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**Working Party No. 3 on Co-operation and Enforcement**

**PUBLIC PROCUREMENT/BID RIGGING ISSUES**

**-- United Kingdom --**

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*The attached document is submitted to Working Party No. 3 of the Competition Committee FOR DISCUSSION under item III of the agenda at its forthcoming meeting on 15 June 2010.*

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1. This paper provides responses from the UK Office of Fair Trading (OFT) to the questions set for the roundtable discussion in Working Party 3 on Public Procurement and Bid-Rigging.

## 1. Executive summary

2. The UK government devotes a large share of public spending to public procurement– with an estimated £221bn<sup>1</sup> spent on public procurement in 2008/2009 for the purchase of goods and services from road building to housing. The 2008 Julius Review<sup>2</sup> found that in 2007/8 the UK public service industry<sup>3</sup> had a turnover of £79 billion, generating £45 billion in direct value added and employing over 1.2 million people. It also indicated that, over a 12 year period to 2007, the public service industry grew at an average annual rate of over 5 per cent in real terms.

3. Bid-rigging in public procurement can therefore have significant detriment for the procuring public authority, including government and public authorities, and ultimately for taxpayers.

4. The Office of Fair Trading (OFT) has alerted government to the risk of collusion in public procurement, and has worked with procurement officials and the UK Serious Fraud Office (SFO)<sup>4</sup> in an effort to fight bid-rigging more effectively.

5. The OFT, together with the UK public body responsible for the provision of advice on public procurement, the Office of Government Commerce (OGC), has provided guidelines for public procurement officials to help them identify any signs of potential collusion. In addition, the OFT has worked with the UK government in promoting a better understanding of how bidding procedures can be designed in order to make it more difficult for competitors to collude. There may however be a tension - certain formal public procurement measures which seek to minimise the risk of corruption can increase the risk of collusion. For example, information on the terms and conditions offered by winning and losing bidders is sought to ensure the fair treatment of bidders and provide information on expenditure of public funds. However, collusion is more easily sustained where there is greater transparency about potential bidders and details of bids.

6. In addition, the OFT's report on *Government in Markets*<sup>5</sup> and its market study *Assessing the impact of public sector procurement on competition*<sup>6</sup> provide advice to policymakers on how public procurement can affect the structure of the market and the incentives of firms to compete in the long run. The purpose of these reports is to highlight how an effective procurement policy can promote efficiency and can ensure that those who offer best 'value for money' are awarded contracts, thus avoiding mismanagement of public funds.

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<sup>1</sup> See the Public Expenditure Statistical Analysis, 2009 [http://www.hm-treasury.gov.uk/pespub\\_pesa09.htm](http://www.hm-treasury.gov.uk/pespub_pesa09.htm).

<sup>2</sup> [www.berr.gov.uk/files/file46965.pdf](http://www.berr.gov.uk/files/file46965.pdf).

<sup>3</sup> The term 'public service industry' refers to firms involved in providing public services on behalf of the UK government.

<sup>4</sup> The SFO is the lead agency in the UK for investigating and prosecuting cases of domestic and overseas corruption and fraud. The OFT works closely with the police and the SFO on criminal investigations, concerning both competition and consumer issues.

<sup>5</sup> See the OFT website: [www.oft.gov.uk/shared\\_of/business\\_leaflets/general/OFT1113.pdf](http://www.oft.gov.uk/shared_of/business_leaflets/general/OFT1113.pdf).

<sup>6</sup> See the OFT website for a copy of the market study: [http://www.oft.gov.uk/advice\\_and\\_resources/resource\\_base/market-studies/completed/procurement](http://www.oft.gov.uk/advice_and_resources/resource_base/market-studies/completed/procurement).

7. At the same time, the OFT has successfully pursued instances of collusion in public and private procurement by pursuing civil competition law infringements, most recently in the *Construction* case which resulted in the imposition of financial penalties totalling £129.2 million on one hundred and three companies found to have engaged in bid-rigging activity including associated ‘compensation payments’ in relation to building projects worth in excess of £200 million. At the time the decision was published, the OFT together with the OGC, provided further advice on how procurement officials can detect bid rigging and design procurement processes so as to minimise the risk of collusion. This included providing reference to recent OECD guidelines on these issues.

