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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

Contribution from Mr. William Kovacic and Mr. Robert Anderson

-- Session V --

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Ensuring integrity and competition in public procurement markets: a dual challenge for good governance

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I. Introduction

Ensuring the effective functioning of public procurement markets necessitates addressing two distinct but inter-related challenges: (i) ensuring *integrity* in the procurement process (i.e., preventing corruption on the part of public officials); and (ii) promoting effective *competition* among suppliers, including by preventing *collusion* among potential bidders. These two challenges sometimes merge, for example where public officials are paid to turn a blind eye to collusive tendering schemes or to release information that facilitates collusion (e.g. the universe of potential bidders or the bids themselves). However, analytically, preventing corruption on the part of public officials and promoting effective competition between potential suppliers are separable challenges: the former (corruption) is first and foremost a principal-agent problem in which the official (i.e. the "agent") enriches himself at the expense of the government or the public (i.e. the "principal"); while the latter (promoting competition) involves preventing collusive practices among potential suppliers and removing barriers that unnecessarily impede healthy competition.[1]

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[1] See, for useful clarification, Frédéric Jenny, "Competition and Anti-Corruption Considerations in Public Procurement," in OECD, *Fighting Corruption and Promoting Integrity in Public Procurement* (Paris, 2005), chapter 3, pp. 29-35 (distinguishing between corruption involving public officials and collusion between potential suppliers, and noting factors contributing to each problem). Related perspectives are provided in Jean-Jacques Laffont and Jean Tirole, *A Theory of Incentives in Procurement and Regulation* (Cambridge, Mass.: MIT Press, 1993); in W.B. Bumett and W.E. Kovacic, "Reform of United States Weapons Acquisition Policy:

The issue of ensuring integrity in public procurement processes has rightly received a good deal of attention at the international level in recent years. It is addressed by various international instruments, including: (i) the UN Convention Against Bribery and Corruption; (ii) the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions; and (iii) the OECD Revised Recommendation on Combating Bribery in International Business Transactions. The prevention of corruption has also been an important focus for non-governmental organizations (NGOs), which have made important contributions in this field.[2] Given this intensive international focus, it is, perhaps, not surprising that the revised text of the WTO Agreement on Government Procurement (GPA)[3] that was provisionally adopted by the Parties to the Agreement in December 2006 contains a new substantive provision that requires procurements to be conducted in a manner that avoids conflicts of interest and prevents corrupt practices, in addition to related references in the preamble to the Agreement.[4] This provision breaks new ground and signals the increasing importance of the Agreement as an international instrument of market governance.

For the most part, the promotion of competition in public procurement markets has not received similar high-level attention as an aspect of international governance.[5] This is despite the fact that competition is a core objective of national procurement systems which is essential to good performance.[6] Certainly, the promotion of efficient conditions for international competition, consistent with the principles of comparative advantage, is central to the purposes of the GPA.[7] As will be discussed in this chapter, the realization of this

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Competition, Teaming Agreements, and Dual-Sourcing," *Yale Journal on Regulation* 6 (1989), pp. 249-317; and in William E. Kovacic, "Commitment in regulation: Defense contracting and extensions to price caps," *Journal of Regulatory Economics*, vol. 3, no. 3, September 1991, pp. 219-240.

[2] See, e.g. the activities of Transparency International, profiled at http://www.transparency.org/.

[3] See GPA/W/297 (available at http://docsonline.wto.org/DDFDocuments/t/PLURI/GPA/W297.doc) and, for commentary, Anderson and Arrowsmith, *this volume*, chapter __.

[4] See Part II, below.

[5] To be sure, there are important exceptions – notably the work of the OECD Competition Committee, the UNCTAD Intergovernmental Group of Experts on Competition Law and Policy and the Consumer Unity and Trust Society (CUTS).

[6] Steven L. Schooner, "Desiderata: Objectives for a System of Government Contract Law," *Public Procurement Law Review*, vol. 11, p. 103; see also Steven L. Schooner, Daniel I. Gordon, and Jessica L. Clark, *Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations* (Working paper, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1133234).

[7] As stated by Judge Diane Wood, a former US Deputy Assistant Attorney General for Antitrust: "While the focus [of the Agreement on Government Procurement] might appear to be on securing access to the government's business for foreign companies, the effect just as surely will be to secure the benefits of competition for the procuring government itself." Diane P. Wood, "The WTO Agreement on Government Procurement: An Antitrust Perspective," in Bernard M. Hoekman and Petros C. Mavroidis, eds., *Law and*

objective necessitates the effective enforcement of national competition law provisions relating to collusive tendering and competition advocacy efforts by relevant agencies in addition to international liberalization via an instrument such as the GPA; none of these measures is likely to achieve its full objectives in the absence of the other.

In general, measures aimed at preventing corruption in public procurement processes, particularly through enhanced transparency, are also consistent with the promotion of competition. Transparency measures promote competition by informing suppliers of opportunities to compete and by giving them confidence that bids will be assessed objectively on their merits – thereby enhancing their ability and incentive to bid on specific procurements.[8] Transparency measures, nonetheless, may not be consistent with the promotion of competition in all respects. In particular, experience in the application of competition law in public procurement markets highlights circumstances in which transparency-enhancing measures (e.g., the public opening of tenders) can facilitate collusion among suppliers.[9] This highlights a need for balancing (mutual accommodation) of competition and anti-corruption concerns. With such balancing, measures aimed at preventing corruption and promoting competition are likely to be strongly mutually reinforcing.

This chapter develops the foregoing lines of argument. The remainder of the chapter is organized as follows. Part II focuses on the challenge of ensuring integrity in public procurement processes, and the measures that can be employed to address the challenge. This includes a discussion of the new provision of the revised GPA text focusing on the "conduct of procurement". Part III reviews basic economic-theoretical considerations and evidence concerning the importance of competition in procurement markets, and the circumstances in which it is likely to thrive. Part IV discusses the principal means through which competition in public procurement markets is promoted. In addition to the possibility of international liberalization via the GPA or a similar instrument (itself a powerful tool for strengthening competition), the role of competition policy in this area is examined.[10] This

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Policy in Public Purchasing: the WTO Agreement on Government Procurement (Ann Arbor: University of Michigan Press, 1997), chapter 14. See, for related discussion, Part III(A), below.

[8] Sue Arrowsmith, *Government Procurement in the WTO* (The Hague: Kluwer Law International, Studies in Transnational Economic Law, vol. 16, 2003), pp. 169-171.

[9] See discussion in Part IV, below, and references cited therein.

[10] The term “competition policy" is sometimes equated with the enforcement of laws that prohibit various forms of anti-competitive business practices (competition or antitrust law). Properly understood,

encompasses: (i) the application of antitrust rules to prevent collusive tendering; (ii) the role of such policy in addressing regulatory and other barriers to competition, through "competition advocacy" activities; and (iii) the application of other aspects of competition law including the treatment of mergers and joint ventures. Competition policy, it is argued, is an essential complement to international liberalization via mechanisms such as the GPA.[11] This part of the chapter, specifically the sub-section on competition advocacy, also reflects on the issue of transparency measures that may facilitate collusion, and suggests some appropriate limits on such measures in this regard. Part V provides concluding remarks.

II. Corruption in public procurement markets: what is the problem (analytically) and how is it addressed?

Corruption in public administration may be defined as the abuse, by public officials, for private gain, of power that has been entrusted to them through statutory or other means.[12] 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). Corruption has rightly been condemned as a barrier to development and a scourge on the welfare of citizens in developing and developed countries alike.[13] This builds on the findings of economists such as Robert Wade that have long identified corrupt procurement practices as a barrier to efficient and sustainable

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however, competition policy encompasses a larger set of policy instruments by which a country can promote business rivalry as a means of improving economic performance. These include, very much, advocacy activities through which competition agencies and other bodies sharing similar interests encourage the adoption of pro-competitive and market-strengthening reforms (see, for related discussion, William E. Kovacic, "The Future of U.S. Competition Policy," theantitrustsource, September 2004, pp. 1-3; William E. Kovacic, "The modern evolution of U.S. competition policy enforcement norms," *Antitrust Law Journal*, 71(2): 377–478; and Robert D. Anderson and Frédéric Jenny, "Competition Policy, Economic Development and the Possible Role of a Multilateral Framework on Competition Policy: Insights from the WTO Working Group on Trade and Competition Policy," in Erlinda Medalla, ed., *Competition Policy in East Asia* (Routledge/Curzon, 2005)). In implementing competition policy at the national level, there is considerable room to account for specific national circumstances and changing capabilities through the initial definition of responsibilities and creation of policymaking instruments, the sequencing of activities, and the adjustment of powers over time. See William E. Kovacic, "Institutional Foundations for Economic Legal Reform in Transition Economies: The Case of Competition Policy and Antitrust Enforcement," 77 *Chicago-Kent Law Review* 265 (2001).

[11] See also Robert D. Anderson and William E. Kovacic, "Competition Policy and International Trade Liberalization: Essential Complements to Ensure Good Performance in Public Procurement Markets," *Public Procurement Law Review*, 2009, issue 2, pp. 67-101. By "essential complements", we mean that neither external liberalization nor the promotion of competition through national competition policies is likely to achieve its full objectives in the absence of the other instrument.

[12] See, e.g. "How do you define corruption?" on the website of Transparency International, at http://www.transparency.org/news_room/faq/corruption_faq .

development.[14] Such practices can also be viewed as an example of the more generic phenomenon of "rent-seeking" – i.e. the dissipation of a society's resources through activities that enrich individual market participants at the expense of others, without contributing to the welfare of society as a whole – a phenomenon which is viewed by some economists as being central to the problem of under-development.[15]

The economist and jurist Frédéric Jenny offers the following analysis of the "principal-agent" problem that is central to the practice of public procurement, and which can lend itself to corrupt practices:

> "Whereas the awarding of the ... contract [is] supposed to be done in such a way as to maximise public welfare, the complexity of transactions makes it impossible for the end-users to award contracts directly and they have to go through an agent over whom they have limited control because of informational asymmetries. For example, [in] public procurement markets, the body in charge of establishing the contract specifications, selecting the bidders and choosing the winning bid is frequently composed of appointed or elected procurement officers who act as intermediaries between the beneficiaries and the potential providers. ... The difficulty stakeholders have in exercising some control over the design and awarding of public procurement contracts, and thus the possibility for corruption, will be greater in cases where the service or the product which is the object of the contract is complex and/or has been designed to meet the specific needs of the demander. [Accordingly,] there is a possibility for procurement officers or the members of the procurement commission to behave strategically, that is to design the contract, to select the bidders and award the contract in such a way that the winning bidder will not necessarily be the one who maximises the social benefits but the bidder who will maximise their own welfare (by offering the largest bribe) without this strategic behaviour being easily detected."[16]

As noted in the Introduction to this paper, the revised text of the Agreement on Government Procurement on which provisional agreement was reached by the GPA Parties in December 2006 incorporates a new substantive provision regarding the "Conduct of procurement". That provision (Article V:4(c)) reads, in relevant parts, as follows:

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[13] See. e.g., B.C. Harms, "Holding Public Officials Accountable in the International Realm," *Cornell International Law Journal*, vol. 33, 2000, at p. 159.

