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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

Contribution from India

-- Session V --

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Contact: H el ene CHADZYNSKA, Programme Manager of the Global Forum on Competition
Tel: +33 1 45 24 91 05; email: helene.chadzynska@oecd.org

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COLLUSION AND CORRUPTION IN PUBLIC PROCUREMENT

-- India --

1. Public procurement can be defined as procurement made by utilising public funds to fulfil needs and requirements of a public authority. Procurement is a key economic tool available with the governments for execution of developmental programmes including delivery of socially important goods & services like Public health, Education, Public Transport etc. Public procurement plays an important role in facilitating use of private sector for public sector goals and acts as a catalyst towards development of particular societal groups and regions.

2. The primary objective of any effective procurement policy is to obtain goods, works and services with a view to shunning mismanagement, avoiding waste of public funds and in process getting the best value for money. Competition among supplier firms would enable governments accomplish this objective and therefore it is imperative that the procurement process is not affected by any endeavour to embrace practices such as collusion, bid rigging, fraud and corruption. While strict enforcement of competition law is crucial, advocacy in terms of informing and educating public procurement agencies about the needs and benefits of competition would help in designing efficient procurement processes and in turn bring down the cost of procurement at desirable level.

3. It is estimated that public procurement constitutes about 15% -20% of GDP in developed and developing jurisdictions. Public procurement is estimated at approximately 20% of Gross Domestic Product in OECD countries¹. In India, public procurement has been estimated to constitute about 30% of GDP². Under the constitutional provisions of India, Union List, State List, and the Concurrent List govern the legislative functions of the central and state governments. State procurement does not figure in any of the lists as a distinct subject and therefore the Union Parliament has the exclusive power to make any laws on the subject of procurement. However, Parliament has not enacted any specific legislation on the subject and hence Public Procurement is performed through Government Policies.³ The matter of procurement is primarily covered by General Financial Rules 1963 (amended in 2005) which are set of executive instructions framed by the Ministry of Finance and the Delegation of Financial Powers Rules 1978. The Department of Expenditure, Ministry of Finance has also issued three separate Manuals on Procurement of Goods, Services and Works as guidelines to all central government departments in the matters of procurement. Further, the Directorate General of Supplies & Disposals (DGS&D) and the Central Vigilance Commission (CVC) have also issued guidelines prescribing the procurement procedure to be followed by all Central Ministries.

¹ The Size of Government Procurement Markets, OECD, 2001.

² "Enhancing value in public procurement", special address by Shri Pratyush Sinha, Central Vigilance Commissioner, Conference on Competition, Public Policy and Common Men, 16th November 2009 organised by Competition Commission of India in Delhi. Although an Article by Vivek Srivastava, Titled, "India's accession to the Government Procurement Agreement: Identifying Costs and Benefits", published in 'India and WTO' by Aditya Mattoo and Robert M. Stern published in 2003 had estimated it at 20%.

³ Tamil Nadu and Kamataka, have recently enacted Acts on 'Transparency in Public Procurement'.

4. Procurement of goods and services in India is carried out by the Ministries, Departments, Local Bodies, Statutory Corporations and Public Undertakings both at Central and state level. The Ministry of Finance at the Centre and the Department of Finance in the States lay down broad rules in the matters of government expenditures including expenditure on the procurement of goods, works and services. The procuring agencies may issue elaborate guidelines based on these rules. The office of Comptroller and Auditor General of India (CAG) carries out ex-post audit of government expenditures and publish annual and special reports highlighting instances of irregular and wasteful expenditures.

5. As public procurement in India is decentralised, all States/PSUs have their own procurement organisations. There is no Central Procurement Authority though Central Purchase Organisations like the Directorate General Supplies and Disposal (DGS&D) and state level purchase organisations are associated with the process of rate contracts (akin to framework agreements) with registered suppliers.

6. There are three types of tenders prescribed in the rules: Advertised Tender Enquiry (ATE); Limited Tender Enquiry (LTE) and Single Tender Enquiry (STE). The general rule in procurement is that any tender above a value of Rs. 25,00,000 must be through invitation by public advertisement. Restricted or limited tenders are prescribed for procurement of goods exceeding Rs.1 lakh but below Rs. 25 lakh or in exceptional circumstances and single tenders are prescribed in the case of exceptional circumstances like urgency and proprietary items. The basic procedural framework, therefore, is no different from World Bank Guidelines or UNCITRAL model law or the other good models of public procurement and it can be said that there is a reasonably good framework of rules, procedures and documents in place.