8. In addition, the UK has seen its first criminal cartel convictions for bid-rigging and other cartel activity in the *Marine Hose* case which involved both public and private contracts.

9. Through these cases, and previous OFT decisions into bid-rigging, the OFT has sent a clear message that collusion in procurement is a serious breach of competition law attracting substantial penalties for the companies and individuals involved. The OFT’s increased enforcement action, along with education of procurement officials in detecting signs of collusion, is designed to have a significant deterrent effect.

10. The OFT recognises however that the majority of businesses want to comply with competition law. Whilst it takes enforcement action where necessary, the OFT also wishes to support businesses seeking to achieve a competition law compliance culture. It recently undertook research into the drivers of compliance and non-compliance with competition law in order to gain a better understanding of the practical challenges faced by businesses seeking to achieve a competition law compliance culture<sup>7</sup>.

## **2. Competition enforcement – bid rigging**

11. Since the UK Competition Act 1998 came into force in 2000, the OFT has investigated a number of civil competition infringements involving bid rigging affecting both public and private procurement.

12. The OFT’s most recent bid rigging investigation into the construction industry is described in detail below.

### **2.1 The OFT construction investigation**

13. On 21 September 2009 the OFT issued an infringement decision imposing fines of £129.2 million (after reductions for leniency) on 103 companies for bid rigging comprising predominantly ‘cover pricing’ in the construction industry in England including associated ‘compensation payments’, following one of its largest ever investigations<sup>8</sup>.

14. Cover pricing describes a situation where one or more bidders collude with a competitor during a tender process to obtain a price or prices which are intended to be too high to win the contract. The tendering authority, for example a local council or other customer, is not made aware of the contacts between bidders, leaving it with a false impression of the level of competition and this may result in it paying inflated prices. The associated compensation payments that were uncovered involved the successful bidders paying an agreed sum of money to the unsuccessful bidders.

<sup>7</sup> See the OFT website: [http://www.offt.gov.uk/shared\\_offt/reports/comp\\_policy/oft1227.pdf](http://www.offt.gov.uk/shared_offt/reports/comp_policy/oft1227.pdf)

<sup>8</sup> Further information including the OFT’s Decision can be found on the OFT website: [www.offt.gov.uk/shared\\_offt/business\\_leaflets/general/CE4327-04\\_Decision\\_public\\_1.pdf](http://www.offt.gov.uk/shared_offt/business_leaflets/general/CE4327-04_Decision_public_1.pdf)

15. The firms were found to have engaged in illegal anti-competitive bid-rigging activities on one hundred and ninety nine tenders during the period 2000 to 2006. The OFT found that in eleven tendering rounds, the lowest bidder faced no genuine competition because all other bids were cover bids, and which is likely to have resulted in the client having unknowingly paid an inflated price. The OFT also found six instances where successful bidders had paid compensation payments of £2,500 to £60,000, which were facilitated by the raising of false invoices.

16. The infringements affected building projects across England worth in excess of £200 million including building projects for schools, universities, hospitals, and numerous private sector projects including the construction of apartment blocks and housing refurbishments. Eighty six out of the one hundred and three firms received reductions in their penalties because they admitted their involvement in cover pricing prior to the OFT's infringement decision. Thirty three of the companies received reductions for leniency.

17. The OFT's investigation originated from a specific complaint in the East Midlands in 2004, but it quickly became clear from the evidence that the practice of cover pricing was widespread. The industry itself described the practice as 'endemic' and the OFT's investigation included dawn raids on fifty seven companies in the period from November 2004 to March 2006. The range of infringements therefore included the East Midlands as well as neighbouring areas Yorkshire and Humberside and other areas in England.

18. The OFT also received evidence of cover pricing implicating many more companies on thousands of tender processes, which presented challenging case management issues and a call for innovative solutions. The OFT prioritised and focused its investigation to a more limited number of infringements by using objective prioritisation criteria, with a view to reaching a decision comparatively swiftly, while still ensuring that the scale and scope of the investigation reflected the 'endemic' nature of the practices in question so as to maximise the deterrent effect of its investigation. The OFT's case strategy and management is discussed in further detail in the two textboxes below.

19. Following the OFT investigation, the UK Contractors Group and National Federation of Builders jointly launched a competition law code of conduct to help avoid breaches of competition law by the construction industry. Although the OFT has not formally endorsed the code of conduct, it is a welcome initiative in response to the OFT's investigation.