[14] See, e.g. Robert Wade, "The system of administrative and political corruption: Canal irrigation in South India," *Journal of Development Studies*, Volume 18, Issue 3, April 1982, pages 287 – 328, and more generally, Robert Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton University Press, 2003).

[15] See, for the classic treatment, Anne O. Krueger, "The political economy of the rent-seeking society," *American Economic Review*, 1974, 64(3): 291–303. The continuing significance of this phenomenon for developinng countries is discussed in Chiedu Osakwe, "Poverty reduction and development: the interaction of trade, macroeconomic and regulatory policies", Tenth Joseph Mubiru Memorial Lecture, organised by the Bank of Uganda, 14 December 2001.

[16] Jenny, above note 1, at p. 31.

"Conduct of Procurement

4. A procuring entity shall conduct covered procurement in a transparent and impartial manner that:

...

(b) avoids conflicts of interest; and

(c) prevents corrupt practices."

Insight into the intended purpose of this provision is provided by related language in the preamble to the revised text, which recognizes the shared purpose of the Agreement with other international instruments and initiatives in deterring corrupt practices. For example, a new recital to the preamble recognizes "that the integrity and predictability of government procurement systems are integral to the efficient and effective management of public resources [and] the performance of the Parties' economies" in addition to the functioning of the multilateral trading system.[17] A further new recital recognizes "the importance of transparent measures regarding government procurement, of carrying out procurements in a transparent and impartial manner, and of avoiding conflicts of interest and corrupt practices, in accordance with applicable international instruments, such as the United Nations Convention Against Corruption".[18]

This provision represents a significant innovation in WTO law, in that, until now, WTO Agreements have generally not referred explicitly to corruption issues. Like all provisions of the Agreement, the provision on conduct of procurement is potentially subject to enforcement proceedings under the WTO Dispute Settlement Understanding. This provision, accordingly, establishes a new enforceable legal obligation on the part of GPA Parties to conduct their procurements in a manner that avoids conflicts of interest and corrupt practices – a significant extension of the WTO's role in regard to governance. On the other hand, as Arrowsmith points out, the general transparency provisions of the Agreement already play an essential role in the promotion of fair practices and the prevention of corruption;[19] in this sense, the issue is not new. In addition to the general procedural provisions of the GPA dealing, for example, with publication of procurement opportunities, advance specification of selection and award criteria, etc., the Agreement's provisions

[17] See the provisionally agreed revised GPA, above note 3, Preamble, third recital.
[18] See the provisionally agreed revised GPA, above note 3, Preamble, sixth recital.
[19] Arrowsmith, above note 8, p. 455 and, more generally, chapter 7, pp. 167-179.

relating to the establishment of domestic review or "bid challenge" procedures are an important bulwark against corruption. These provisions require each GPA Party to establish or maintain such procedures and to observe related procedural guarantees, notably that supplier challenges be reviewed in a timely, effective, transparent and non-discriminative manner.[20] These provisions recognize that, properly designed and administered, such procedures provide a fast, low-cost forum for bringing to light allegations of improper practices that affect individual suppliers and go a long way to establish a culture of "competition on the merits".[21]

Recent work by other international organizations – particularly the OECD – provides additional insights that are relevant to implementation of the prohibition in Article V:4(c), and reinforces the importance of general transparency provisions in this regard. Recently, the OECD has promulgated a set of "Principles for Integrity in Public Procurement" building on other relevant international provisions and experience with regard to the promotion of best practices in this area.[22] These principles are concerned with the entire public procurement cycle and include elements of transparency, good management, prevention of misconduct, as well as accountability and control (see Box 1). A related set of recommendations provides guidance on the implementation of the principles, e.g. through a related checklist and procedure for risk-mapping.[23]

Box 1. The OECD Principles for Enhancing Integrity in Public Procurement

The OECD has identified ten principles in order to provide policy makers with Principles for enhancing integrity throughout the entire public procurement cycle, taking into account international laws, as well as national laws and organizational structures of member countries. These include elements of transparency, good management, prevention of misconduct, as well as accountability and control.

A. Transparency

1. Member countries should provide an adequate degree of transparency in the entire public procurement cycle in order to promote fair and equitable treatment for potential suppliers

2. Member countries should maximize transparency in competitive tendering and take

[20] See Article XVII of the provisionally agreed revised GPA and Article XX of the GPA 1994.
[21] See, for essential qualification and commmentary, chapters 19-21 of this volume.
[22] See also OECD, Integrity in Public Procurement: Good Practice from A to Z (Paris: OECD, 2007).
[23] Also available in "OECD Principles for Integrity in Public Procurement," (2009), available online at: http://www.oecd.org/document/25/0,3343,en_2649_34135_42768665_1_1_1_1,00.html.

precautionary measures to enhance integrity, in particular for exceptions to competitive tendering

B. Good management

3. Member countries should ensure that public funds are used in public procurement according to the purposes intended

4. Member countries should ensure that procurement officials meet high professional standards of knowledge, skills and integrity

C. Prevention of misconduct, compliance and monitoring

5. Member countries should put mechanisms in place to prevent risks to integrity in public procurement

6. Member countries should encourage close co-operation between government and the private sector to maintain high standards of integrity, particularly in contract management

7. Member countries should provide specific mechanisms to monitor public procurement as well as to detect misconduct and apply sanctions accordingly

D. Accountability and control

8. Member countries should establish a clear chain of responsibility together with effective control mechanisms

9. Member countries should handle complaints from potential suppliers in a fair and timely manner

10. Member countries should empower civil society organizations, media and the wider public to scrutinize public procurement

Source: "OECD Principles for Integrity in Public Procurement," (2009), available online at: http://www.oecd.org/document/25/0,3343,en_2649_34135_42768665_1_1_1_1,00.html

Clearly, the OECD Principles set out in Box 1 embody an important degree of commonality with the GPA. The promotion of transparency is a core objective and principle of the Agreement (as it is of other WTO Agreements, as well), embodied in both specific provisions on transparency of procurement information in the existing and revised texts and in the general procedural provisions of the Agreement in addition to relevant aspects of the preamble.[24] Furthermore, consistent with OECD Principle 2, the GPA provides for fully competitive and transparent, open tendering as a "default" tendering procedure, restricts the use of limited tendering and provides for special transparency measures in cases of selective tendering.[25] The above-emphasized provisions regarding supplier challenges and separate

[24] See GPA, preamble, third recital and Article XVII as well as the provisionally agreed revised GPA, above note 3, Preamble, sixth recital and Article XVI.

[25] See, e.g. Articles VII:4-8 and XIII of the provisionally agreed revised GPA, above note 3.

provisions of the Agreement dealing with exclusion of suppliers on the basis of misconduct and similar grounds[26] represent key means of giving effect to Principle 7 and – at least to some extent – also Principles 5 and 9. Similar observations can be made in regard to the commonality of the OECD principles and the UNCITRAL Model Law on Procurement of Goods, Construction and Services,[27] with the qualification that the UNCITRAL Law is a voluntary instrument providing a menu of options for national governments rather than an international treaty.

This part of the chapter has examined the basis of international concerns regarding the promotion of integrity (i.e. the prevention of corruption) in public procurement markets and institutions, in addition to the ways in which these concerns are addressed in the existing and revised GPA texts and other related international instruments and activities. The next two sections delve into an important parallel concern: the promotion and maintenance of competition. The argument is made that these two concerns – the prevention of corruption and the promotion of competition - should, in broad terms, be viewed as allied rather than in tension with each other. Nonetheless, giving due weight to the promotion of competition may require some modest refinements in the application of anti-corruption and transparency measures.

III. Competition in public procurement markets: why and how much does it matter, what can undermine it?

The idea that competition tends in most circumstances to generate lower prices and/or higher quality for a given price is one of the more basic propositions in industrial organization, the branch of economics that deals with industrial structure and performance. It is nonetheless worth briefly reviewing the basis for this proposition. Although scholars continue to debate the finer points, economic literature identifies at least four main channels through which competition can have these desirable effects. First, with free entry and an absence of collusion, prices will be driven to marginal costs. Second, costs themselves will be minimized, as firms compete for survival. Third, competition serves as an important

[26] See revised GPA text, above note 3, Article VIII:3.

[27] 1994 - UNCITRAL Model Law on Procurement of Goods, Construction and Services, with Guide to Enactment, available at: http://www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/1994Model.html.

driver of innovation.[28] Fourth, competition enables the participating firms to learn from one another and thereby to continuously improve their products in addition to their marketing, production and managerial techniques.[29]

Apart from the guidance that emerges from the above-mentioned literature on competition and industrial organization generally, the benefits of competition have been explored in economic literature that deals specifically with bidding processes and procurement. This literature establishes a direct relationship between the extent of competition in procurement markets and the costs to governments of the goods and services that are procured.[30] The importance of competition for cost-effective public procurement is corroborated by the considerable efforts that firms typically devote, in business-to-business commercial transactions, to ensure that their procurement departments make effective use of competition to reduce the cost and increase the quality of inputs.[31]

Case histories and examples that illustrate the gains from the promotion of competition in government procurement regimes are fewer and less well documented than would be ideal.[32] Nonetheless, such examples as are available suggest that the gains can be substantial. A number of such examples, taken from an OECD survey, are collected in Box 2. The examples referred to therein indicate that savings to public treasuries of between 17 and 43 % have been achieved in some developing countries through the implementation of more transparent and competitive government procurement regimes. In a

Box 2. Examples of cost-savings in developing countries based on the implementation of more transparent and competitive procurement systems

A 2003 OECD study of the benefits of transparent and competitive procurement processes refers to the following examples of benefits achieved:

[28] See US, Federal Trade Commission, *To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy*, October 2003; US, Department of Justice and Federal Trade Commission, *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition*, April 2007; and Robert D. Anderson and Nancy T. Gallini, *Competition Policy and Intellectual Property Rights in the Knowledge-based Economy*, Calgary: University of Calgary Press for the Industry Canada Research Series, 1998.