7. The Defence Procurement Procedure - 2008⁴ provides comprehensive policy guidelines for all capital acquisitions undertaken by the Ministry of Defence, Defence Services, Indian Coast Guard, Defence Research and Development Organisation (DRDO), and the Ordnance Factory Board (OFB). Defence Procurement Manual governs the procedure for revenue procurement in these organisations. The Government of India has also evolved special procedures and guidelines for procurement of PPP Projects.

8. The basic guiding principles of public procurement in India, inter alia, include maximising economy, efficiency and effectiveness, fairness, competition among suppliers for supply of goods/services to be procured and transparency in the procedures. The rules governing public procurement are binding only on the State as defined in Article 12 of the Constitution of India. The expression "State" is widely defined and interpreted to include not only the Government but also agencies and other autonomous bodies directly or indirectly controlled by it. Hence private bodies not under the control of the Government are not bound by the procurement procedures prescribed under the rules prescribed by the Government.

9. The tendering authority has to proceed in accordance with the limitations contained in the tender document or in the applicable Manuals or Rules. The general rule is that the tender is awarded to the lowest bidder (L-1). Post tender negotiations are severely discouraged and even L-1 post tender negotiations are not permitted except for reasons to be recorded in writing. Judicial review of administrative action is vested in the high courts. A tenderer shall have a right to be heard in case it feels that the proper tendering process has not been followed or that its bid has been wrongly rejected. The general rule prescribed by Courts, is that any person having a conflict of interest will not be part of the bid evaluation or award process.

⁴ The Defence Procurement Procedure – 2002 (DPP- 2002) came into effect from 30 December 2002. The scope of the same was enlarged in June 2003 to include procurements flowing out of 'Buy and Make through Imported Transfer of Technology (TOT)' decisions. This procedure was reviewed in 2005 and later in 2006. The Defence Procurement Procedure – 2006, was again reviewed and revised based on experience gained in implementation and DPP 2008 came into existence with effect from August 2008.

10. The procurement by the Central Government Ministries and Departments by and large works satisfactorily using fair and reasonable procedures. However, cases of corrupt practices, instances of bid – rigging and collusive bidding have also come to fore.

11. The problem of corruption is rooted in substituting public welfare by the personal interest of employees. Personal payoffs result out of anti-competitive practices giving rise to poor quality and higher costs of public procurement. Anti-competitive procurement manifests in practices like specifications which could be chosen either to favour some suppliers or as entry barriers for others or procurement of non standard items. Bureaucratic hurdles can also be effectively used to erect entry barriers selectively. Annual worldwide bribery of about US \$1 trillion⁵ has been estimated on account of corrupt practices in procurement.

12. While anti-competitive procurement policies can be used effectively by the public officials to engage in corrupt practices, anti-competitive behaviour by the supplier firms can also generate benefits for them. By colluding with the public officials, the suppliers can form informal cartels to create entry-barriers. In Indian context, public works contracts are prime examples of such collusion. Unlawful gains through public procurement become the main objective of many individuals.⁶

13. Collusion between the supplier and the procurement agency to maximise payoffs is major problem with public procurement which may take various shapes; viz quantity variations or changes in specification, paying for fictitious work, accepting poor quality product or work etc.

14. Corruption affects the allocation of public resources since projects more likely to provide opportunities to illegal gratification are preferred and in process many socially desirable schemes may get neglected. Corruption leads to a different process of allocation of contracts compared to a genuine competitive process. Corruption either gives rise to a situation where the contract is not awarded to the lowest bidder but rather to the firm who has offered a bribe or to a situation in which there are fewer bidders than would otherwise have been the case, thus, distorting the competitive process. There is complementarity in corruption and anti-competitive practices as corrupt procurement officials may ask the supplier firm to ensure (through bid-rigging) that its bid will be the lowest bid. Other competing firms may simply agree either in exchange of some consideration or out of promise of sub-contract of main work. There are possibilities of tacit exchange in sense that if the competing firms collude, markets can later on be allocated, giving gains to all the firms which are parties to this arrangement.