**Box 1. Case strategy and case management: prioritisation**

The OFT narrowed the scope of the case by firstly categorising the initial evidence according to 'evidential weight' in order to focus on those parties where evidence of bid rigging was greatest and strongest.

Secondly, the OFT proceeded to investigate only those companies where there were reasonable grounds to suspect their involvement in bid rigging on at least five tenders.

This resulted in a range of suspected infringements and parties that reflected the endemic nature of the practices in question, in that it covered:

- a broad spread of companies, in terms of size (with turnover ranging from around £100,000 to over £2.5 billion),
- a broad spread of companies in terms of location (with companies operating from various different regions of England, as well as nationally).

In addition, it was necessary to pursue both companies that had and companies that had not received leniency to ensure that companies are not deterred from coming forward as leniency applicants (with 70 companies that had not applied for leniency as well as the 33 that had applied).

For each of these companies, the OFT selected five tenders for further investigation and then proceeded to interview witnesses (estimators and managers employed by the leniency applicants) in respect of those tenders. The OFT also contacted the procurers to ensure that it based its investigation on accurate information regarding the bids made for each tender.

### **Box 2. Case strategy and case management: availability of leniency and ‘fast track’ offers**

In order to limit and focus its investigation, the OFT also decided in the beginning of 2007 to close the door to any further leniency applications so as to keep the investigation manageable and to proceed in an efficient and timely manner. At the same time the OFT launched a ‘Fast Track Offer’ to those companies that had not applied for leniency but remained under investigation.

If other companies had applied for leniency, it would not have been possible for the OFT to progress the investigation in an efficient and timely manner due to the need to investigate fresh allegations and to make a further selection of tenders and companies for investigation.

Notwithstanding the decision to close the door to further leniency applicants, the OFT nevertheless wished to put the non-lenieny parties on notice that they were under investigation, to inform them of the tenders in respect of which they were suspected of engaging in bid rigging activities, and as part of its ongoing investigation to give them an opportunity to provide a voluntary admission of liability. In exchange for any admissions, the parties were offered a 25 per cent reduction of any financial penalty that the OFT ultimately imposed in respect of any suspect tenders for which admissions were received. This constituted the OFT’s ‘Fast Track Offer’.

The OFT did not provide the non-lenieny companies with the evidence against them at this stage, but the companies were given the opportunity to provide the OFT with the identity of the companies with whom they had engaged in bid rigging on each tender, thereby providing independent corroboration of the OFT’s existing evidence.

Of the eighty five non-lenieny Parties that were sent Fast Track Offer letters by the OFT, forty five admitted engaging in bid rigging activities in all or some of the suspect tenders identified by the OFT. This led to significant procedural efficiencies and resource savings for the OFT’s investigative team, allowing it to conclude the investigation more efficiently and comparatively quickly.

### **3. Roofing investigations**

20. Prior to the OFT *Construction* investigation the OFT investigated collusion in the roofing industry in various parts of the UK. The OFT issued several decisions between 2004 and 2006 fining companies for cover pricing and provision of compensation payments in the roofing industry, as follows:

- March 2004 – West Midlands flat roofing – fines of £300k after leniency imposed on 9 companies<sup>9</sup>. This decision was appealed to the Competition Appeals Tribunal, which upheld the OFT’s decision on liability in its entirety but made a small reduction to the penalty imposed on one of the parties.

<sup>9</sup> [www.of.gov.uk/shared\\_of/ca98\\_public\\_register/decisions/westmidlandsroofing.pdf](http://www.of.gov.uk/shared_of/ca98_public_register/decisions/westmidlandsroofing.pdf).

- March 2005 – North East flat roofing – fines of £470k after leniency imposed on 7 companies<sup>10</sup>.
- March 2005 – Scottish roofing – fines of £87k after leniency imposed on 4 companies<sup>11</sup>.
- July 2005 – Scottish roofing II – fines of £138k after leniency imposed on 6 companies<sup>12</sup>
- February 2006 – Mastic asphalt – fines of £1.55 million after leniency imposed on 13 companies throughout England and Scotland<sup>13</sup>. This decision was appealed to the Competition Appeals Tribunal, which upheld the OFT’s decision on liability in its entirety.

