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COMPETITION COMMITTEE**

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Working Party No. 3 on Co-operation and Enforcement

**PUBLIC PROCUREMENT - THE ROLE OF COMPETITION AUTHORITIES IN PROMOTING
COMPETITION**

-- Hungary --

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The attached document is submitted by Hungary to Working Party No. 3 of the Competition Committee FOR DISCUSSION under item VI of the agenda at its forthcoming meeting on 5 June 2007.

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1. Public procurement procedures are regulated by Act CXXIX of 2003. This Act is fully harmonised with the relevant EC directives. It sets general rules on the issue and frames the specific rules on the different types of procedures. As it does not contain specific provisions on bid rigging, undertakings colluding to restrict competition among themselves regarding a particular tender are therefore subject to the general prohibition of restrictive agreements under the Competition Act and the enforcement activity of the competition authority of Hungary, the GVH.

2. In the previous years the GVH conducted a number of investigations of alleged bid riggings. Based on its own and international experiences the GVH issued a leaflet for procurement officials containing indicators of rigged bids. It plans the adoption of a new, more in depth paper in the near future. The GVH also became active in terms of advocacy along two main lines. One is the defence of the effective applicability of the Competition Act, the other is the advocating of procedural rules that would make the creation of a cartel more difficult. While successful in the first type of its attempts, the recommendations relating to the design of public procurement procedures mainly remained ineffective. The first, unusually high fines imposed on construction cartels raised public awareness on the issue and caused lively political debate and increased legislative activity peaking in the criminalisation of such cartels in 2005. Having regard to the effective deterrence that might derive from private enforcement, the President of the GVH sent letters to the representatives of entities damaged by cartels prosecuted by the GVH raising their attention to their possibility to claim such damages before court.

1. Individual procedures

3. The GVH closed 20 investigations relating to cartels in public procurement procedures 15 of which ended with prohibition decision and fines. At this moment eight procedures are in process. The procedures mainly related to construction cartels (highways, roads, buildings) and IT services. Often the procedures were not initiated on the basis of information received from procurement officials but were based on direct information on the existence of the cartel deriving from other sources e.g. former employees, information from the police. Therefore the procedures were mostly initiated with dawn raids almost always presenting direct evidence, so the assessment of the design of the procurement procedure or the analysis of possible indicators of illegal collusion was not necessary in the early stages of the investigations. However certain general observations can be made on the basis of experiences.

4. In many cases the contracting authority reduced the number of bidders with the application of either restricted procedures, or through the exclusion of participants due to formal errors in their offers. It seems that this circumstance highly facilitated the establishment of cartels, or otherwise contributed to an increase of the offered price. Sometimes such a restriction even seemed to be rather questionable. In one case after the first (rigged) tender was dismissed, the work was won in the second round by an undertaking that was considered incapable for the works and was excluded from the first procedure.¹ It also happened, that though the contest organizer preliminarily established that all five participants were able to complete the works, it started negotiations only with three of them, who later actually rigged their bids.² In an other case after the exclusion of four of the five participants, the fifth party was informed before the negotiations that it is the only participant still in competition. Having received that information the final price offer of the fifth undertaking submitted during the negotiation was even higher than the one given in the second, rigged bid after the dismissal of the first procedure.³

¹ Case Vj-20/2005

² Case Vj-28/2003

³ Case VJ-74/2005

5. It seems to be true that the more bidders are present in a tender, the greater the uncertainty about winning. The importance of uncertainty is clearly identifiable in a case where several e-mail messages were sent to a competitor a week before the deadline for the submission of the bids, urging it to express agreement on the cooperation and complaining that there might be problems with its mobile phone as he was unreachable for several attempts.⁴ Therefore though with regard to administrative costs it seems acceptable to rank and then restrict the number of suppliers in negotiated or restricted procedures, contracting authorities should also take into account the increased likelihood of cartels in such situations. Setting unnecessarily strict technical requirements for bidders can also be a source of significant competitive harm. However, some restrictions may be necessary, if low-balling bidders (who bid unrealistically low, gambling on a later contract renegotiation, and if this does not happen, letting the deal fail) are to be excluded.

6. Though it does not belong to the powers of the GVH to discover collusion between the contract organiser and the competing undertakings, it is obliged to report possible violations of the Criminal Code identified during its procedure to the criminal authorities. In a case concerning the procedure for the joint purchase of IT services for a number of universities the GVH established the existence of the cartel and as it considered that an official of the contracting party cooperated with the competitors it submitted a denunciation to the public prosecutor. Though first refused, upon a complaint of the GVH against that refusal the investigation of the police was finally initiated.

7. A recent case also seems to support that in certain cases officials of the contract organiser collude with the undertakings participating in the tender. An investigation of the GVH was closed due to the lack of sufficient evidence on a cartel concerning the purchase of IT services by the Ministry of Defence. This was so because the GVH was not able to collect enough evidence during its dawn raids and the Ministry has – in breach of the Act on Public Procurements – destroyed documents related to the given tender.

