

Collusive Tendering as a Restrictive International Business Practice

As governmental participation in economic activity, especially in relation to the undertaking of public works, becomes more pronounced, so does public procurement in terms of goods and services increase. Indeed, according to calculations made by the Organization of Economic Cooperation and Development (the OECD) recently, public procurement, for example, in the OECD member countries accounted for 5 to 14 percent of the Gross National Product (GNP).¹ Among states, the idea or practice whereby governments restrict or favor only their own nationals in the award of contracts for public works, is deemed, on economic grounds, to be unwise. This is because, from an international business transactions point of view, effective competition tends to be forestalled or distorted when public supply contracts are awarded by public authorities with favors or preferences for their own national producers or enterprises. It is noteworthy, therefore, that in this respect the European Economic Community (the EEC) realized a few years ago, the need for the progressive and effective opening up of all public and semi-public contracts as part of a general move towards the "completion of the Internal Market and Industrial Policy."² It was, indeed, made quite clear then that supplies for the public sector represented a considerable and increasing share of EEC consumption. Consequently, measures were initiated for the gradual and effective extension of the right to tender for public and semi-public supply contracts within the business and the commercial system of the EEC.³

However, it is not to be assumed that when states decide to throw open their invitations for tenders for public supply contracts the situation becomes

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¹See THE OECD OBSERVER, No. 84 (November/December, 1976), p. 15.

²See *Communication from the European Communities' Commission to the Member States Concerning Activities Essential to the Proper Functioning of an Economic and Monetary Union*, BULLETIN OF THE EUROPEAN COMMUNITIES, Supplement 5/73), p. 15.

³See *Memorandum from the European Communities' Commission on the Technological and Industrial Policy Programme*, presented to the Council of the European Communities on the 7th of May, 1973. (BULLETIN OF THE EUROPEAN COMMUNITIES, Supplement 7/73).

economically well-regulated and that rational forces are allowed to operate to ensure that economic efficiency would become the norm. On the contrary, companies or firms increasingly attempt to get together in collusion to bid for such contracts. Needless to say that such attempts would be likely to lead to economic inefficiency and distortion in the general business pattern within a state.

It is the main aim here to examine some of the essential aspects of the Report⁴ of the OECD's Committee of Experts on Restrictive Business Practices on the main problems raised by collusive tendering practices and some of the possible new measures recommended by that Committee. But that does not preclude us from paying some attention to the broader international economico-legal issue concerning tenders for public or semi-public supply contracts, and the practice of States in discriminating against non-nationals. In this respect, the various measures introduced by the EEC to counteract such discriminatory practices may be briefly considered.

Bias Against Non-nationals in Public or Semi-public Supply Tenders

As an integral part of its technological and industrial policy and within the general framework of its antitrust rules and principles, the EEC has sought to abolish all forms of preferences and restrictions adopted by its member-states in favor of national enterprises or national production when it comes to the question of issuing invitations for tender in respect to public works or to public supply contracts. Indeed, on the 26th of July, 1971, the Council of the European Communities adopted two Directives for attaining freedom of establishment and freedom to provide services in the matter of public and semi-public works contracts. The first⁵ of these two Directives has carried into effect, as regards public works contracts, the principle of the prohibition of discrimination on the basis of nationality. The second⁶ Directive has proved for coordination of the national procedures of the EEC member-states for the award of public works contracts. Some of the basic principles which this latter Directive is meant to embrace are:

- (i) the prohibition of national technical specifications having a discriminatory effect
- (ii) advertising of notices of contracts at the community level by publication in the Official Journal of the European Communities; and
- (iii) introduction of objective criteria for the selection of enterprises and the award of contracts by national administrations. To ensure that such

⁴The main report itself is to be found in *COLLUSIVE TENDERING*, OECD, Paris, 1976.

⁵71/304/EEC.