21. The UK has also seen its first criminal cartel convictions for bid-rigging and other cartel activity in the *Marine hose* case which involved both public and private contracts.

### **3.1 *Marine hose cartel***<sup>14</sup>

22. In 2008 three UK businessmen were sentenced to between 20 and 30 months’ imprisonment for cartel offences under the Enterprise Act 2002. All three were also disqualified from acting as company directors for periods of between five and seven years. In addition over £1m were confiscated under the Proceeds of Crime Act 2002.

23. These are the first convictions for a cartel offence since criminal prosecution powers were given to the OFT under the Enterprise Act 2002 which makes it a criminal offence for two or more individuals dishonestly to agree to make or implement (or cause to be made or implemented) cartel arrangements between two or more undertakings which fix prices, divide markets or customers, limit or prevent production or supply, or rig bids, in each case in relation to supplies in the UK. Unlike the civil regime, the criminal cartel offence is therefore targeted at individuals rather than businesses.

24. The offence carries a maximum sentence of five years’ imprisonment and/or an unlimited fine. In addition, where an offence has been committed in connection with the management of a company, the offender may be disqualified for up to 15 years from being a company director or in any way concerned in the management of a company. Further, in cases where the offender has benefitted financially from the offence, the court may order the confiscation of assets under the Proceeds of Crime Act 2002 up to the value of the benefit or, where less, the value of the available assets.

25. The three individuals pleaded guilty to dishonestly participating in a worldwide cartel involving all the major manufacturers of marine hose, in which the global market was divided among the manufacturers according to agreed market shares and bids on individual contracts were rigged, by reference to a common price list. In addition, it was also agreed that contracts emanating from a manufacturer’s ‘home territory’ should be reserved to that manufacturer.

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<sup>10</sup> [www.offt.gov.uk/shared\\_offt/ca98\\_public\\_register/decisions/ner.pdf](http://www.offt.gov.uk/shared_offt/ca98_public_register/decisions/ner.pdf).

<sup>11</sup> [www.offt.gov.uk/shared\\_offt/ca98\\_public\\_register/decisions/scot.pdf](http://www.offt.gov.uk/shared_offt/ca98_public_register/decisions/scot.pdf).

<sup>12</sup> [www.offt.gov.uk/shared\\_offt/ca98\\_public\\_register/decisions/scotroof.pdf](http://www.offt.gov.uk/shared_offt/ca98_public_register/decisions/scotroof.pdf).

<sup>13</sup> [www.offt.gov.uk/shared\\_offt/ca98\\_public\\_register/decisions/flatroof.pdf](http://www.offt.gov.uk/shared_offt/ca98_public_register/decisions/flatroof.pdf).

<sup>14</sup> For more information, see the OFT website: <http://www.offt.gov.uk/news/press/2008/72-08>.

26. It was accepted by the defendants that the cartel is likely to have resulted in higher prices for customers in the UK. These included a UK government department, the Ministry of Defence, who had used public procurement processes.

#### 4. Exclusion from bidding in public procurement auctions

27. As a general principle, the OFT considers that, where it is lawful to do so, excluding companies found guilty of illegal bid-rigging from public procurement auctions for a period of time, would act as an additional deterrent to such conduct, and could therefore strengthen efforts to eradicate such illegal activity. In the absence of any provision for leniency applicants to be treated differently from non-leniency applicants in this regard, however, the OFT recognises that this also has the potential to undermine the detection of bid-rigging by reducing incentives for leniency applicants to come forward with information.

28. Notwithstanding the potential benefit of excluding those found to have participated in bid-rigging from public tenders, the OFT concluded, following extensive consultation with the OGC, that automatically excluding the parties found to have engaged in bid rigging would not be appropriate in the particular circumstances of the *Construction* case.

29. The endemic nature of the practice within the UK construction industry suggested that many other companies were likely to have been involved in bid rigging, even though such activity remained undetected. For this reason, it cannot be assumed that the parties to the investigation were the only companies that may have engaged in such activity. In those circumstances, the OFT and the OGC recommended in a note to procurers<sup>15</sup>, issued at the time of the issue of the OFT's infringement decision in September 2009, that the parties should not be excluded automatically from future tenders, on the grounds that they were parties to the OFT decision, or be the subject of similar adverse measures making it more difficult for them to qualify for such tenders. Rather, it was a matter for individual procurers to decide what action, if any, they should take in their own particular circumstances, having taken appropriate legal advice as necessary.

