard core cartels in public procurement. In 2009, the Competition Committee developed a specific methodology to help governments improve public procurement by fighting bid rigging. The OECD Guidelines for Fighting Bid Rigging in Public Procurement, now included in the Recommendation, assist procurement officials to reduce the risks of bid rigging through careful design of the procurement process and to detect bid rigging conspiracies during the procurement process. The purpose of the Guidelines is to help procurement officials to identify:

- Markets in which bid rigging is more likely to occur so that special precautions can be taken.
- Methods that maximise the number of bids.
- Best practices for tender specifications, requirements and award criteria.
- Procedures that inhibit communication among bidders.
- Suspicious pricing patterns, statements, documents and behaviour by firms, that procurement agents can use to detect bid rigging.

More information on the OECD Bid Rigging Guidelines can be found at [www.oecd.org/competition/bidrigging](http://www.oecd.org/competition/bidrigging).

***OECD Principles for Enhancing Integrity in Public Procurement***

The OECD has developed a set of Principles for Enhancing Integrity in Public Procurement. The Principles were approved as a Recommendation by the OECD Council in October 2008. This instrument provides guidance to policy makers on how to enhance integrity in public procurement. The Principles are anchored around 4 pillars: (i) transparency; (ii) good management; (iii) prevention of misconduct, compliance and monitoring; and (iv) accountability and control. The Principles support the implementation of international legal instruments developed within the framework of the OECD, as well as other organisations such as the United Nations, the World Trade Organisation and the European Union.

To help countries implement the Principles for Integrity in Public Procurement, the OECD has developed a compilation of existing tools used in member and non-member countries (the “Toolbox”). The aim of the Toolbox is to support public officials in designing and developing guidance and procedures at various points in the procurement cycle.

More information on the OECD Principles for Enhancing Integrity in Public Procurement can be found at [www.oecd.org/gov/ethics/procurement](http://www.oecd.org/gov/ethics/procurement).

**5.2 *Creating networks between enforcement agencies***

40. Establishing national (and international) networks of experts from procurement administrations, competition authorities and public prosecutors to improve the exchange of information and experiences that enhance the detection and prevention of corruption and bribery.

### **Box 6. Examples of national co-operation networks**

*Brazil* – A Public Procurement Unit was created within SDE (the Secretariat of Economic Law), the Ministry of Justice’s competition authority (now merged with CADE under the 2011 competition law), for the specific purpose of fighting bid rigging. The unit, in collaboration with the Office of the Comptroller General (Contraladoria-Geral da União - CGU), the Federal Court of Auditors (Tribunal de Contas da União – TCU), and the Ministry of Planning, among others, works to provide training to federal and state procurement officials on bid rigging issues. It monitors procurement procedures and has initiated several formal proceedings in relation to public works and other contracts linked to the Brazil 2014 World Cup and the Rio 2016 Olympics, which are major sources of sizable public tenders.

*Chile* – In 2008, the Fiscalía Nacional Económica (FNE) in Chile brought together several public bodies and an association of public procurement officers to create the Inter-Agency Task Force for Fighting Bid Rigging (Comité Anti-Colusión entre Oferentes en Licitaciones de Abastecimiento Público). The Taskforce helped build awareness of collusion, the importance of tackling it, how to detect it and steps agencies can take to prevent collusion. Other initiatives included: the development of guidelines with Chile Compras, the e-procurement agency, based on the OECD materials; the incorporation of bid rigging detection criteria into standard audits performed by the General Comptroller; and the creation of anti-bid rigging units in the Ministry of Public Works

*Canada* – Corruption is not within the mandate of Canada’s Competition Bureau, except when a procurement official aids the commissioning of bid rigging offences committed by other parties (suppliers). In 2010, in response to allegations of corruption and bid rigging in the Quebec construction industry, the Province of Quebec announced the creation of a unit comprised of 40 officers from various law enforcement agencies, including the Competition Bureau, dedicated to investigating the corruption and bid rigging allegations. The Bureau’s role is to provide advice and expertise on aspects falling within its enforcement responsibilities, principally bid rigging.

*Indonesia* – The Indonesian Competition Authority (KPPU) has made many efforts to prevent collusion in public procurement, including entering into co-operation agreements with other state agencies. A memorandum of understanding was agreed with the Indonesian Corruption Eradication Commission (KPK) in February 2006. The scope of the co-operation covers access to data information and co-ordination related to respective case findings. If the KPPU uncovers corruption in the course of its antitrust investigations, it notifies the corruption activities to the KPK, while the KPK continues to focus on the collusion aspects, and vice versa.