[29] Useful elaboration of all four channels referred to above is provided in Dennis W. Carlton and Jeffrey M. Perloff, *Modern Industrial Organization* (Addison-Wesley, 2004).

[30] See, generally, Paul Milgrom, "Auctions and Bidding: A Primer," *Journal of Economic Perspectives*, vol. 3(3), 1989, pp. 3-22 and Paul D. Klemperer, (ed.) (2000) *The Economic Theory of Auctions*, Edward Elgar, Cheltenham, UK. See also R.I. Carr, "Impact of the Number of Bidders on Competition," *Journal of Construction Engineering and Management*, Vol. 109, no. 1, pp. 61-73, March 1983.

[31] See, e.g., David N. Burt and Richard L. Pinkerton, *A Purchasing Manager's Guide to Strategic, Proactive Procurement* (AMACOM, 2006).

[32] Simon J. Evenett and Bernard Hoekman, *International Co-operation and the Reform of Public Procurement Polices* (mimeo, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=821424, 2004).

- In **Bangladesh**, a substantial reduction in electricity prices due to the introduction of transparent and competitive procurement procedures.
- A saving of 47 percent in the procurement of certain military goods in **Columbia** through the improvement of transparency and procurement procedures.
- A 43 percent saving in the cost of purchasing medicines in **Guatemala**, due to the introduction of more transparent and competitive procurement procedures and the elimination of any tender specifications that favour a particular tender.
- A substantial reduction in the budget for expenditures on pharmaceuticals in **Nicaragua**, due to the establishment of a transparent procurement agency accompanied by the effective implementation of an essential drug list.
- In **Pakistan**, a saving of more than Rs 187 million (US $3.1m) for the Karachi Water and Sewerage Board through the introduction of an open and transparent bidding process.

Source: OECD, *Transparency in Government Procurement: The Benefits of Efficient Governance* (TD/TC/WP/(2002)31/Rev2/14 April 2003).

broadly similar vein, an independent external study for the European Commission found that increased competition and transparency resulting from implementation of the Public Procurement Directives of the European Communities in the period between 1993 and 2002 generated cost savings of between a little less than €5 billion and almost €25 billion.[33]

A further important corroborating source of information regarding the benefits of competition which is sometimes overlooked is provided by evidence of *higher* costs to public treasuries that arise when competition is suppressed, for example through collusive tendering. Such evidence is examined in Part IV(B), below. For the present, it may be noted that collusion in public procurement markets has been conservatively estimated to raise prices on the order of 20 % or more above competitive levels.[34] The benefit of introducing competition where it has not previously existed may be expected to be of a comparable magnitude.

The foregoing does not take into account explicitly the additional benefits that can accrue to countries by opening their procurement markets to *foreign* as compared to domestic competitors, for example via accession to the GPA. International liberalization – whether with respect to markets for public procurement or other economic sectors – is often conceived principally as a tool through which countries gain access to foreign markets for their national suppliers.[35] In fact, however, much of the benefit (arguably, the main benefit) of

[33] Europe Economics, Evaluation of Public Procurement Directives, Markt/2004/10/D, September 2006, available at http://ec.europa.eu/internal_market/publicprocurement/docs/final_report_en.pdf.

[34] See Luke M. Froeb, Robert A. Koyak and Gregory J. Werden, "What is the effect of bid rigging on prices?" *Economics Letters*, vol. 42(4), 1993, pages 419-423. Somewhat higher estimates of average cartel overcharges are reported in Margaret C. Levenstein and Valerie Y. Suslow, "What determines cartel success?" *Journal of Economic Literature*, Vol. XLIV, March 2006, pp. 43–95.

[35] This is the all-too-familiar "mercantilist" paradigm for international trade relations.

international liberalization actually accrues to the countries undergoing liberalization. A principal aspect of this benefit is the enhanced competition in the home market that external liberalization generates. External liberalization also creates the possibility of specialization and exchange based on the principles of comparative advantage. This is no less true for the international liberalization of procurement markets than it is for other markets.[36] International liberalization of procurement markets can also provide access to technology that is not available in the home market (i.e. the market in which goods and services are being procured).[37] Clearly, this point may be of particular significance for developing, transition and smaller economies.

Economic analysis also provides insights into the circumstances in which competition is particularly susceptible to being suppressed through collusive practices. A classic contribution by Stigler identified three challenges that must be faced for successful collusion to take place: first, the cartel members must agree on the terms of their co-operation (in a bid rigging context, this would encompass matters such as which firm will win, how the others will be compensated, etc.); second, deviations from the agreement (e.g. by firms that promise to bid high and then bid lower in an attempt to win the contract anyway) must be detected); and (iii) defectors must be punished, e.g. through expulsion from future cooperative arrangements.[38] A related challenge involves excluding or bringing into the cartel new entrants that are attracted by the possibility of *supra*-competitive profits.[39] Stigler also posited an inverse relationship between the number of competitors in a market and the possibilities for collusion, on the basis that more competitors make it more difficult to reach an agreement. This proposition has been elaborated on and challenged in subsequent game-theoretic literature, including the literature on "super-games".[40] While this literature identifies a range of possibilities and outcomes on the basis of various assumptions regarding the behaviour of market participants, the basic idea that more potential sellers make collusion more difficult continues to command broad support. This reflects the simple fact that the greater the number of sellers, the more difficult it is for them to get together and agree on

[36] Arrowsmith, *Government Procurement in the WTO* , above note 8.
[37] Schooner, above note 6.
[38] George J. Stigler, "A Theory of Oligopoly," *Journal of Political Economy*, 1964, vol. 72, no. 1, pp. 44-61.
[39] William E. Kovacic, Robert C. Marshalll, Leslie M. Marx and Matthew E. Raiff, "Bidding rings and the design of anti-collusive measures for auctions and procurements," in Nicola Dimitri, Gustavo Piga and Giancarlo Spagnolo, *Handbook of Procurement* (Cambridge: Cambridge University Press, 2006), chapter 15.
[40] See Jean Tirole, *The Theory of Industrial Organization* (MIT Press, 1988).

prices, bids, customers and/or territories and (perhaps even more so) to enforce the relevant agreements.

In addition to situations involving a small number of potential sellers, experience points to the following additional circumstances as potentially facilitating collusion:[41]

- The probability of collusion increases where restrictive specifications are used for the product being procured.
- The more standardized a product is, the easier it is for competing firms to reach agreement on a common price structure. By contrast, it is harder to reach an agreement where other forms of competition, such as with respect to design, features, quality, or service, are important.
- The likelihood of collusion can be enhanced by repeat purchases, since the vendors may become familiar with other bidders and recurring contracts provide the opportunity for competitors to share the work.
- Collusion is more likely if the competitors know each other well through social connections, trade associations, legitimate business contacts, or shifting employment from one company to another.[42]
- Collusion is facilitated if bidders have opportunities to meet together in advance of the submission of bids, for last-minute consultations.

As will be elaborated in Part IV below, collusion can also be facilitated by aspects of the procurement process itself. Domestic content requirements or bans on foreign bidders directly limit the set of potential suppliers and thereby diminish the capacity of entry to upset cartel coordination.[43] The unsealing of bids in public for all bidders to observe can enable cartel members to determine whether co-conspirators fulfilled promises either not to bid or to

[41] These points have been adapted principally from US, Department of Justice, above note 63; similar material is available on the websites of several other national competition enforcement authorities.

[42] US Department of Justice, above note 63. Readers familiar with the writings of Adam Smith, *The Wealth of Nations*, 1776, will recall his dictum that "People of the same trade seldom meet together, even for merriment or diversion, but the evening ends in a conspiracy against the public, or in some contrivance to raise prices".

[43] Malcolm B. Coate, "Techniques for Protecting Against Collusion in Sealed Bid Markets," 30 *Antitrust Bulletin*, 1985, 897, 899-90.

submit artificially high "cover bids".[44] This concern provides the rationale for limiting the availability of certain kinds of information in the market, despite general transparency considerations which might otherwise favour releasing it. The use of electronic procurement tools and framework contracts, while offering significant potential gains in efficiency for both suppliers and procuring entities, also pose complex challenges for the maintenance of competition. Advocacy efforts to address these concerns can, therefore, be an important additional element of a successful overall strategy to promote competition and deter collusion in procurement markets.

In reflecting on the above considerations regarding the role of competition in public procurement processes, it is important to acknowledge that the promotion of competition is by no means the only value at play in effective procurement systems. The importance of integrity in such systems has already been discussed. Other values, for example accountability, flexibility and administrative simplicity, are also important. Moreover, there may also be trade-offs involved between competition and these other values.[45] To cite an example that can sometimes be abused, procurements in response to national emergencies may, arguably, justify the suspension of normal competitive procedures.[46] Arrangements such as "framework agreements" can also involve a trade-off between competition and transactional efficiency.[47] The next part of this chapter elaborates on the roles of both international liberalization and national competition (antitrust) policies in promoting competition in such markets.

IV. The roles of international liberalization and national competition laws and policies in ensuring competition in public procurement markets

This part of the chapter examines key tools through which competition can be promoted in national procurement markets. To begin with, and as has already been mentioned, the GPA itself is an important tool for promoting competition. The ways in which it does this are summarized in sub-section A, below. A key premise of this chapter is, however, that while international liberalization – whether via the GPA, a bilateral agreement or unilaterally, is an important tool for enhancing competition in procurement markets, it is

[44] Kovacic et al, above note 39.
[45] Schooner, above note 6.
[46] But cf. the analysis in Schwartz, *this volume*.
[47] See discussion, below.

not, by itself, a *sufficient* tool for ensuring an optimal degree of competition. National competition laws and policies play an essential complementary role in this regard. This role encompasses, at a minimum, the following elements: (i) the adoption and enforcement of effective rules to prevent *collusive tendering*; (ii) *"competition advocacy" activities* that promote the use of sound public contracting procedures and the progressive elimination of regulatory and other barriers to competition; and (iii) *other aspects of the enforcement of competition rules* including the treatment of mergers and joint ventures. These elements are discussed in the remaining sub-sections of this part of the chapter.