⁶71/305/EEC.

principles are closely observed by the EEC member-states, the Council of the European Communities, on that same date, decided to set up an Advisory Committee⁷ through whose intervention the proper policing of the operation of that Directive could be brought about. In effect, therefore, the second Directive was calculated to bring into line the laws of the EEC member-states on that matter. Indeed, the EEC member-states were required to adopt the necessary measures for complying with that Directive within twelve months of the latter's notification. That period expired on the 29th of July, 1972.

It is significant in the respect that in the recent case of *Re the Public Works Directive 1971*,⁸ between the Commission of the European Communities and the Italian Republic, the Court of Justice of the European Communities held that the Italian Republic, by failing to adopt within the prescribed period the measures necessary for complying with the EEC Directive 71/305, had also failed to fulfill an obligation under the EEC Treaty. Moreover, it has been recently indicated that the Commission of the European Communities has been keeping a close watch on all cases of reservations and preferences for national producers in the award of public and semi-public contracts which are deemed to contravene Articles 30 and 34 of the EEC Treaty as well as to contravene the provisions of the various EEC Directives.⁹

Nature and Scope of the Practice of Collusive Tendering

The practice of collusive tendering may be defined as an agreement, overt or tacit, between enterprises with a view to restricting or eliminating competition in respect of bids submitted in response to an invitation to tender. To be more precise, it is one of the practices by which excessively high prices are charged by enterprises when they get together to tender for such contracts. The conditions or circumstances likely to give rise to the practice of collusive tendering have somehow been identified by the OECD's Committee of Experts on Restrictive Business Practices as follows: (i) the technical requirements of certain contracts which tend to encourage companies or firms to get together on their bids; (ii) the existence of information agreements on prices may tend to have a similar effect; and (iii) the presence of cartels or restrictive business practices in the relevant industries may constitute a likely source of encouragement to companies or firms to get together on their bids. The strong bargaining position and the virtual monopoly power of companies or firms which get

⁷71/306/EEC.

⁸Case 10/76, [1976] C.M.L.R. 699.

⁹See *The Tenth General Report on the Activities of the European Communities in 1976*, p. 83, para. 131.

together on their bids for tenders for public supply contracts could hardly be overlooked.

Under price information agreements, for example, manufacturers or producers keep each other regularly informed of past, present and, sometimes, future prices. Consequently, a link comes to be established between such agreements and the practice of collusive tendering. The link between information agreements and collusive tendering has been observed in several OECD countries. In France, for example, where there was a decision made in 1972 involving the laying of electrical cables, information exchanges developed gradually into a concerted action for sharing out contracts for public works. Similarly, price cartels may conduce to a collusive tendering practice being adopted by enterprises. It is noteworthy that some OECD countries have found that when a certain degree of cartelization is allowed to operate in the economy, the enterprises involved in such cartels tend to continue to operate on the occasion of an invitation to tender.

Ways of Controlling the Practice of Collusive Tendering

Although the OECD's Committee of Experts on Restrictive Business Practices found that the practice of collusive tendering was covered by the overall antitrust laws in a number of the OECD member countries, yet that Committee also found that the problem had become so acute in some of those countries that their governments had deemed it necessary to take specific action against the practice. Thus, for example, in Finland and Sweden an absolute prohibition had been placed on that practice without those two countries advertent at all to their usual case-by-case treatment of most other types of restrictive business practices. In Denmark, a partial prohibition had been imposed on the practice. Consequently, the prohibition would apply only in the construction industry. Moreover, detailed rules had been laid down to govern the submission of tenders. More comprehensively, Belgium had adopted a law on public contracts in respect to public works, supplies and services. That law indeed contained a provision prohibiting an agreement or arrangement likely to distort the normal conditions of competition touching contracts placed by the state or by other public bodies.