*Peru* – The OSCE (Organismo Supervisor de las Contrataciones del Estado) is the agency responsible for the supervision of the compliance of the tender procedures with the public procurement regulation. If the agency suspects a corruption or collusion matter, it must suspend the tender procedure and send the case to the National Comptroller Unit for investigation. A recent amendment (on 9 August 2012) to the implementing regulations of the Procurement Act authorises the OSCE to publicise the names of the executive officers from the companies that have been sanctioned in procurement procedures, to deter other authorities from contracting with them.

*United States* – On 13 February 2009, the US Congress passed the American Recovery and Reinvestment Act, as a direct response to the economic crisis. Its goals are to create new jobs, spur economic activity, and invest in long-term growth, and underpin accountability and transparency in government spending. As part of this initiative, the Government provided USD 787 billion (rising to USD 840 million) some of which was to fund federal contracts. In May 2009, the U.S. Department of Justice’s Antitrust Division launched its Recovery Act Initiative as a co-ordinated effort to help detect fraud and collusion in the award of economic stimulus projects.

### **5.3 Best practices and vigorous enforcement**

41. The most effective deterrent for collusion and corruption is to develop clear best practices, rules and regulations on detecting collusion and corruption in procurement processes, coupled with strong enforcement. Experiences with both anti-corruption and anti-collusion polices clearly indicate that high penalties (both civil, criminal and administrative) and high probability of catching perpetrators, have proved to be the most effective means to fight bribery and collusion in public procurement.

42. 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.

43. A number of sanctions that are specific to the public procurement context may also be available to further discourage firms and public officials from engaging in these practices. 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.

44. 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.

#### **Box 7. Sanctions and deterrents specific to public procurement**

##### ***Self-certifications***

Certifications of compliance with the law by bidders and by procurers alike have proved to be very useful. In some countries, for example, bidders are required to submit a Certificate of Independent Bid Determination (CIBD) as a requirement for bidding. CIBDs typically require each bidder to certify under oath that it has not agreed with its competitors about bids, that it has not disclosed bid prices to any of its competitors and that it has not attempted to convince a competitor to rig bids. CIBDs not only inform bidders about the illegality of bid rigging, but they also make prosecution of bid riggers easier, and they add additional penalties, including possibly criminal penalties for the filing of a false statement to the government. Similarly, in some countries such as the United States, government officials involved in procurement are required to certify that they have no knowledge of or did not improperly release procurement information and that they have attended specific training courses. In some cases, they are asked to provide on voluntary basis personal financial information to rule out possible conflict of interests.

*Brazil* – Suppliers/contractors in federal public procurement processes related to the 2014 FIFA World Cup and the 2016 Olympic Games, are required to file a certificate confirming that they have not engaged in any form of bid rigging and are aware that they could face prosecution for both cartelisation and fraudulent misrepresentation.

##### ***Disqualification orders***

Alongside conventional civil, criminal and administrative sanctions, some countries have adopted specific sanctions for illegal conduct in public procurement. In particular, sanctioning corruption and bid rigging through a denial of access to future bidding opportunities – also known as disqualification or debarment – have received particular attention. Views on how to implement these sanctions are mixed. On the one hand, debarment can be a serious weapon to achieve specific and general deterrence. On the other hand, as a systematic (and automatic) debarment policy bears risks for collusion in markets where there are already few potential suppliers. These drawbacks could be avoided if the disqualification order is directed at the individuals involved in the conspiracy and not their company. Debarment of individuals reduces incentives to engage in illegal conduct, but allows the company to continue to participate in future procurement opportunities. Other sanctions, such as monetary sanctions, could still be imposed on the companies for the breach of competition or ethical rules by their employees.

Since 1999 the *World Bank Group* has used the debarment to protect Bank Group funds, and as away to hold fraudulent individuals or firms accountable for their misconduct. Publicising the debarments deters potentially wayward firms from participating in Bank Group projects thereby increasing the opportunity for competition among bidders and protecting Bank Group funds from misuse.<sup>21</sup>

*United States* – Antitrust violations involving bid rigging can also result in a contractor’s suspension or debarment. In the US, the Federal Acquisition Regulation (FAR), provision 9.407-2 (a)(2) permits the purchasing agency to suspend contractors suspected of violating “Federal or State antitrust statutes relating to the submission of offers” and states that an indictment for antitrust violations “constitutes adequate evidence for suspension.”

*Korea* – It is mandatory for the Korea Fair Trade Commission (KFTC) to notify the Public Procurement Service (PPS) of any habitual bid riggers in public tenders. The PPS disqualifies those bidders from future public tenders for a certain period of time.