30. Public authorities were advised to consider the specifics of their procurement, as well as the points outlined below, in deciding the most appropriate course of action on a case by case basis, namely that:

- the parties to the OFT's infringement decision had received significant financial penalties appropriate to the infringement findings in the OFT's infringement decision;
- it would be wrong automatically to assume that construction companies that were not named in the decision had not also been involved in bid rigging;
- as a result of the OFT's investigation, the parties could be expected to be particularly aware of the competition rules and the need for compliance and, if anything, are more likely to be compliant; and
- many of the parties had cooperated fully with the OFT's investigation and a significant proportion had taken measures to introduce or reinforce formal compliance programmes and to ensure that their staff are aware of their competition law obligations.

31. The OFT added for the avoidance of doubt, however, that this recommendation was only intended to apply to this case.

<sup>15</sup> [www.offt.gov.uk/shared\\_offt/business\\_leaflets/general/Information-Note2.pdf](http://www.offt.gov.uk/shared_offt/business_leaflets/general/Information-Note2.pdf).

## 5. Wider advocacy efforts to improve efficiency of public procurement

32. Our experience in the UK is that competition authorities can play an active advocacy role in advising other parts of government on procurement. They can assist in at least three ways:

- **Advice on designing public procurement processes:** First, they can provide a framework for identifying how different procurement approaches might affect competition, and hence provide general advice on designing public procurement processes. For example, they can contribute to overall procurement guidance issued by central government.
- **Detailed analysis of particular markets:** Second, competition authorities can carry out more detailed analysis of particular markets, giving specific advice on procurement approaches in those sectors. This is likely to be more appropriate in cases where new markets are being opened up to private sector involvement, or where there are particular competition concerns.
- **Guidance and training to public procurers involved in running procurement processes:** Third, they can provide guidance and training to public procurers involved in running procurement processes, to help identify particular competition problems – particularly the possibility of bid rigging and collusion.

33. The following paragraphs give more detail on the first two points.

### 5.1 General framework advice: 2004 market study

34. The OFT market study *Assessing the impact of public sector procurement on competition*<sup>16</sup> aimed to provide a framework for analysing the effects of procurement on competition and markets. At a high level, it identified three broad ways in which procurement processes can affect competition:

- **Short term effects**, relating for example to the level of participation in a tender, the similarity of bidders and the ability of bidders to engage in tacit collusion. In general, more bidders imply higher competition. However, there may be valid reasons for restricting competition if evaluating bids is costly, or if a large number of bidders lead to higher prices when participants bid more cautiously. Competition is likely to be stronger when bidders are similar, for example where they are similar in terms of size, cost structures, ownership, degrees of vertical integration etc. It is easier to sustain collusion if bids are transparent, bidders interact periodically, and demand is stable and predictable.
- **Long term effects**, capturing changes in investment, market structure and technology as a result of procurement decisions. Public procurement can have long term consequences for example by changing the number of firms in the market, increasing the gap between market leaders and other suppliers and creating incumbency advantages for contractors, thus eroding competition. Such concerns might suggest strategies such as awarding multiple contracts and selecting a different bidder for each of these contracts, or by helping new entrants become established in other ways.
- **Knock-on effects**, where the public sector's procurement decisions affect other buyers in the market. For instance, if public sector contractors gain advantages over firms that do not supply to the public sector, this can lead to restricted or distorted competition for other (non-public sector) buyers and low prices for the public sector.

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<sup>16</sup> See the OFT website for a copy of the market study:  
[http://www.of.gov.uk/advice\\_and\\_resources/resource\\_base/market-studies/completed/procurement](http://www.of.gov.uk/advice_and_resources/resource_base/market-studies/completed/procurement).