A. INTERNATIONAL LIBERALIZATION AS A TOOL FOR STRENGTHENING COMPETITION

Participation in the Agreement on Government Procurement promotes competition in at least four distinct ways.[48] First, it provides a vehicle for the progressive opening of Parties' markets to international competition through market access or "coverage" commitments that are negotiated and incorporated in the schedules contained in Appendix I of the Agreement. Procurement which is "covered" in this way then becomes subject to rules requiring non-discriminatory treatment ("national treatment") of other GPA Parties' goods, services and suppliers. Second, as already noted, the various provisions of the Agreement relating to the provision of information to potential suppliers, contract awards, qualification of suppliers and other elements of the procurement process provide a framework that is intended to ensure transparent and non-discriminatory conditions of competition between suppliers, including both domestic and foreign suppliers.[49] Such measures promote competition by informing suppliers of opportunities to compete and by giving them confidence that bids will be assessed objectively on their merits – thereby enhancing their ability and incentive to bid on specific procurements.

Third, as noted in the discussion on integrity in public procurement in Part II, the Agreement on Government Procurement requires that all GPA Parties put in place national bid challenge systems ("domestic review procedures") through which suppliers can challenge questionable contract awards or other decisions by national procurement authorities. Minimum standards and procedures to ensure the independence and impartiality of the bodies

[48] To some extent, these benefits may also be achieved through participation in bilateral or regional arrangements relating to government procurement policy. See Anderson, Müller, Osei-Lah, Pardo De Leon and Pelletier, *this volume*, chapter __.

[49] Possible tradeoffs between competition and transparency are discussed below.

responsible for such systems are also set out in the Agreement. When fairly administered, such systems enhance supplier confidence that contracts will ultimately be awarded on the basis of product quality and competitive pricing, rather than patronage or cronyism. In this way, they can contribute to a culture of competition on the merits in public procurement markets.[50] Fourth, the GPA provides recourse to the WTO Dispute Settlement Understanding (DSU) in circumstances where Parties believe that international competition has been suppressed through measures taken by other Parties in breach of their GPA commitments. Applicability of the DSU is a standard feature of WTO Agreements. In the area of public procurement, recourse to the DSU has been vastly less extensive than individual bid challenges before national authorities. Such applicability nonetheless represents an essential complement to individual bid challenges as a mechanism for considering systemic matters that may not be adequately addressed in individual bid challenges.[51] A further specific contribution of foreign competition in public procurement markets, whether via the GPA or otherwise, can be to reduce the feasibility of collusion.[52]

B. PREVENTING COLLUSION AMONG SUPPLIERS[53]

Although the opening of national procurement markets either through unilateral action or via negotiations under the WTO Agreement on Government Procurement or other international instruments makes substantially increased competition in procurement markets possible, it does not guarantee this result. Rather, collusive agreements ("cartels" or "bid-rigging") between potential suppliers directly undercut this possibility. For this reason, competition or antitrust rules relating to these practices are an essential counterpart to a liberalized government procurement regime. The WTO Agreement on Government Procurement recognizes the role of such measures, without going as far as requiring Parties to adopt them.[54]

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[50] See, for related discussion, Christopher R. Yukins and Steven L. Schooner, "Incrementalism: Eroding the Impediments to a Global Public Procurement Market," *Georgetown Journal of International Law*, Vol. 38, No. 529, Spring 2007.

[51] For a review of key international disputes under both the current Agreement on Government procurement and its predecessor, the Tokyo Round Code on Government Procurement, see Mitsuo Matsushita, "Major WTO Dispute Cases Concerning Government Procurement," 1 *Asian Journal of WTO and International Health Law and Policy* 299 (2006).

[52] See Part IV(B)(5), below.

[53] See, for complementary discussions and additional information on policy developments in OECD member countries, OECD, *Public Procurement* (Policy Roundtable, 2007); OECD, *Competition in Bidding Markets* (Policy Roundtable, 2006) and OECD, *Competition Policy and Procurement Markets* (Policy Roundtable, 1998).

[54] In particular, Article XV of the Agreement provides for the use of limited tendering procedures in circumstances where the tenders submitted in an open or selective tendering process have been collusive.

(1) Universality of the challenge of deterring collusive practices

Box 3 (next page) presents examples of bid rigging schemes that have been successfully prosecuted in recent years in various jurisdictions including developed, developing and transition economies. Several of the examples (those from China, Indonesia, Peru and Chinese Taipei) are taken from inputs prepared by those countries for the 2001 OECD Global Forum on Competition. These cases demonstrate the universality of the challenge of deterring collusive practices – i.e. such practices are in no way limited either to developed or to developing countries.[55] The cases also illustrate a number of common characteristics of bid rigging schemes. For example, in several of the cases collusion seems to have been facilitated by restrictive regulations and/or practices of the procuring entities. The role of common orthographic errors in the tendering documents of "competing" bidders as a "suspicious sign" – illustrated in the case from Peru – is well known to developed country competition officials.[56]

The cases in Box 3 also illustrate that the mere opening of bidding processes to foreign-based suppliers may not generate effective competition, if effective rules are not in place to deter collusion. The fourth case noted in the table - a conspiracy to rig bids on construction contracts funded by the United States Agency for International Development (USAID) in Egypt – is interesting in that it shows the ability of collusion in tendering processes to impact directly on international assistance efforts. Of course, these are but a few examples of the much larger numbers of bid rigging schemes that have been successfully prosecuted by relevant authorities.

[55] The foregoing is not at all to suggest that the maintenance of competition in developing countries does not involve special issues and challenges. Factors differentiating the role of competition policy in developing as compared to developed countries may include any or all of the following: (a) higher 'natural' entry barriers due to inadequate business infrastructure, including distribution channels, and (sometimes) intrusive regulatory regimes; (b) asymmetries of information in both product and credit markets; (c) a greater proportion of local (non-tradable) markets; and (d) over-stretched/inadequately developed law enforcement and judicial systems. William E. Kovacic, "Institutional Foundations for Economic Legal Reform in Transition Economies: The Case of Competition Policy and Antitrust Enforcement," above note 10, and Anderson and Jenny, above note 10. The point is simply that the problems faced by developing and transition economies in maintaining competition are not wholly dissimilar to those of developed countries and, therefore, that there is much to be gained for both sides in sharing experiences.

[56] See related discussion, below.

Box 3: Examples of international and domestic collusive tendering schemes that have been prosecuted in various jurisdictions

a) International removal and relocation services in Belgium

In 2008, the European Commission imposed fines totalling € 32,755,500 on various large firms providing international removal and relocation services in Belgium for fixing prices, sharing the market and bid rigging, in violation of the EC Treaty's ban on cartels (Article 81). The cartel operated for almost nineteen years. Cartel members fixed prices, presented bogus quotes to clients and compensated each other for lost bids.

Source: "Antitrust: Commission fines providers of international removal services in Belgium over €32.7 million for complex cartel" (EC Commission, Press Release, IP/08/415, 11 March 2008).

b) The International Marine Hose Case

Marine hose is a flexible rubber hose used to transport oil between tankers and storage facilities and buoys. According to court papers and other documents, firms based in the United Kingdom (U.K.), France, Italy, and Japan conspired to fix prices and rig for hundreds of millions of dollars worth of marine hose and related products which was sold to other firms in addition to government agencies. The conspirators met in locations such as Key Largo, Fla., Bangkok, and London. The investigation of this case involved coordinated enforcement efforts by the US Department of Justice, the EC Commission and the UK Office of Fair Trading.

Source: US Department of Justice, "Eight executives arrested on charges of conspiring to rig bids, fix prices, and allocate markets for sales of marine hose," Press Release, May 2, 2007 and "Three United Kingdom Nationals Charges With Participating in Worldwide Bid-Rigging Conspiracy in the Marine Hose Industry," US Department of Justice, Press Release, December 3, 2007.

c) Prosecution of bid rigging in school construction in China

Ten construction companies were prosecuted for bid rigging on contract for the construction of a school building. The ten companies including No.2 Construction Company agreed that No.2 Construction Company would get the contract in exchange for payments to the other companies. They also assigned one of the companies to calculate the bidding prices of all candidates. No.2 Construction Company won the bid at a higher price than before. The administration for industry and commerce issued a decision, declaring that the bid was invalid and the illegal gains were confiscated.

Source: OECD Global Forum on Competition, Summary of cartel cases described by invitees (CCNM/GF/COMP(2001)4, 5 October 2001).

d) Bid rigging on USAID contracts in Egypt

Philipp Holzmann AG, a Frankfurt, Germany construction firm, pleaded guilty and was sentenced to pay a $30-million fine for its participation in a conspiracy to rig bids on construction contracts funded by the United States Agency for International Development (USAID) in Egypt.

Source: U.S. Department of Justice, "German Company Pleads Guilty To Rigging Bids on USAID Construction Contracts in Egypt," (Press Release, 18 August 2000).

e) The rigging of bids for the supply of pipe and pipe-processing services in Indonesia

Three pipe processors were found to have exchanged their prices with each other at a meeting in a hotel the evening before the bids were opened. Material evidence was contained in statements of a complainant, as well as in the testimony of witnesses from the respondents. As this was the first case ever brought by the Commission, no fines or other sanctions were imposed. Instead, the Commission ordered that the contract between Caltex and the apparent lowest bidder be dissolved and that entire tender process be redone.

Source: OECD Global Forum on Competition, Summary of cartel cases described by invitees (CCNM/GF/COMP(2001)4, 5 October 2001).

f) Rigging bids for the supply of construction services in Peru

Three companies were convicted of participating in bid rigging on a contract for the construction of a secondary electricity net in Puerto Maldonado City. The claim was based on evidence from the documents presented by the three bidders. The documents contained the same redaction and the same format; they also presented the same orthographic errors, the same time of construction and almost the same price bid. Following appropriate investigation, the Free Competition Commission ordered the three companies to cease the practice and imposed fines of amount of nearly EUR 1,800 on each of the respondents.