15. Central Vigilance Commission (CVC)⁷ was set up in India in 1964 to guide the central government and its agencies in tackling corruption by public officials. It supervises investigations under the Prevention of Corruption Act, 1988. The CVC has also issued guidelines and instructions to curb corruption in procurement. Each Ministry or Department has its own vigilance machinery which looks into the procurement related misdemeanours. CVC has issued ‘Standard Operating Procedure’ laying guidelines for adoption of Integrity Pact and role of independent external monitor in respect of all major procurements. Department of Personnel and Training has suggested to all State Chief Secretaries to consider IP adoption in respect of State Public Sector Undertakings (PSUs) as outlined by CVC. Ministry of Defence in its 2008 Procurement Policy has proposed to adopt IP in all defence deals of Rs 100 crore and above. So far, 38 Central PSUs have committed to adopt IP.

⁵ Interview by Director, World Bank Institute Global Governance, Daniel Kaufmann <http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:20190295~menuPK:34457~pagePK:34370~piPK:34424~theSitePK:4607,00.html> (accessed on 23.12.2009).

⁶ Many such individuals also try their luck in politics by using ill-gotten funds at their disposal.

⁷ Details may be seen at (www.cvc.nic.in).

16. State Vigilance Commissions have also been set up in some states. Besides, Lokayuktas or ombudsmen have been put in some states to investigate charges of corruption against public servants, politicians and officers. The Right to Information Act, 2005 with its objective of arming citizens with right to get information marks a benchmark in transparency and accountability in governance.

17. *Section 3(3) of Competition Act, 2002* specifically provides that any agreement entered into between enterprises or associations of enterprises or persons or associations of persons or between any person and enterprise or practice carried on, or decision taken by, any association of enterprises or association of persons, including cartels, engaged in identical or similar trade of goods or provision of services, *which directly or indirectly results in bid rigging or collusive bidding, shall be presumed to have an appreciable adverse effect on competition.* Since the concerned section has been notified only in May 2009 the results of enforcement actions have not yet been fructified. However, significant steps have been taken towards advocacy on the issue of public procurement. Several conferences and workshops have been organised for the benefit of public procurement officers and other stakeholders. A seminar on "Public Procurement Reforms for Better value for Money" was held recently in New Delhi. Another conference was organised in November on "Competition and Public Procurement Policy" in which many eminent experts had the occasion to put across their view points.

18. Currently, many countries are in the process of evolving ways to save costs by preventing corruption in government procurement. Korea's experience demonstrates that using IT can be one of the most effective policy tools in this direction. Proper adoption of an e-procurement system can expand transparency in the procurement market and also contribute to the prevention of corruption. Towards this, Department of Expenditure, Ministry of Finance, Govt. of India has taken significant steps by issuing instructions to all Govt. Ministries/ Departments/Organisations to switch over to e-procurement regime.

19. Corruption induces lack of competition which leads to the neglect of innovation. More potential suppliers in market not only results in additional competition giving rise to lower prices, innovations, better quality goods & services but also translates into reduced tax burden. The governments also in the process find more funds at their disposal for delivering public goods.

20. Collusion in public procurement may be reduced by careful consideration of the various features of the bid process. Procurement tenders are required to be designed in such a way that the bidders' ability to reach collusive arrangements is significantly reduced. Competition authorities need to make efforts to increase awareness of the cost of bid-rigging to the government and to the taxpayers by way of educating and training procurement officials and government investigators and take exemplary actions against firms involved in bid-rigging and other illegal conduct which undermines competition. Competition authorities can develop check lists to help procurement agencies in detecting instances of possible collusion.

21. A stronger antitrust and anti-competition agency with strong co-ordination with other law enforcement agencies will contribute to reducing the corruption in public procurements. Systematic exchange of information between the antitrust bodies and anti-corruption bureaus is highly desirable in this regard. Drive against corruption and steps towards enforcement to eliminate anti-competitive practices are complementary in nature since improvement in the procedure by which the tender documents are designed and the bidders are ultimately selected will not only reduce corruption but also enhance competition in the procurement market.