The prevalence and the economic significance of the practice of collusive tendering could indeed be gleaned from various cases decided in the different member countries of the OECD. For example, in the Federal Republic of Germany, the German Federal Cartel Office estimated in 1973, that 2,000 enterprises in the building industry in Northern Germany alone had taken part in collusive tenders between the period 1959 and 1973 in respect of projects worth 7 billion German marks. Not unexpectedly, it was assessed that such legal col-

lusion had had the effect of raising prices by 9 percent on the average above the normal competitive prices. In Great Britain, over 70 agreements involving collusion between companies or firms concerned with electrical installations or mechanical services in the building industry over the period 1963 to 1969, were submitted to the Restrictive Trade Practices Court for adjudication during the period 1970-1972. In the United States, 26 criminal collusive bidding antitrust cases were filed by the Antitrust Division between the period 1972 and mid-1973 against companies or firms. Equally, in France, the Technical Commission on Cartels and Dominant Positions had given a significant number of opinions in which the practice of collusive tendering had been adverted to and condemned by that body.

Yet, as in most areas of business or commercial activities, it is one thing when laws are passed to regulate them. It is another thing when such laws actually come to be enforced. In the latter process, the efficacy of the laws may not prove to be all that much, as experience in the enforcement of economic measures would seem to indicate. Not unexpectedly, therefore, there are problems of control or the policing of legal enforcement in the area of the practice of collusive tendering. It will be convenient to examine some of those problems in a separate section.

Problems of Control or Policing

The OECD's Committee of Experts on Restrictive Business Practices has identified three main areas where problems in relation to control or policing of the practice of collusive tendering may arise. First of all, there is the problem of effective detection. Second, there is the problem of obtaining sufficient evidence for the purpose of instituting legal proceedings within the framework of the existing laws. Third, there is the problem of deciding on the appropriate penalties and remedies which would render control or policing more worthwhile. It was quite rightly realized by the OECD's Committee that such problems could not be entirely left to be tackled by measures based on antitrust or competition laws. Those problems would seem to require the incorporation of certain administrative measures into rules concerning the procedures normally established for tenders for public contracts. It is necessary to examine each of those problems so as to make it easier for the consideration of measures needed to be introduced to ensure effective control or policing in this area of economic activity.

In relation to difficulties of detection, it has to be realized that the secrecy with which the effectiveness and the fraudulent character of the practice of collusive tendering is surrounded tends to militate against effective detection. The fact that public procurement authorities may unsuspectingly believe that they are dealing with completely independent bids, would tend to render the

deceit or fraud involved in the practice of collusive tendering really effective. Moreover, it would seem that there is more official alertness as regards competitive conduct, such as that practiced in joint bids, joint sales agencies or open agreements not to compete in the course of bidding, which are carried out openly, albeit they are not intrinsically fraudulent, than there would seem to be official alertness in respect to collusive behavior. Added to that, the difficulty of detection would seem to be compounded by the fact that the procurement authorities who receive bids for public supply contracts and are solely responsible for the award of such contracts, are not always sufficiently specialized in the problems of business or commercial competition. Moreover, the antitrust authorities only become aware of signs of collusive tendering when so alerted by the procurement authorities or in the course of an inquiry into a specific sector of economic activity.

For purposes of remedying such an anomalous situation, the OECD's Committee of Experts on Restrictive Business Practices considers it desirable that there should be positive steps taken to bring about close cooperation between procurement officers and antitrust authorities. Moreover, government officials who are concerned with issuing invitations to tender at the national or the local level, should be made more aware of the problems. They should even be regularly invited by the antitrust authorities to provide details of identical or otherwise suspicious bids or of other signs of collusion. On the part of the antitrust authorities themselves, the OECD's Committee suggests that they should be made to carry out thorough inquiries, at regular intervals, especially in relation to concentrated sectors of economic activity, with a view to ascertaining whether bids submitted are, in fact, entirely independent of each other. Of course, it is recognized that the antitrust authorities would only be able to do so for so long as permitted by national legislation. To render control or policing in that area more effective, it is equally suggested that there should be an exchange of information at the national level to acquaint procurement authorities in one region with the level of prices and conditions of similar contracts elsewhere.