Source: OECD Global Forum on Competition, Summary of cartel cases described by invitees (CCNM/GF/COMP(2001)4, 5 October 2001).

g) The rigging of bids for the procurement of truck-mounted mobile cranes by the Taiwan Power Company in Chinese Taipei

Six companies were prosecuted for having knowingly, and through mutual communications, apportioned the number, suppliers, and amounts of the winning bids before the bid opening. These acts violated Article 14 of the Fair Trade Law, which prohibits concerted acts. The Commission ordered them to cease the concerted practices. The case also included another violation of the Law committed by Taiwan Power Company that improperly restricted the criteria to bid on its contract. The company was ordered to cease its actions.

Source: OECD Global Forum on Competition, Summary of cartel cases described by invitees (CCNM/GF/COMP(2001)4, 5 October 2001).

Bid-rigging in public procurement markets accounts for a striking percentage of prosecutions by competition authorities in jurisdictions where such authorities are well-established. For example, from 1972 through 1992, the U.S. Department of Justice (DOJ) obtained 1159 criminal indictments for Sherman Act violations. Some 625 of these indictments, nearly 54%, attacked collusion against public procurement bodies.[57] The frequency of such cases suggests that suppliers view public bodies as attractive targets for collusive schemes.

[57] These data were collected from the Commerce Clearing House Trade Regulation Reporter for the years in question.

A further point worth emphasizing is that a large proportion of cartel agreements that have been uncovered by the competition authorities of major developed jurisdictions in the past decade (including both collusive tendering for government contracts and price-fixing arrangements not involving government procurement processes) have been international in scope.[58] Such arrangements directly undercut the gains from trade liberalization in addition to impacting directly on the welfare of citizens.[59] They manifest a clear need for international co-operation in the enforcement of competition laws. They are also of interest in that they demonstrate that, contrary to the assumptions of some trade policy practitioners, external market opening alone cannot always ensure vigorous competition in the absence of effective competition laws.[60]

(2) Varieties of collusive tendering

Collusive tendering schemes take a variety of common forms. Probably the most common is "bid rotation", by which suppliers organize their bids to determine which firm will win a contract.[61] The "losers" agree to refrain from bidding or to inflate their bids in the expectation that they will win when their turn comes up. Other common forms of bid rigging include "complementary bidding", in which some competitors agree to submit bids that either are too high to be accepted or contain special terms that will not be acceptable to the buyer, and "bid suppression", in which one or more competitors who otherwise would be expected to bid, or who have previously bid, agree to refrain from bidding or withdraw a previously submitted bid so that the designated winning competitor's bid will be accepted. The low bidder often secures support for the plan by giving its co-conspirators side payments or subcontracts.[62] All such schemes have at least one element in common, namely an agreement

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[58] See Levenstein and Suslow, above note 34; Julian Clarke and Simon J. Evenett, "A multilateral framework for competition policy?," in State Secretariat of Economic Affairs and Simon Evenett, *The Singapore Issues and the World Trading System: the Road to Cancun and Beyond* (Bern: State Secretariat for Economic Affairs); and Simon J. Evenett, Margaret Levenstein and Valerie Suslow, 'International cartel enforcement: lessons from the 1990s', *The World Economy*, vol. 24, iss. 9, 2001, pp. 1221-45.

[59] Anderson and Jenny, above note 10.

[60] Cf. Alan Winters, 'Doha and world poverty targets," World Bank, mimeo, 2002 and Richard Blackhurst, 'Trade Policy is Competition Policy', in *Competition and Economic Development*, OECD: 1991.

[61] Representative illustrations include United States v. Dynalectric Co., 859 F.2d 1559 (11th Cir. 1988); United States v. Northern Improvement Co., 814 F.2d 540 (8th Cir. 1987); United States v. A-A-A Electrical Co., 788 F.2d 242 (4th Cir. 1986); United States v. Portsmouth Paving Corp., 694 F.2d 312 (4th Cir. 1982).

[62] *See* United States v. All Star Indus., 962 F.2d 465 (5th Cir. 1992). The use of side payments to facilitate bid rotation conspiracies is common where contractors face each other regularly, such as bidding for highway paving contracts. *See, e.g.*, United States v. A-A-A Electrical Co., 788 F.2d 242 (4th Cir. 1986); United States v. Inryco, Inc., 642 F.2d 290, 292 (9th Cir. 1981); *David Thompson*, 621 F.2d at 1149-50; *Azzarelli Construction*, 612 F.2d at 297.

between some or all of the bidders that limits or eliminates competition between them and (normally) predetermines the winning bidder.[63] Additional information on specific forms of bid rigging is summarized in Box 4.

Box 4: Basic Types of Collusive Tendering

Bid Suppression: In bid suppression schemes, one or more competitors who otherwise would be expected to bid, or who have previously bid, agree to refrain from bidding or withdraw a previously submitted bid so that the designated winning competitor's bid will be accepted.

Complementary Bidding: Complementary bidding (also known as "cover" or "courtesy" bidding) occurs when some competitors agree to submit bids that either are too high to be accepted or contain special terms that will not be acceptable to the buyer. Such bids are not intended to secure the buyer's acceptance, but are merely designed to create a (false) appearance of genuine competitive bidding.

Bid Rotation: In bid rotation schemes, all conspirators submit bids but take turns being the low bidder. The terms of the rotation may vary; for example, competitors may take turns on contracts according to the size of the contract, allocating equal amounts to each conspirator or allocating volumes that correspond to the size of each conspirator company.

Subcontracting as a compensating mechanism: Competitors who agree not to bid or to submit a losing bid frequently receive subcontracts or supply contracts in exchange from the successful low bidder. In some schemes, a low bidder agrees to withdraw its bid in favour of the next lowest bidder in exchange for a subcontract that divides the illegally-obtained higher price between them. Note, however, that sub-contracting is not necessarily anti-competitive if it is not done in furtherance of efforts to limit competition in the award of the main contract.

Source: Adapted from U.S., Department of Justice, "Price-Fixing, Bid-Rigging and Market Allocation Schemes: What They Are and What to Look For" (available on the internet at http://www.usdoj.gov/atr/public/guidelines/211578.htm).

(3) Estimates of the price impact of collusion in public procurement processes

Collusion adds directly to the price paid by procuring entities for goods and services procured. An obvious question of interest is the extent of the premium that is paid. One of the more sophisticated estimates was done by Froeb et al using data from an investigation of the rigging of bids for the supply of frozen seafood to the US Department of Defense. They found, with a high degree of statistical confidence, that the rigging of bids had raised the

[63] See, for a useful overview, U.S., Department of Justice, "Price-Fixing, Bid-Rigging and Market Allocation Schemes: What They Are and What to Look For," (available on the internet at http://www.usdoj.gov/atr/public/guidelines/211578.htm).

price paid by the Department by 23.1 % (this was the smallest point estimate).[64] This is broadly in line with more recent estimates of the costs of cartelization in international markets.[65] In their analysis of the price impact of international cartels, Levenstein and Suslow report a median cartel overcharge for all types of cartels of 25%; and one of 32% for international cartels (the overcharge is calculated by comparing cartel prices to a competitive benchmark).[66] Clearly, the costs of cartelization (and, therefore, the potential benefits of anti-cartel enforcement) are substantial.[67]

(4) The deterrence of collusive tendering through competition law enforcement

A pre-requisite for the deterrence of collusive tendering is an effective legal prohibition of such conduct, normally in a national competition or antitrust law.[68] (Reference is made here to "deterring" rather than "preventing" collusion since it is probably impossible to eliminate such conduct altogether.) Often, bid rigging in public procurement processes is prohibited through general antitrust provisions against cartels or conspiracies in restraint of trade;[69] however, it can also be the subject of legal provisions that focus specifically on collusion in public procurement markets.[70] In some jurisdictions, bid rigging can also trigger penalties under statutes aimed at the prevention of fraud. To be effective, legal prohibitions against collusive tendering should be backed up by an effective enforcement regime and by appropriate sanctions (penalties) including heavy fines and, in the view of many experts, prison sentences.[71] In transition economies, such a prohibition serves an important purpose by making clear that the government will not tolerate private efforts to recreate collective

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[64] Froeb, Koyak and Werden, above note 34.

[65] See, e.g., John M. Connor, "Price-Fixing Overcharges: Legal and Economic Evidence", SSRN Working Paper, 2005, Available at: http://ssrn.com/abstract=787924.

[66] Levenstein and Suslow, above note 34.

[67] Clarke and Evenett have shown, the resource saving that can be generated by only a marginal reduction in bid rigging on government contracts (e.g., on the order of 1%) is greater than the average annual operating budget of the competition agency in most countries, often by a factor of several times over. Clarke and Evenett, above note 58, p. 127.

[68] More than one hundred countries now have such laws.

[69] This is the case, for example, in the United States and the European Community.

[70] This is the case, for example in Canada, where bid rigging can, depending on the circumstances, be dealt with under either a specific provision of the *Competition Act* which addresses bid rigging as such or under the more general provision on conspiracies in restraint of trade.

[71] See OECD, *Fighting Hard-Core Cartels – Harm, Effective Sanctions and Leniency Programme*, OECD, 2002; see also Richard Whish, "Control of Cartels and Other Anti-competitive Agreements," in Vinod Dhall, *Competition Law Today: Concepts, Issues and the Law in Practice* (New Delhi: Oxford University Press, 2007), chapter 1.

planning techniques that the country has abandoned. There are indications that the effective prohibition of "naked" or "hardcore" cartels is becoming an internationally accepted norm.[72]

Enactment of an appropriate competition law provision prohibiting bid rigging and other collusive arrangements is only the beginning. Recent efforts to deter such arrangements through effective enforcement of relevant statutory provisions have taken two main forms. First, sanctions for culpable parties have been substantially increased.[73] Convictions in bid rigging cases can now result in significant penalties. In the US, for corporate defendants, the Sherman Act now sets a maximum fine of $100 million. Corporate violators also may be fined up to the greater of twice the firm's gross pecuniary gain from the violation or twice the gross pecuniary loss by victims.[74] Individuals may be fined up to $1,000,000, twice the pecuniary loss by victims, or twice the defendant's gross pecuniary gain from the violation, whichever is greatest.[75] Individuals also may be sentenced to as many as ten years in prison. If it brings a civil suit to enforce the Sherman Act, the DOJ may seek an injunction or may obtain treble damages for injury the federal government has suffered as a purchaser. Under the Civil False Claims Act,[76] the Department may seek treble damages in cases of collusive bidding and, even when no actual damages can be proven, may obtain civil penalties of up to $10,000 for each separate voucher or invoice submitted under a government contract tainted by collusion. State governments injured in their capacity as purchasers also have standing to seek treble damages. In broad terms, the trend to impose heavy penalties on defendants in cases of bid rigging and collusive tendering has been progressively replicated in other jurisdictions such as the European Communities and Canada.