#### ***Civil society participation***

Civil society participation in key stages of the public procurement cycle promotes direct public scrutiny and transparency. Some OECD countries have mandatory or voluntary participation mechanisms in place, mostly for the bid opening process and public hearings on the terms of a contract. *Japan* and *Korea* are obligated to involve citizens in one or more stages of the procurement cycle, including through: consultations on definition of needs, oversight of the bid opening process, public hearings regarding the terms of a contract, involvement in complaints process during contract implementation, and monitoring contract delivery. In other countries, such as *the Czech Republic*, *Poland* and the *United States*, civil society involvement in the procurement process is predominantly on a voluntary basis.<sup>22</sup>

The *World Bank* report on roads notes that an important complement to engaging civil society monitors is requiring the publication of the contract and related documentation such as audit reports, fund disbarments schedules, and project performance reports. Publication of such information raises the threat of scrutiny by the media and civil society, thus reducing the likelihood of bribery and other corrupt payments.<sup>23</sup>

*Mexico* – The State of Mexico’s various procurement groups are required, in certain circumstances, to use a social witness in a procurement procedure. Article 1.42 of the State of Mexico’s Administrative Code notes that using social witnesses is a mechanism to increase public participation in the most relevant public procurement procedures – those involving a high level of financial resources, social impact and economic and social development. Any individual and legal entity may apply to become a social witness for any procurement procedure carried out by the State’s secretariats, agencies, municipalities, auxiliary organisations and administrative tribunals. Social witnesses participate in all stages of the procurement process and issue a written report to the Secretariat of the Comptroller at the conclusion of the process. A social witness is required to inform the Secretariat of the Comptroller about any irregularity observed during a procurement procedure. One of the OECD’s recommendation in its analytical report on procurement in the State of Mexico suggests that: “[t]he role of social witness in tendering procedures should be enhanced, at both the State and Federal levels, by focusing not just on transparency but also on competition issues.”<sup>24</sup>

#### **5.4 *The role of competition authorities and competition policy in the fight against corruption***

45. Good laws for the financing of political parties, high ethical standards in the civil service, a satisfactory level of resources and technical expertise, as well as transparent information for controlling bodies are essential for fighting corruption. This requires strong working relationships between

<sup>21</sup> For instance, the Macmillan publishing company was banned by the World Bank from taking up contracts financed by the Bank for six years after it admitted paying bribes to public officials during a bidding process for an education project in Sudan backed by a World Bank fund. *The Times*, 6 May 2010.

<sup>22</sup> OECD (2011b), *supra* n.1 at 98.

<sup>23</sup> World Bank (2011), *supra* n.4.

<sup>24</sup> See OECD (2012a), *supra* n.15 at 98.

competition, corruption, and procurement authorities. By taking stock of existing working methods and concerns, competition authorities' advocacy programmes will be better able to respond to the joint challenges facing procurement agencies. Advocacy efforts by competition authorities (and indeed by procurement agencies) can also target private companies, particularly those who are frequently active in bidding markets. While this effort could be costly in terms of resources and time, it may have beneficial effects in the long-term. There are various ways this could be achieved, including the following:

- Firms could be required by the tender notice to adopt internal procurement compliance programmes as a condition for bidding in a public procurement tender. Such compliance guidelines could be written in co-operation with or approved by the competition authority.
- Another condition could be to require the individuals who are responsible for bidding to have attended regular briefings and programmes thereby encouraging knowledge of the penalties for collusion and corruption. Those programmes could be offered by officials of the various authorities concerned, including the competition and procurement agencies.

46. Beyond advocacy, an effective antitrust regime and vigorous antitrust enforcement can significantly contribute to reducing corruption in public procurements. It is well established that rents induced by a lack of competition can foster corruption. When a company enjoys a rent and its business is under the influence of a public official, the public official can reap some of the rent by surrendering his control rights in exchange for a bribe. Thus an increase in rents, even those originating from a restriction of competition, tends to increase corruption. This suggests that policies aimed at fighting corruption should not only reform the legal system to increase punishment for malfeasance or to increase remunerations of public officials to reduce their incentive to accept kick backs, but should also adopt measures to increase competition in the procurement process as a way of limiting the scope for corruption.

## **6. Finding the most effective institutional framework**

47. 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, the most effective approach requires co-operation between the various enforcement agencies, whether by means of a formal memorandum of understanding, notification requirements or other mechanisms.

48. The benefits to a co-ordinated 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 co-operation policy can improve knowledge of misconduct in public procurement amongst enforcement agencies more generally.

49. Systematic exchanges of information between various enforcement agencies and joint investigations are therefore highly recommended. In particular, it would seem wise to systematically open a competition investigation on procurement markets for which evidence of corruption has been found. In addition, it may be possible to control collusion and favouritism by designating procurement-oversight agencies. This may involve the creation of a separate supervisory body to monitor the procurement official's conduct and ensuring that the procurement process is not used to distort competition.