35. The market study then applied these general principles to some specific procurement practices that affect potential bidders. These included:

- **Restrictions on participation and increased participation costs:** It was found that formal public sector procurement practices can reduce participation by and increase participation costs for, small bidders. For example, this might be through excessive information requirements, restricted communication of contract opportunities or overly narrow qualification criteria. It is important for the public sector to strike a balance between the costs and benefits of increasing participation.
- **Contract aggregation:** Public sector procurement often involves contract aggregation, which is bundling contracts into fewer larger contracts that are tendered less frequently. This entails savings in the cost of conducting and managing tenders as well as lower prices due to economies of scale and scope. But, it can dampen competition by excluding small firms that cannot meet all the requirements, removing in-contract competition by moving demand between contractors at the margin, and amplifying incumbency advantages. There may also be a risk that discussions between sub-contractors on a large contract might facilitate collusion. On the other hand, it may promote competition by reducing the scope for tacit collusion through repeated interaction, helping firms overcome entry barriers by assuring demand to the bidder and stimulating investment.
- **Self-supply:** Often the public sector has the option to self supply rather than procure. This can affect competition as the decision not to procure externally limits the size of the market for other buyers. The public sector needs to ensure that self supply is indeed the cheaper option, but price comparison may not be easy in a non-competitive market. Thus there is a danger that self-supply is favoured when in fact this would be inefficient due to an incorrect evaluation or assessment of the costs underlying self-supply.

36. Overall, the OFT found that the competition effects of procurement are complex and depend on the particular procurement settings. However a general framework can provide a useful basis for a more specific and detailed analysis. One of the results of the study was to identify areas of public procurement that might raise particular competition concerns, which then allowed us to follow up with more specific advice.

## **5.2 *Specific advice: 2006 report on waste procurement***

37. Following the 2004 procurement report, the OFT sought to identify certain key sectors where it might be able to offer specific advice on the procurement method being applied. One of these was waste procurement. Local authorities at the time were required to devise new waste management strategies in order to meet the government's landfill reduction targets. The OFT, together with the OGC and the Department for Environment Food and Rural Affairs (Defra), produced a report on public procurement and competition in the municipal waste management sector.

38. The report made a number of recommendations to enhance competition at various stages of waste management which are described in the textbox below.

### Box 3. Advice on procurement methods: waste management

- The length of contracts for waste collection services should be set to enable suppliers to recover sunk costs and a reasonable return on their investment, but no longer (and generally no longer than five years).
- Procurement should be open, free from overly restrictive criteria in order to encourage more bids.
- Procurement should ensure fair competition between self-supply and private sector bidders (see paragraph 0 above).
- Joint procurement of collection with other waste management services must be carefully considered and the risks of collusion should be recognised.

Waste disposal is more capital intensive than collection, and often large private firms are seen to supply integrated waste management services. The report therefore recommended that local authorities should remain open to the option of consortia bids including smaller firms with relevant experience, and should try to arrange sites and planning permission prior to tendering so as not to deter bidders, however the risk of collusion should be recognised in order to be able to identify instances of collusion. Fair competition between private and public bidders should be maintained and care should be taken when aggregating contracts. Waste treatment facilities that meet the needs of local authorities as well as private demand should be considered.

## 6. Regulatory or institutional conditions that can help facilitate bid rigging

39. The 2004 OFT market study on public procurement found that the design of public procurement processes can affect the likelihood of collusion.<sup>17</sup> Accordingly, there may be steps that procurement authorities can take to reduce the risk of bid rigging in particular cases.

40. The market study noted that it is more difficult to sustain collusion as the number of bidders increases, and as bidders become more dissimilar (for example in terms of size, cost structure, ownership, degrees of vertical integration). Other factors that may impact on the likelihood of collusion include:

- **Transparency:** collusion is more easily sustained if bidders can observe when other firms are trying to charge prices below the collusive level. The more likely such under-bidding would be detected, the more effective is the threat of retaliation by other firms which ultimately sustains the collusive outcome. This means that increased transparency such as information about the terms and conditions offered by winning and losing bidders in a competitive tender may increase the risk of collusion. What might be considered beneficial for other public policy grounds (minimising the risk of corruption and ensuring fair treatment of bidders, information on expenditure of public funds) can in fact increase the risk of collusion.
- **Frequency of interaction:** collusion is more easily sustained when bidders interact repeatedly, either in the same market over time, or in different markets, because repeated interaction allows for more effective punishment of firms trying to charge prices below the collusive level. This means that splitting up a contract across multiple tenders can increase the risk of collusion.
- **Stability of demand:** collusion is more easily sustained in markets where demand is relatively stable and predictable. This is because demand volatility makes it more difficult to detect attempts by firms to grab a larger share of the market by charging lower prices, and the incentives

<sup>17</sup> OFT (2004), paragraph 1.22.

to under-bid competitors are larger if demand is large at present, but expected to fall in the future. This means that a constant, predictable flow of demand from the public sector may increase the risk of collusion.