Concerning the difficulty of obtaining sufficient evidence for legal proceedings within the limits of the existing restrictive business practice laws, the fact that, with the exception of the Scandinavian countries,¹⁰ the practice of collusive tendering has not been deemed harmful *per se* under the national laws of the other OECD member countries would seem to make matters more difficult. That is because the principle of "abuse" has hitherto been the basis on which such national laws have been invoked and applied. Consequently, it has been left to the antitrust authorities to prove or establish the harmful effects of such a practice on a case-by-case basis. But since the case-by-case

¹⁰Where collusive tendering as a business practice is specifically prohibited.

method would seem to be an arduous and a lengthy method requiring an evaluation of extensive and conflicting evidence, it could hardly be deemed effective in a general sense. Indeed, an examination of the case law of the individual OECD member countries would seem to bear that out. In that situation, legislation which combines rules for prohibiting price cartels and those for prohibiting the practice of collusive tendering may provide or yield some more positive results. It is noteworthy that, in this respect, the OECD's Committee of Experts on Restrictive Business Practices found that to have been so, particularly as was borne out by the experience of the United States. Apart from that, it was found that in the those member countries of the OECD where a general prohibition of price cartels existed, problems of enforcement had arisen as a result of inadequate legal powers or the lack of substantive rules and principles of law covering that area of activity.

Thus, for example, in the Federal Republic of Germany, the mere establishment of the existence of an agreement or such similar conduct, would not be enough under the antitrust law of that country. It would be necessary to go further and establish that such an agreement or conduct has actually been put into operation. Consequently, the antitrust authorities must prove that agreed tenders have been submitted by the parties. But since the parties normally take due precautions not to apply any such agreement in a strict or precise manner with a view to circumventing the law, it would be extremely difficult for the antitrust authorities to prove that agreed tenders have, in fact, been submitted by the parties. It may be expected that such parties may take the trouble to vary their bids slightly to make it appear that there has been no collusion between them. For example, in Canada before January 1976, the Combines Investigation Act which applied basically to goods and not to services, prevented any legal action being taken in a number of cases including the practice of collusive tendering, particularly in the construction industry. However, a recent amendment of that legislation has been effected to cover services. In France, although the practice of collusive tendering is treated as an illegal cartel, the cumbersome nature of the administrative machinery for eventually instituting legal proceedings which may not come about at all, would appear somehow too unwieldy for effective action. This is because, the Technical Commission on Cartels and Dominant Positions has, first of all, to make a detailed economic report, and then to submit an opinion to the responsible Minister. The latter may then decide what legal action, if any, to take. Indeed, the Minister may decide not to institute any legal proceedings at all. Although with the Nordic countries, except Norway, the practice of collusive tendering is specifically prohibited, and price cartels are subjected to the test of "abuse." Such a situation raises some problems as regards enforcement. For example, it becomes difficult to determine the link between the practice of collusive tendering and a decisive influence on the prices quoted in bids, or even to

prove that such a decisive influence on the prices of bids may have existed at all, if only agreements made at the time of invitations to tender are prohibited. This is because a large number of agreements or concerted actions in that sphere would seem to be left out. Moreover, it does not require much imagination to realize that it is possible for collusive behavior on prices to take more subtle forms.