Antitrust violations involving bid-rigging can also result in a contractor's suspension or debarment. In the US, Federal Acquisition Regulation (FAR) 9.407-2(a)(2) permits the

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[72] Harry First, The Vitamins Case: Cartel Prosecutions and the Coming of International Competition Law, 68 *Antitrust Law Journal* 711 (2001) (prosecution of vitamins cartel suggests broader international acceptance of anti-cartel norm). The deterrence of hardcore cartels was also a major focus of work in the WTO Working Group on the Interaction between Trade and Competition Policy when that body was active. See *Report (2002) of the WTO Working Group on the Interaction between Trade and Competition Policy to the General Council* (WT/WGTCP/6), paragraphs 47-64, available on the internet at http://www.wto.org/english/tratop_e/comp_e/wgtcp_docs_e.htm.

[73] The expansion of antitrust sanctions for cartel behavior is traced in Stephen Calkins, "Corporate Compliance and the Antitrust Agencies' Bi-Modal Penalties," 60 *Law & Contemporary Problems* 127 (1997); Wouter P.J. Wils, "Is Criminalization of EU Competition Law the Answer?" 28 *World Competition: Law and Economics Review* (2005).

[74] 18 U.S.C. § 3623 (1994).

[75] *Id.* at § 3623.

[76] 31 U.S.C. §§ 3729-31 (1994).

purchasing agency to suspend contractors suspected of a violation of "Federal or State antitrust statutes relating to the submission of offers" and states that an indictment for antitrust violations "constitutes adequate evidence for suspension."[77] The entry of a criminal conviction or civil judgment for violating federal or state antitrust statutes relating to the submission of offers creates grounds for debarment.[78]

A second important tool for the deterrence of bid rigging has been to provide inducements for cartel participants to inform government competition agencies of wrongdoing through so-called leniency programs. In broad terms, such programs encourage cartel members to come forward, confess to their activities and assist the competent authorities in investigating and prosecuting their fellow cartel members. In exchange, they receive amnesty for their own behavior. Normally, only one company (the "first in") can qualify for leniency.

Leniency programs for co-operation in anti-cartel enforcement cases were introduced in the US in the 1980s and progressively strengthened through the 1990s.[79] Following the lead of the United States, the European Commission adopted such a programme in 1996.[80] The Commission's initial Leniency Notice, which was not as successful as expected, was replaced by a new one in 2002.[81] The main change was that, once a firm was admitted to the programme, immunity became automatic. Subsequently, the European Commission and all EC Member States adopted a model leniency programme developed within the European Competition Network (a network linking all competition authorities in the Community).[82] As

[77] 48 C.F.R. § 9.407-2(a)(2).

[78] 48 C.F.R. § 9.406-2(a)(2).

[79] On the development and operation of modern leniency programs, see Joe Chen & Joseph E. Harrington, Jr, "The Impact of the Corporate Leniency Program on Cartel Formation and the Cartel Price Path," in *Political Economy of Antitrust* (Vivek Ghosal & Johan Sennek eds.); Julian M. Joshua, "Leniency in U.S. and EU Cartel Cases," Antitrust, vol. 14, no. 3, at 19 (Summer 2000) (comparing U.S. and EU leniency programs); Donald C. Klawiter, "Corporate Leniency in the Age of International Cartels: The American Experience," *Antitrust*, vol. 14, no. 3, at 13 (Summer 2000) (describing development of U.S. leniency policy); and Massimo Motta & Michele Polo, "Leniency Programs and Cartel Prosecution," 21 *International Journal of Industrial Organization* 347 (2003). Regarding leniency programs in the European Community, see Robert D. Anderson and Alberto Heimler, " What has Competition Done for Europe? An Inter-Disciplinary Answer, " *Aussenwirtschaft*, 62. Jahrgang (2007), Heft IV, pp. 419-454.

[80] Commission Notice on the non-imposition or reduction of fines in cartel cases, *Official Journal C 207*, 18 July 1996 pp. 4 – 6.

[81] Commission notice on immunity from fines and reduction of fines in cartel cases, *Official Journal C 45*, 19 February 2002, pp. 3-5.

[82] Internet: http://ec.europa.eu/comm/competition/cartels/legislation/leniency_legislation.html.

a result, the Commission programme was again amended in 2006, mainly to clarify the type and quality of information to be provided by leniency applicants.[83]

US enforcement authorities stress the following three characteristics as being critical to the success of leniency programs. First, there must be severe sanctions in place for firms and individuals that do not obtain amnesty. Without this, the incentive to cooperate will not be present. Second, there must be a genuine fear of detection, based on a credible possibility that illegal behaviour will be detected, prosecuted and sanctioned. Third, there must be predictability and transparency to the amnesty program such that potential applicants a high degree of assurance that, if they take the risk of coming forward, they will get the reward.[84]

In addition to the foregoing measures (effective sanctions and leniency programmes to induce cooperation), enforcement agencies also stress the importance of procurement personnel being alert to various "suspicious signs" that may signal the presence of collusion. A number of these are set out in Box 5. To be sure, the involvement of competition agencies (or, where appropriate, police or other investigatory authorities) is generally necessary to the investigation and prosecution of bid rigging. However, it is the procurement officials who are most likely to be in a position to observe behaviour that may indicate the presence of collusion. Consequently, training programs to enhance procurement officials' "collusion-awareness" are an important adjunct to the enforcement of competition law by the responsible authorities.

[83] Commission notice on immunity from fines and reduction of fines in cartel cases, Official Journal C 298, 8 December 2006, pp. 17-22.

[84] Thomas O. Barnett, "Criminal Enforcement of Antitrust Laws: The U.S. Model" (Remarks before the Presented at the Fordham Competition Law Institute's Annual Conference on International Antitrust Law and Policy New York, New York, September 14, 2006).

Box 5. Suspicious signs: behaviour that may signal the presence of collusive tendering

a) Potentially suspicious bid patterns

- The same suppliers submit bids and each company seems to take a turn being the successful bidder.
- Some bids are much higher than published price lists, previous bids by the same firms, or internal agency cost estimates.
- Fewer than the normal number of competitors submit bids.
- A company appears to be bidding substantially higher on some bids than on other bids, with no apparent cost differences to account for the disparity.
- Bid prices drop whenever a new or infrequent bidder submits a bid.
- A successful bidder routinely subcontracts work to competitors that submitted unsuccessful bids on the same project.
- A company withdraws its successful bid and subsequently is subcontracted work by the new winning contractor.

b) Suspicious Statements and Behaviour

- Bid proposals or forms submitted by different vendors contain common features or irregularities (e.g. identical calculations, spelling errors, handwriting or typeface that suggest they may have been prepared jointly).
- A company requests a bid package for itself and a competitor or submits both its own and another company's bids.
- A company submits a bid when it is incapable of successfully performing the contract (this may be a complementary bid).
- A company brings multiple bids to a bid opening and submits its bid only after determining who else is bidding.
- A bidder or salesperson makes: (a) any reference to industry-wide or association price schedules; (b) statements indicating advance knowledge of competitors' pricing; (c) statements to the effect that a particular contract or project "belongs" to a certain vendor; or (d) statements indicating that a particular bid was only submitted as a "courtesy," "complementary," "token," or "cover" bid.

NB: It should be emphasized that the foregoing are merely signs that may trigger suspicions; they are not, by themselves, proof of collusion.

Source: Adapted from U.S. Department of Justice, "Price-Fixing, Bid-Rigging and Market Allocation Schemes: What They Are and What to Look For" (available on the internet at http://www.usdoj.gov/atr/public/guidelines/211578.htm).

The deterrence of bid rigging can also be facilitated by legal requirements to inform the enforcement authorities of apparent violations. In the US, federal procurement statutes

and regulations require executive agencies to notify the Department of Justice (DOJ) about bids or proposals that indicate antitrust violations.[85] Another potentially very useful practice – perhaps particularly so in developing jurisdictions where there may be limited awareness of the requirements of competition law within the business community – is to require contractors to certify that they have set their prices independently. In the US, this is done through the requirement for a "Certificate of Independent Price Determination".[86] Where appropriate, basic information on relevant competition law provisions can be provided with tender documentation. Another basic tool for guarding against the possibility of collusion involves the preparation of an internal estimate of the competitive-market cost of significant projects, as a benchmark to evaluate the possibility of collusive overcharges. It must be acknowledged, however, that such estimates are only useful to the extent that they accurately reflect actual market conditions. Finally, it should be noted that the detection of bid rigging can also be facilitated by econometric tools that can assist in the identification of suspicious bidding patterns.[87]

Competition law enforcement relating to collusive tendering does not take place in a vacuum. As already noted, other laws and policies – including, very much, those pertaining to tendering processes – can either facilitate or help to prevent collusion. Domestic content requirements directly limit the set of potential suppliers and thereby diminish the capacity of entry to upset cartel coordination. The unsealing of bids in public for all bidders to observe can enable cartel members to determine whether co-conspirators fulfilled promises either not to bid or to submit artificially high "cover bids". The use of electronic procurement tools and framework contracts, while offering significant potential gains in efficiency for both suppliers and procuring entities, also pose complex challenges for the maintenance of competition. Advocacy efforts to address these concerns are, therefore, an important adjunct to law enforcement in this area. Such efforts are the focus of the next sub-section of this chapter.

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[85] The statutory requirement appears in 10 U.S.C. § 2305(b)(9) (1994) and 41 U.S.C. § 253b(i) (1994). Section 3.303(a) of the Federal Acquisition Regulations directs agencies to notify the Attorney General of evidence of collusive bidding. 48 C.F.R. § 3.303(a). FAR 3.301(b) requires agency personnel to refer instances of identical bids in advertised bidding to the Attorney General and to supply evidence of suspected antitrust violations to the agency office responsible for debarring and suspending contractors. 48 C.F.R. § 3.301(b).

[86] *See* FAR 3.103-1, 48 C.F.R. § 3.103-1 (solicitations for firm-fixed-price contracts must include Certificate of Independent Price Determination, by which supplier declares that it set its prices "independently").