41. It follows that, for example, greater transparency about potential bidders and details of bids, might facilitate collusion or bid rigging. More generally there might be a tension between measures to avoid corruption by ensuring fair treatment of bidders, and measures to increase competition.

42. Formal rules governing public procurement which are designed to avoid any abuse of discretion by the public sector in selecting and evaluating bids can make communication among rival companies easier, promoting collusion among bidders.

43. In some cases, procurers may be able to design procurement processes to influence some of these factors and hence reduce the risk of bid rigging. For example, the OFT report considered the likely competition impacts of including a self-supply option in a procurement contest (see paragraph 0 above). The report found that a self-supply option could sometimes provide an effective fall-back position for the public sector to purchasing from external suppliers. This can impose a competitive constraint, and allow the public procurer to benchmark private bidders and possibly make it easier to identify bid rigging. For example, in a case study on procurement of contracts for building and operating prisons, it was found that having a 'public sector comparator' which allows the procurer to consider whether bids are significantly above the likely cost, could be a good way of undermining collusion incentives.<sup>18</sup>

44. As discussed in the report, there could be other negative consequences of having a self-supply option, particularly for example if there is not perceived to be a level playing field between the in-house bid and external competitors. For example, because the self-supply bid does not fully take into account all possible costs which should properly be allocated to the self-supply bid. In these cases, allowing self-supply can deter entry to the procurement process and hence reduce the overall level of competition. In practice therefore, there are complex trade-offs that need to be made. However, the overall message is that the approach to procurement can have an impact on incentives for collusion, and indeed on wider competition in the market.

## **7. Incentives to focus on the detection of bid-rigging?**

45. OFT considers that the incentives of officials responsible for public procurement are in line with competition authorities: both seek to ensure that the market bids competitively (both in terms of price and quality). As set out above, the OFT therefore plays an active advocacy role in advising other parts of government on procurement, for example by advising on designing public procurement processes and in providing guidance and training to public procurers involved in running procurement processes, to help identify particular competition problems – particularly the possibility of bid rigging and collusion.

46. The OFT does not provide specific incentives in order for public procurement officials to focus on the detection of bid-rigging. The OFT has introduced an informant reward programme, whereby it offers financial rewards (of up to £100,000 (in exceptional circumstances)) for information about cartel behaviour.<sup>19</sup> The financial rewards programme is primarily intended for those likely to hold 'inside' information of cartel conduct. Whilst procurement officials are generally unlikely to hold such information, the OFT does not exclude the possibility of rewarding procurement officials for such

<sup>18</sup> OFT (2004), paragraph 5.39.

<sup>19</sup> For further information see: <http://www.of.gov.uk/OFTwork/competition-act-and-cartels/cartels/rewards>.

information, provided they have not themselves participated in the cartel conduct (in which case an approach for immunity would be more appropriate)

## **8. Certificates of independent bid determination**

47. Many procurers use certificates of independent bid determination (CIBD) of their own accord in the UK. There is no prescribed format for such certificates although the OFT has made available templates to any company that requests it. In 2006 the OFT worked with the OGC to issue guidance on maximising competition in procurement<sup>20</sup>. This guidance included advice on detecting and preventing bid rigging, including at paragraph 58 the following advice:

*“Think of using non-collusion clauses and/or certificates of independent bids (self-certification by the supplier that they have not colluded with others, containing warnings exposing those who make false declarations to legal action: OFT can provide recommended text”.*

48. The OFT does not enforce CIBD violations as this falls outside of its remit. In addition, the OFT considers that self-certification alone may not be sufficient to deter parties from bid rigging. During the investigation into bid rigging in the construction industry the OFT found numerous instances where such certificates had been completed and yet the companies had engaged in bid rigging. However CIBDs can potentially open up, under civil or criminal law, an alternative or complementary ground for parties to recover damages, and if used can increase deterrence, particularly where this is complemented with the threat of enforcement action by a competition authority.