In view of all such difficulties, the OECD's Committee of Experts on Restrictive Business Practices considers it necessary that in most of the member countries of the OECD, strong measures should be taken to strengthen the national antitrust rules against all types of price agreements if the practice of collusive tendering is to be tackled effectively. Moreover, measures are needed to improve collaboration between procurement authorities and their antitrust counterparts. The OECD's Committee also recommends that where it is impossible to establish competition between suppliers, the procuring authorities should resort to some system of purchasing other than by calls or invitations for competitive bids. Equally, by relying on the successful results produced in Great Britain and in the United States, the OECD's Committee suggests, as another course of action, that each bidder should be required to certify in writing that he has not been party to any collusion with other companies or firms, and that he has not informed any other bidder of his intention to bid or of any details of that bid. The Committee considers that such an approach may be particularly useful in those OECD member countries where legislation on restrictive business practices does not specifically prohibit the practice of collusive tendering or price cartels. The Committee concludes from that, that it may prove easier to institute legal proceedings against the practice of collusive tendering on the basis of failure to fulfill obligations connected with certification than it would be under legislation on restrictive business practices.

Lastly, as regards the problem of what penalties and remedies should be devised to ensure the viability of the control or the regulation of the practice of collusive tendering, it would seem necessary that a clear-cut distinction should be made between collusive tendering of a secret and fraudulent character on the one hand, and joint bids or other forms of agreement for bids not influenced by deceit or fraud on the other. Such a distinction needs to be reflected in the legal penalties or sanctions sought to be imposed. Touching nonsecret and nonfraudulent tendering agreements which are openly operated and take the form of cooperation or rationalization agreements or joint tenders, the OECD's Committee of Experts on Restrictive Business Practices would seem to suggest that legal penalties or sanctions should not be applied to them. However, the Committee would appear to favor their strict regulation under national restrictive business practices laws to the extent permitted by staff resources and legal means. This should be so provided that small and medium-

sized enterprises have access to the various legal forms of cooperation which would allow them to be on an equal competitive footing with large enterprises. For the purposes of exercising strict control over such agreements, the Committee would like to see the procurement authorities allow large contracts or complex public works requiring preparation of detailed estimates to serve as a pretext for concerted action by companies or firms. In such cases, the public authorities should be entitled to refuse to accept jointly prepared estimates, and be able to refund part of the costs incurred by those who submit serious estimates. However, bearing in mind the Danish experience on that score, the Committee advises the exercise of the utmost caution in the use of that option.

On the other hand, the OECD's Committee of Experts on Restrictive Business Practices is in favor of a strong line being taken in relation to secret and fraudulent agreements between companies or firms which take part in responding to invitations to tender for public contracts. The Committee would like to see an outright prohibition of such agreements without requiring economic analysis of its implications for the public interest in every case. More directly, the Committee would advise any member country of the OECD which has not so far introduced criminal sanctions with respect to the practice of collusive tendering of a secret and fraudulent nature to do so. This could be an alternative to administrative sanctions. But that presupposes that the national law of any such member country prohibits the practice of collusive tendering or of price cartels. The Committee would also like to see the state, local authorities or private individuals suffering from the effects of particular practices of collusive tendering, given the right to institute civil proceedings for damages against culprits. In that respect, aggrieved competitors should also be allowed the same right. Treating civil proceedings as indirectly supplementing and strengthening the criminal penalties, the Committee considers that the former may constitute an important deterrent against the practice of collusive tendering. The Committee considers that such conclusion is borne out by evidence in the United States in the *Heavy Electrical* case. In that case, fines amounting to about \$2 million were imposed on the culprits concerned. At the same time, civil proceedings were instituted by the United States government and by the Tennessee Valley Authority against one of the firms convicted,¹¹ and the latter resulted in the payment of more than \$6 million damages by that firm. Furthermore, numerous civil proceedings were instituted by private individuals for treble damages in connection with the same set of cases against several defendants which resulted in the payment of damages of more than \$360 million.