[87] See, e.g. Robert H. Porter & J. Douglas Zona, Detection of Bid Rigging in Procurement Auctions, 101 Journal of Political Economy 518 (1993); Robert H. Porter & J. Douglas Zona, Ohio School Milk Markets: An Analysis of Bidding (NBER Working Paper No. 6037: May 1997).

C. COMPETITION ADVOCACY AND EDUCATION: FOSTERING SUPPORT FOR PRO-COMPETITIVE PROCUREMENT REGIMES AND ADDRESSING REGULATORY BARRIERS/OTHER GOVERNMENT MEASURES THAT IMPEDE COMPETITION

Competition agencies – and other public interest-oriented institutions such as research institutes and policy think-tanks - can play an important role in regard to the reform of government measures affecting competition. This is recognised in many jurisdictions, where competition agencies engage in "advocacy" activities (e.g., research, analysis, submissions to parliamentary bodies, etc.) aimed at influencing the evolution of government policies and raising awareness of restraints on competition. There is, in fact, a growing recognition that such work is of critical importance, co-equal in many circumstances with the competition law enforcement function.[88]

Three main areas can be identified for competition advocacy activities aimed at promoting competition in public procurement markets: *first*, general public education efforts aimed at building support for the institutions of a healthy market economy, including sound public contracting rules and procedures; *second*, efforts aimed at modifying or eliminating specific aspects of procurement policy and regulations that may (intentionally or inadvertently) suppress competition; and *third*, broader efforts to modify or reduce sectoral and/or cross-sectoral policies that are not specifically concerned with procurement but which affect the scope for competition in public procurement markets. These might include licensing or other restrictions on entry or participation in markets and cross-sectoral or "framework" laws and policies that unnecessarily make it more difficult for firms to compete.[89] Each of these categories merits elaboration.

(1) General public education efforts aimed at building support for the institutions of a healthy market economy, including transparent and competitive contracting procedures

[88] The importance of competition advocacy activities as a complement to competition law enforcement is emphasized in the competition-related work of the OECD and the WTO. See also Kovacic, "Institutional Foundations for Economic Legal Reform in Transition Economies: The Case of Competition Policy and Antitrust Enforcement," above note 10 and Anderson and Jenny, above note 10.

[89] This is not at all to suggest that regulation does not have a legitimate role to play as an element of governance; on the contrary, it is well established that regulation of one kind or another can serve an important role in remedying market failures whether due to the existence of externalities, asymmetries of information or "natural monopolies". The challenge for competition agencies and other "competition advocates" is to identify situations where regulation has been imposed in the absence of a valid market failure rationale, or the degree or nature of regulation is counter-productive.

An important aspect of competition advocacy concerns basic public education regarding the institutions of a healthy market economy. To have positive long-lived effects, procurement and other economic policy and legislative reforms ultimately must command public support. In this regard, competition advocates can be a catalyst for debate about the appropriate role of government intervention in the economy and the correct choice of strategies for conducting procurements. Performing the education function before constituencies outside the government can help to build a political constituency for market-oriented policies.

In the current economic environment, an important dimension of such advocacy may be to ensure that public infrastructure spending programmes follow proper contracting procedures and thereby maximize long-run value to citizens. The economic downturn of 2008-09 has triggered increased emphasis on public infrastructure spending as an element of economic stimulus packages, not only in the United States but around the globe. Yet the public benefits to be created through infrastructure spending – which presumably will last well beyond the current recession – depend very importantly on adherence to procurement procedures that ensure vigorous competition in markets and accountability for the use of public funds. Indeed, a time of greater-than-usual public procurement/infrastructure investment would seem to be a critical time for ensuring that proper procedures are followed to ensure competitive and transparent contracting.[90] Competition advocates and procurement authorities have a common interest in fostering a consensus to this effect.

Competition advocacy in transition and developing economies raises special issues. While such economies often have the most pressing needs for upgrading of national transportation and other infrastructure, they may also suffer from a legacy of corruption and clientism in state procurement policies that undercuts efforts at modernization and renewal.[91] A common path of reform efforts in such economies is to engage the elites - public sector and private sector professionals who often have gained formal training in Western universities or held positions that provide extensive contact with Western market institutions. While

[90] See Steven L. Schooner and Christopher R. Yukins, "Public Procurement: Focus on People, Value for Money and Systemic Integrity, Not Protectionism," George Washington University Law School Legal Studies Research Paper No. 460, 2009. Robert D. Anderson, "Remarks to the 2010 West Government Contracts Law in Review Conference," 5 January 2010 and "Public works: filling the hole," *The Economist*, December 13, 2008, p. 16.

[91] See, generally, Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton University Press, above note 14.

understandable, this approach has its limitations. Extending participation in and support for the reform process beyond the elites, to the larger body of citizens who live in extreme poverty or are politically disaffected, requires conscious efforts to increase public awareness of the rationales for reform and the encouragement of public participation in the design and implementation of specific measures.

As already noted, a particularly important audience for consciousness-raising concerning the importance and maintenance of competition concerns contracting personnel – i.e. staff members of purring entities – who should be well-informed regarding the risks of collusion, the harm that it causes and the means of preventing it.[92] The prevention of collusion in the procurement process also requires effective co-operation between procurement and competition agencies. For these purposes, competition agency staff can be invited to participate in training seminars for procurement officials that include modules on the detection and prevention of bid rigging, or can otherwise work with procurement officials to help ensure a high level of awareness.[93]

(2) Advocacy efforts focused on procurement policies and regulations that can limit competition

Public procurement policies can limit competition and even assist firms in behaving anti-competitively in at least two ways. A first way is to restrict entry into procurement markets, particularly by imposing domestic or local content rules that exclude potential bidders. A majority of countries have policies that favour their domestic suppliers in regard to at least some aspects of their public procurement. A second area of possible concern involves procedures that aim to increase the integrity of the procurement system but may also

[92] OECD, *Third Report on the Implementation of the 1998 Recommendation*, at 21 (finding that "in many countries procurement authorities and officials are not yet sufficiently aware of the danger of cartels among companies participating in bidding procedures and of the imiportant role they can play in preventing and detecting cartels.").

[93] Training seminars and workshops on government procurement which are presented by the WTO Secretariat for relevant officials pursuant to the Secretariat's annual technical assistance plan also typically include a module on the detection and prevention of collusive tendering, on the basis that this is important to ensure that the goals of procurement liberalization are not undercut by such activities. See, for related details, the discussion at http://www.wto.org/english/tratop_e/gproc_e/gptech_coop_e.htm .

have the unintended effects of limiting entry and facilitating supplier coordination.[94] For example, expansive civil and criminal strictures against fraud in public procurement markets that create asymmetries between public and private contracting can discourage firms from serving public purchasers.[95]

A further important example concerns the process for opening bids in sealed bid procurements. Typically, bids are unsealed in public and displayed for all bidders to observe.[96] While widely seen as being important as an anti-corruption measure, this process can also facilitate collusion by enabling cartel members to determine whether co-conspirators fulfilled promises either not to bid or to submit artificially high "cover bids" (recall the discussion in Part IV:B, above). A possible reform, in this regard, could be to permit the private inspection of bids by a guardian inside the purchasing agency, such as an inspector general. Such a measure could impede efforts by cartel members to detect cheating without undermining the integrity of the award process.[97]

The foregoing also raises possible issues in regard to the above-discussed OECD principles and recommendations for the promotion of integrity in public procurement. While, as we have emphasized, in general transparency (OECD principle 1) enhances competition and provides a level playing field for competing suppliers, too liberal dissemination of information may also result in enhanced opportunities for collusion among suppliers. For example, information on procurement planning (addressed in OECD principle 3) may be used by suppliers e.g. to prepare bid rotation schemes and similar forms of anti-competitive practices. Therefore, a balance will have to be sought between transparency standards that are necessary to discourage corruption and the requirements of competition.

Developments in procurement methodologies, including the increasing use of electronic procurement tools, reverse auctions and framework contracts, while offering

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[94] See, generally, OECD, *Competition Policy and Procurement Markets* (Paris: DAFFE/CLP/(99)3FINAL, 1999).

[95] William E. Kovacic, "The Civil False Claims Act as a Deterrent to Participation in Public Procurement Markets,"6 *Supreme Court Economic Law Review*, 1998, 201.

[96] John Cibinic Jr. & Ralph C. Nash, Jr., *Formation of Government Contracts* 522-25 (3d ed. 1998).

[97] As stated by Kovacic et al, "If an auctioneer with first-price sealed bidding reveals the amounts of the bids of all the bidders, then the problem that a bidding ring faces in policing the bids of its members is made much easier. In general, the less information provided on auction outcomes, the more difficult it is for a bidding ring to operate. Unfortunately, in many settings it will be impossible to hide the identity of the winner, but

significant potential gains in efficiency for both suppliers and procuring entities, also pose complex challenges for the maintenance of competition. For example, electronic procurement tools (e.g. electronic reverse auctions) are capable of being used to facilitate collusion if potentially competing firms gain access to each other's bids. One key here is to ensure a high degree of confidentiality of individual bids prior to the contract award.

Similarly, the use of "framework agreements" or "frameworks" (sometimes also known as two-stage contracting) as a public contracting tool, while capable of generating important transactional efficiencies, can also pose significant challenges with respect to the maintenance of competition, accountability and non-discriminatory procurement processes. While the usage of the term "frameworks" can vary across jurisdictions, a broad definition would include the following elements:

> "(a) The solicitation of tenders or offers against set terms and conditions;
>
> (b) The submission of tenders indicating the terms (e.g. price) on which different suppliers are willing to supply;
>
> (c) Chosen supplier(s) and the procuring entity entering into a "framework agreement" on the basis of the tenders; and
>
> (d) Subsequent placing of periodic orders (to conclude procurement contracts) with the supplier(s) under the terms of the "framework agreement", as particular requirements arise." [98]

Such contracts account for a large and increasing proportion of overall procurement activity in major jurisdictions.[99]

Ongoing work on the issue of framework agreements in the context of the revision of the UNCITRAL Model Law on Procurement encompasses important concerns regarding their implications for the maintenance of competition and transparency, in addition to recognition

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certainly the full range of bids with first-price sealed bidding need not be revealed." Kovacic et al, above note 39.