## **9. Advocating for a competition law compliance culture**

49. Whilst the OFT takes enforcement action where necessary, the OFT also wishes to support businesses seeking to achieve a competition law compliance culture, so that breaches of competition law, including bid-rigging, are avoided in the first place.

50. The OFT recently undertook research into the drivers of compliance and non-compliance with competition law in order to gain a better understanding of the practical challenges faced by businesses seeking to achieve a competition law compliance culture<sup>21</sup>. The report was published on the OFT website on 19 May 2010.

### **9.1 Drivers of compliance and non-compliance**

51. The research<sup>22</sup> highlighted that competition law compliance often stands alongside other compliance requirements in areas such as health and safety, environmental protection or anti-bribery and corruption and is therefore often part of a broader compliance agenda. Competition law compliance is often expressly included in the interviewee business's codes of conduct and statements of corporate responsibility.

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<sup>20</sup> See [www.ogc.gov.uk/documents/CP0144MakingCompetitionWorkForYou.pdf](http://www.ogc.gov.uk/documents/CP0144MakingCompetitionWorkForYou.pdf).

<sup>21</sup> In parallel with this research, the OFT has undertaken research into drivers of compliance and non-compliance with consumer law, as well as research into levels of awareness of competition law, see paragraph 2.2. These workstreams aim to assist the OFT in assessing the most effective ways we can use our limited resources to drive compliance with both competition and consumer law.

<sup>22</sup> The OFT conducted 22 detailed interviews with businesses and also benefited from a number of group discussions with in-house counsel and private practice lawyers.

52. The key drivers for competition law compliance are the fear of reputational damage and financial penalties. Individual sanctions, such as the risk of criminal proceedings, director disqualification, personal reputational damage or internal disciplinary sanctions, are also an important factor in encouraging individuals to focus on competition law compliance. And a commitment to competition law compliance from the top of the organisation down is crucial to driving compliance in the organisation as a whole.

53. Competition law compliance is also seen by some organisations as a way to helping them to win business by positioning themselves as ethical businesses. Many businesses align employee incentives to competition law compliance activities, such as performance bonuses being contingent on completion of competition training.

54. The research also explored what compliance challenges might arise for businesses. These range from any apparent ambiguity or lack of management commitment to competition law compliance to rogue employees, confusion or uncertainty about the law, employee error or naivety, loss of trust in legal advice or a 'box-ticking' approach to compliance. Furthermore, if competition law compliance has to compete for 'airtime' with other compliance activities, then this can drive non-compliance.

## 9.2 *Competition law compliance guidance update*

55. Following its research, the OFT will review and update its guidance on competition law compliance<sup>23</sup> to reflect current best practice. It will suggest a risk-based four-step approach to an effective competition law compliance culture<sup>24</sup>.

**Figure 1. Effective Competition Law Compliance Culture: Virtuous Circle**



<sup>23</sup> [http://www.of.gov.uk/shared\\_of/business\\_leaflets/ca98\\_mini\\_guides/of424.pdf](http://www.of.gov.uk/shared_of/business_leaflets/ca98_mini_guides/of424.pdf).

<sup>24</sup> The OFT intends to publish a draft guidance document for consultation, with more detail on each of the steps, later in 2010.

**Box 4.**

The **core** of an effective compliance culture is to have an unambiguous commitment to competition law compliance from the top down. Without unambiguous commitment, the remaining steps are unlikely to be effective.

The **first step** is for the business to identify the key competition law compliance risks it faces. They may relate to the risk of cartel activities, abuse of dominance, the arrival of new staff, participation to extern events or when engaging in mergers and acquisitions activity. The identification can also be base on previous enforcement action.

The **second step** is for the risks identified to be assessed as high, medium or low risks for the business, based on the likelihood of the risks occurring.

The **third step** is for appropriate risk-mitigation activities. These would generally include appropriate policies and procedures, and appropriate training activities.

The business should also consider how best to achieve behaviour change within the organisation to achieve an effective competition law compliance culture. Activities might include competition law compliance training, procedures for obtaining advice on possible competition law issues or internal disciplinary procedures for staff involved in breaches of competition law.

The **fourth step** is the review stage. It is important that businesses regularly review all stages of the process to ensure that there is unambiguous commitment to compliance from the top down, that the risks identified or the assessment of them have not changed and that the risk mitigation activities are appropriate and effective