### **Box 8. The Public Spending Committee in Brazil**

In 2008, the Office of the Comptroller General of the Union launched the Public Spending Committee (*Observatório da Despesa Pública-ODP*) as the basis for on-going detection and sanctioning of misconduct and corruption. Through the Public Spending Committee, procurement expenditure data is cross-checked with other government databases as a means of identifying atypical situations that, while not a priori evidence of irregularities, warrant further examination. Based on the data gathered over the last several years, a number of daily cross-checks are made between procurement and other government data. This exercise generates “orange” or “red” flags that can be followed up and investigated by the Office of the Comptroller General. In many cases, follow up actions are conducted together with Special Advisor on Internal Control and internal audits units within public organisations. Examples include suspicious patterns suggesting possible bid rotation and market division among competitors by sector, geographic area or time period, which might indicate that bidders are acting in a collusive scheme.

50. Some countries have enacted specific legislation aimed at fighting collusion when public procurement officials are directly involved in orchestrating the bid rigging. While the anti-competitive conduct of the firms involved is caught by the provision in the competition laws, the competition authorities generally lack enforcement tools against the illegal conduct of the public officials involved. This is often the case as corruption is categorised in many countries as a criminal offence, which is prosecuted under the general criminal law enforcement system.

### **Box 9. Examples of recent laws sanctioning collusion and corruption in public procurement**

*Colombia* – On 12 July 2011, the Colombian Federal Executive approved the Anti-Corruption Statute which includes a provision sanctioning bid rigging in the context of public procurement. Under Article 27 of the Anti-Corruption Statute any person who, in the course of a public procurement selection process, reaches an agreement to unlawfully alter the process, faces six to twelve years in prison and a fine ranging from 200 to 1000 times the minimum monthly wage (about USD 550). This statute also prohibits the procuring entities from procuring goods or contract services from companies that have financed political campaigns.

*Mexico* – On 12 June, 2012, the Mexican Federal Executive enacted the Federal Anti-Corruption Act, which includes sanctions for public officials and individuals involved in corruption practices related to public procurement in Mexico. Article 27 sets out penalties for individuals ranging from 1000 to 50,000 times the minimum wage applicable in the Federal District and the penalties for corporations ranging from 10,000 to 2 million times the minimum wage applicable in the Federal District. Additionally, the penalties may be increased to 35 per cent of the total value of the contract when the contract has been awarded to the infringer.

*Japan* – Under the 2002 Act Concerning the Elimination and Prevention of Involvement in Bid Rigging, the Japan Fair Trade Commission (JFTC) can take action against public officials involved in bid rigging (so-called “government-initiated bid rigging”). When the JFTC discovers that procurement officials have been involved in a bid rigging conspiracy, it enforces the Anti-Monopoly Act against the companies involved and at the same time it can request the head of the procurement agency involved to investigate the misconduct by its employees and to take all necessary measures to eliminate their involvement in the bid rigging conspiracy. The adopted measures must be made public. In addition, if the investigation has confirmed the involvement of public officials in bid rigging, the administration is entitled to demand compensation from the employees involved for the damage caused.

51. Co-operation 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 co-operation. While a combined approach is not a necessary requirement of an effective strategy, whatever the structure of the

co-operation 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.

## **7. Final remarks**

52. Given the significance of public procurement for national economies, it is important for governments to address the difficult issues arising from the interface between policies aiming at eliminating collusion and corruption in public tenders. Both practices generate significant damages for taxpayers and should be addressed in a co-ordinated fashion to maximise the deterrent effect of both anti-competition and anti-corruption laws. There may be difficult trade-offs between the two policies. As this paper has identified, the desired degree of transparency of the procurement process is one of example of these difficult policy choices. Should governments opt for a maximum level of transparency to reduce the risks of corruption and keep public officials accountable? Or should they opt for a minimum level of transparency to limit the opportunities for bidders to engage in collusive practices? Should open and transparent procedures be favoured in every case over direct negotiations? These questions cannot be answered in the abstract and procurement officials should tailor their choices to the specifics of each tender.

53. Competition and anti-corruption authorities can be of great support in helping procurement officials find the most appropriate balance. Improved national and international co-operation between the three sets of officials is therefore key to tackling collusion and corruption in public procurement. The use of guidelines and best practices, possibly reflecting experiences at an international level, alongside concerted information sharing information between the public officials involved can result in more efficient procurement.

54. Consequently, the optimal strategy to tackle both collusion and corruption in public procurement appears to require a three-pronged approach combining development of best practice rules for public procurement with wide-ranging advocacy efforts and vigorous law. This in turn will deliver cost savings to governments and taxpayers, which can benefit economic development and growth in developed and developing economies alike.

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