An Overview

The problem of state action in favoring national enterprises against foreign

¹¹The General Electric Company.

or outside companies or firms when accepting tenders for public works, on the one hand and the practice of collusive tendering on the other may be different in nature and scope, but they would seem to lead to the same or similar economic result. Such economic result is the inefficient utilization of scarce economic resources, especially when unnecessary price increases would seem to be generated thereby. There would not seem to be any clear and easy solution to the problem that individual states are in the practice of favoring their own national enterprises in the granting of public service contracts. But where regional economic groupings are established with a view to creating customs unions or free trade areas, the need for legal control of discrimination in the award of public works contracts would seem to arise. The situation of the EEC provides a good example of that. It would not seem difficult within the context of a customs union or a free trade area, for effective action to be taken to ensure the proper advertising and awarding of public service contracts to the most efficient companies or firms, regardless of their nationality. It is part of the very essence of a common market for goods and services, that invitations to tender for public contracts and the award of the same should be free of all types of discrimination on the basis of nationality. This latter, the EEC indeed has been able to achieve within its economic-legal framework.

The more difficult problem concerns the practice of collusive tendering which may take place within a state's own economic system and be detrimental to it. Here, of course, the culprits are not states, but individual enterprises. In that respect, it falls to the turn of individual states to introduce measures to forestall such practices. The problems about effective means of detection in relation to that practice, the lack of sufficient evidence for the purposes of prosecuting or of instituting proceedings within existing legal frameworks, and the need for determining the sort of penalties and remedies for dealing with that practice, would not seem to be insurmountable. The OECD's Committee on Restrictive Business Practices suggestions for improvement in the existing legal machinery may be said to constitute an advance on existing legal rules and procedures for dealing with the practice of collusive tendering. Most of those suggestions, such as those concerning the need for close cooperation between procurement authorities and antitrust authorities, the need for thorough investigations into bids made by enterprise, the collection and collation of data and information, the need for other administrative measures to supplement the operation of the machinery created under the existing legal rules, may be commonsensical enough.

But it requires something more than common sense to gauge the workings of certain psychological forces within such an area of economic activity. Thus, when it is required that a bidder should certify in writing that he has not been a party to any collusion with other firms, and that he has not informed any other bidder of his intention to bid or of any details of that bid, the effectiveness of

that requirement as a psychological sanction, could hardly be underestimated. Touching sanctions and remedies, the idea that not only the state and local authorities, but also private individuals suffering or aggrieved by a practice of collusive tendering should be entitled to institute civil proceedings for damages against culprits, in addition to criminal proceedings and penalties, is quite a useful one. Indeed, one could do no better than agree with the OECD's Committee of Experts on Restrictive Business Practices that such a powerful combination of civil and penal sanctions would be bound to produce a most effective deterrent against the practice of collusive tendering. Equally, the distinction drawn between secret and fraudulent bids on the one hand, and open and genuine ones on the other for the purposes of imposing sanctions and for the provision of remedies, is an important one. Not only does it make good legal sense, but it also makes good economic sense.

Conclusion

Economic and legal reasons are readily available for condemning the practice of collusive tendering in respect to public service contracts. For economic reasons, it may be said that the practice is wasteful of scarce economic resources and imposes an unnecessary burden on the taxpayer. The consumer also suffers in that he is required, more often than not, to pay higher prices. This would tend to keep inefficient companies or firms in business. For legal reasons, it would seem quite obvious that secret and fraudulent deals to defeat the ends of the law or those of economic or social standards, are morally and legally reprehensible and therefore need to be condemned. Those who engage in that practice, therefore, need to be penalized. From the point of view of international business competition, the fact that companies or firms outside a particular state, but which companies or firms could easily be awarded public supply contracts on the basis of their efficiency and low costs, are actually prevented from being awarded such contracts because of the practice of collusive tendering by other companies or firms, mostly national ones, would seem to militate against any meaningful idea of an efficient international business practice or standards. In that respect, the OECD may be said to have laid a strong basis for effective action by states. Considering that there are twenty-four member countries¹² and one country with a special status¹³ which make up the composition of the OECD, the recommendations made by that body's Committee of Experts on Restrictive Business Practices deserve very careful and ready attention.

¹²Namely: Australia, Austria, Belgium, Canada, Denmark, Finland, France, the Federal Republic of Germany, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States of America.

¹³Yugoslavia.