[98] See Sue Arrowsmith and Caroline Nicholas, "Regulating framework agreements under the UNCITRAL Model Law on procurement," in S.Arrowsmith (ed.), *Procurement Regulation for the 21st Century: Reform of the UNCITRAL Model Law on Public Procurement*, forthcoming, West; 2009, chapter 2. The US concept of "Indefinite Delivery/Indefinite Quantity" or "ID/IQ" contracts is a type of framework agreement. See, for useful background, Daniel I. Gordon and Jonathan L. Kang, "Task-Order Contracting in the U.S. Federal System: The Current System and Its Historical Context," mimeo, May 2007.

[99] According to Yukins and Schooner, as much as 40 % of the approximately $400 billion US federal procurement market is administered through such inter-agency framework agreements. Yukins and Schooner, above note 50.

of the efficiency benefits that they can bring. Summarizing the thrust of this work, Arrowsmith and Nicholas observe as follows:

> "... it is also recognized that without precise and adequate controls the operation of frameworks can inflict undue damage on the twin principles of competition and transparency that underlie the Model Law. It has therefore been sought to devise a careful system for operating frameworks that preserves these twin principles throughout. Of particular note is the fact that the UNCITRAL system will provide for a clearly defined transparent and competitive procedure for placing orders under a framework agreement – a process that has not always been clearly regulated and adequately controlled in national procurement systems and which seems to present particular dangers. This will be allied to measures that require procuring entities to provide information on awards they have made and that apply the supplier complaints system to orders under a framework. In this way, states that implement the Model Law are encouraged to reap the benefits of framework agreements whilst reducing the risks that frameworks may present for transparent and competitive procurement."[100]

An important question for competition advocates and trade liberalization bodies is whether further work on these issues is needed in the framework either of national competition policies or of trade instruments.

(3) Efforts to address regulatory and other obstacles to competition that are not specifically linked to the procurement process, but which nonetheless impact on competition in public procurement markets

Regulatory obstacles to competition that are not specifically linked to the procurement process, but which can nonetheless impact on competition in public procurement markets are of two main kinds: (i) industry-specific measures; and (ii) cross-sectoral or "framework" laws and policies. With regard to the former, such measures include a wide range of licensing and other requirements that impede entry to markets, for example by imposing excessive financial solvency requirements. The anti-competitive effects that such requirements can entail have long been recognized. Experience in both developed and developing countries shows that, in many cases, rather than having regulation imposed on them for the public benefit, incumbent firms have sought regulation for their own benefit, for the purpose of limiting entry into the industry and helping them to enjoy higher prices for

[100] Arrowsmith and Nicholas, above note 98. See also Caroline Nicholas, "Framework Agreements and the UNCITRAL Model Law on Procurement," *Public Procurement Law Review*, 2008, Number 5, pp. NA20-30.

their products.[101] Recognition of the significance of such conduct as a barrier to economic development dates back at least to Krueger's classic analysis,[102] and is affirmed in recent analyses by the World Bank and other development-related agencies.

The impact of regulatory obstacles to competition has also received attention in the context of international trading arrangements. For example, in the 1998 Report of the WTO Working Group on the Interaction between Trade and Competition Policy the following views were expressed regarding the significance of such obstacles:

> "The following examples of regulatory situations having adverse effects on competition ... were advanced: outmoded or unnecessary regulations; a failure by countries to recognize each others' technical standards; state zoning laws or sanitary and phytosanitary requirements that limited entry unnecessarily or served as disguised tools for excluding competing suppliers; legal systems that facilitated strategic use of the courts by firms to harass competitors; and discriminatory R&D funding practices. It was suggested that the regulations that needed to be reviewed could be classified as follows: regulation that openly discriminated in favour of domestic suppliers; regulations that were non-discriminatory on the surface but subtly discriminatory in their substantive requirements; regulations that simply were no longer needed; and poorly designed regulations that were desirable in principle but unnecessarily intrusive."[103]

Any or all of the above-noted regulatory measures can be an appropriate focus for competition advocacy activities.

D. OTHER ASPECTS OF COMPETITION LAW BEARING ON PUBLIC PROCUREMENT MARKETS

Competition in public procurement markets is also affected by other aspects of competition law and policy. A first important example relates to the treatment of *mergers and joint ventures*. In the absence of effective legal provisions to prohibit anti-competitive mergers, competing firms can directly circumvent competition by merging their operations. This is a clear alternative to the use of bid rigging or similar agreements. In the event that firms desire to maintain distinct identities, joint ventures can be formed for the purpose of bidding on specific procurements. The effective regulation of anti-competitive mergers and joint ventures is a challenging problem, in that by no means all such arrangements are anti-

[101] The classic diagnoses of this problem are provided in George J. Stigler, 'The theory of economic regulation', *Bell Journal of Economics and Management Science* 2(1): Spring 1971, 3–21; and William A. Jordan, "Producer protection, prior market structure and the effects of government regulation," *Journal of Law and Economics* XV(1): April 1972, 151–76.

[102] Krueger, above note 15.

[103] WTO, Report (1998) of the Working Group on the Interaction between Trade and Competition Policy (WT/WGTCP/2), p. 36.

competitive. Rather, a majority are likely to be either pro-competitive (i.e. likely to strengthen rivalry through cost savings and synergies) or at least neutral in their effects.[104] Effective tools must be developed to distinguish those arrangements that are likely to harm competition from the others.

Antitrust rules dealing with *single-firm monopolization and/or abuse of dominant position* can also play a role in regard to public procurement markets.[105] One area in which such rules may come into play relates to privatization. Economic law reform programs commonly involve the privatization of state-owned assets through various forms of auctioning mechanisms. Such programs often raise significant competition policy issues. Without adequate attention to competition concerns, the strategy and methods chosen to alienate assets may simply transform state-owned monopolies into durable privately held monopolies.[106]

Competition policy oversight in the post-privatization period can help the public reap the benefits of placing such assets into the private sector. For example, where the government dissolves a monolithic public enterprise into a number of privately-owned successor firms, the successors may seek to use mergers, holding companies, or other institutional arrangements to re-establish the monopoly structure of the public ownership era. Some forms of consolidation or cooperation will increase efficiency by enabling the participants, for example, to realize scale economies or link complementary assets. Competition policy oversight of outright consolidations or cooperation by contract can help ensure that such measures are not mere efforts to create a private variant of the predecessor public monopoly.

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[104] In countries with mature competition regimes, typically only a small percentage (1% or less) of mergers are deemed anti-competitive. See Robert D. Anderson and S. Dev Khosla, *Competition Policy As a Dimension of Economic Policy: A Comparative Perspective* (Industry Canada Occasional Paper, 1995).

[105] See, for a recent review of relevant US rules and enforcement approaches, U.S. Department of Justice, *Competition and Monopoly: Single-Firm Conduct Under Section 2 of the Sherman Act* (2008); see also William E. Kovacic, "Modern U.S. Competition Law and the Treatment of Dominant Firms: Comments on the Department of Justice and Federal Trade Commission Proceedings Relating to Section 2 of the Sherman Act" (available on the internet at http://www.ftc.gov/os/2008/09/080908section2stmtkovacic.pdf). Related perspectives are provided in William E. Kovacic, "The Intellectual DNA of Modern U.S. Competition Law for Dominant Firm Behavior: The Chicago/Harvard Double Helix," 2007 Columbia Business Law Review, pp. 1-82 and in William E. Kovacic, "Designing Antitrust Remedies for Dominant Firm Misconduct", *Connecticut Law Review*, vol. 31, 1999, pp. 1285-1319. The evolution of corresponding approaches in the European Community is discussed in Anderson and Heimler, above note 79; and in Robert D. Anderson and Alberto Heimler, "Abuse of Dominant Position: Enforcement Issues and Approaches for Developing Countries," in Dhall, ed., above note 71, chapter 2, pp. 59-92.

[106] J.J. Laffont, *Regulation and Development* (Cambridge University Press, 2005).

V. Concluding remarks

Ensuring good governance in relation to public procurement systems (and thereby maximizing value for money for taxpayers) requires the addressing of two distinct but inter-related challenges: (i) ensuring integrity on the part of public officials administering the procurement processes; and (ii) promoting *competition* and preventing *collusion* among alternative suppliers. Both corruption and collusion undermine the intended benefits of procurement reforms and international liberalization via the WTO Agreement on Government Procurement. Although they may sometimes occur together, they are also analytically distinct problems that each merit attention in their own right.

Corruption in public procurement systems has rightly been condemned as a barrier to development and a scourge on the welfare of citizens in developing and developed countries alike. Such practices - which can also be viewed as an example of the more generic phenomenon of "rent-seeking" – are intrinsically related to the "principal-agent" problem that characterizes much public procurement. The problem of corruption and the harm that it causes have been given explicit recognition in the 1996 revised text of the GPA, a new development in WTO law that reflects increasing awareness of governance issues as an aspect of development. In addition to the general procedural provisions of the GPA dealing, for example, with publication of procurement opportunities, advance specification of selection and award criteria, etc., the Agreement's provisions relating to the establishment of domestic review or "bid challenge" procedures are an important bulwark against corrupt practices.

With respect to the challenge of promoting competition in public procurement markets, this is key benefit of the international liberalization via the WTO Agreement on Government Procurement. This chapter has argued, nonetheless, that international liberalization is not, by itself, a *sufficient* tool for ensuring an optimal degree of competition. National competition laws and policies play an essential complementary role in this regard. As has been discussed, this role encompasses: (i) the adoption and enforcement of effective rules to prevent bid rigging (collusive tendering); (ii) promoting the progressive elimination of regulatory and other barriers to competition, chiefly through "competition advocacy" activities; and (iii) other aspects of competition law enforcement including the treatment of

mergers and joint ventures. Specific challenges for competition authorities in the area of public procurement include: (a) promoting awareness among procurement officials of "suspicious signs" of collusion between suppliers; and (b) fostering institutional links between procurement and competition agencies.

In addressing these issues, this chapter has taken as a point of departure that measures aimed at increasing transparency and, thereby, preventing corruption in public procurement processes are consistent with the promotion of competition. Such measures expand the possibilities for competition by informing suppliers of opportunities to compete and by giving them confidence that bids will be assessed objectively on their merits. Nonetheless, as has also been noted, experience in the application of competition law in public procurement markets highlights circumstances in which transparency-enhancing measures can facilitate collusion among suppliers. This highlights a need for balancing (mutual accommodation) of competition and anti-corruption concerns in well-designed procurement systems. We believe that, with such balancing, measures aimed at preventing corruption and promoting competition are likely to be strongly mutually reinforcing.