2. General guidance for procurement officials

8. In 2006 the GVH published a leaflet providing guidance for procurement officials. The leaflet presented the legal and economic background as well as major characteristics of cartels in general. It also enumerated a number of formal and substantial circumstances that might indicate that the bids are actually rigged in a given procedure. In its final part the paper presents the main lines of a competition supervision procedure, including the application of leniency policy. The leaflet was mainly based on a Canadian brochure supplemented by the experiences of the GVH.

9. As formal indicators of a possible collusion the leaflet enumerates:

- a bidder submits a competitor's bid as well,
- the bids contain the same mistakes, typo,
- the look and appearance of the bids are similar,
- the same annexes, attestations etc. are missing,
- information is available that the bidders actually met, or negotiated during the period for making the bids,
- a bidder seems to be aware of the content of its competitors' offers.

⁴ Case Vj-21/2005

10. As substantial indicators the leaflet stipulates:

- bidders indicate the same prices, identical in their details too,
- there is a considerable difference between the lowest and the other bids,
- a new supplier offers a price previously not typical on the market, and the other bidders follow it,
- almost always a given undertaking provides the winning bid, and it invites the competitors as subcontractors,
- bidders name each other as subcontractors in their offers (formally illegal according to the Act on Public Procurements),
- it is revealed that only one of the bidders has actually turned to the upstream suppliers for offers,
- the winner withdraws thereby forcing the contracting entity to choose the second best (likely behaviour in case of “beauty contests” where the colluding parties can not predict the exact outcome of the procedure),
- the offer of the local competitor contains the same transport costs as that of distant competitors,
- bidders invoke the “industrial price lists” in their offers.

3. Advocacy

11. The GVH attempted to influence the design of public procedural rules in order to reduce the possibility of collusion. Concerning the Competitive Dialogue Procedure⁵ the GVH noted that if conducted in a way that all participants may be present on a single dialogue with the contracting authority, then the procedure can function as a room for exchange of information facilitating collusion in a later stage of the tender. The GVH therefore suggested that competitive dialogue should not be organised in a way that competitors are present together. This opinion of the GVH was not introduced into the Act and now it depends on the will of the competitors whether the discussions are organised separately or together with the other undertakings.

12. The GVH also signalled that the possibility to enter into framework agreements⁶ up to four years makes the sharing of the market easier. It was suggested, that the maximum time frame should be reduced to two years. This suggestion was not heard either.

13. It was also recommended that the Act should provide the possibility to contracting authorities to suspend or declare void the procedure and to turn to the GVH, should they suspect that it is affected by a

⁵ Competitive dialogue procedure is a public procurement procedure where the contracting authority conducts a dialogue with the candidates admitted to that procedure in accordance with the provisions of the Act, with the aim of laying down the specifics concerning the subject matter of the procedure or the type and conditions of the contract within the framework of the requirements set out by the contracting entity, and on the basis of which the candidates chosen are invited to tender.

⁶ A framework agreement is an agreement between one or more contracting entities and one or more suppliers, contractors or service providers, the purpose of which is to establish the terms, in particular with regard to the prices and, where appropriate, the quantity envisaged, governing the contracts to be awarded during a given period.

possible collusion among the bidders. In the stage of appeal the Public Procurement Arbitration Committee would be authorised to the application of such measures. Though the Committee does have the power to bring interim measures in certain cases, like the suspicion of the existence of a cartel, no explicit provision on this matter was introduced into the Act.

14. The GVH submitted a recommendation that a tenderer should not be allowed to submit a joint tender in the same public procurement procedure with another tenderer, and it should not be allowed to participate in that same procedure as a subcontractor proposed to be contracted for a value in excess of ten per cent of the value of the contract. This proposition was endorsed by the Parliament.

15. A successful advocacy initiative related to an additional sanction of collusion in past procurement procedures. According to the original text the contracting authority was entitled to exclude participants if they were found by the GVH to be members of a cartel in a previous procedure within the last five years. The GVH considered that such a possibility can have a negative effect on willingness to cooperate with the GVH in the framework of leniency policy. Upon its recommendation the Act was amended and only those undertakings can now be excluded from the procedure, which were found to be in breach of competition law and were the subject of a fine. This way undertakings profiting from full leniency are not threatened by the possible exclusion of future proceedings while the additional sanction on the other perpetrators remained effective.

4. Criminalisation

16. A record fine imposed in a highway construction cartel raised considerable political attention to the problem of cartels in public procurements. Draft legislation was soon submitted qualifying restrictive agreements in public procurements as crimes punishable up to 5 years imprisonment. Though a number of inconsistencies were highlighted by the GVH during the adoption of the new penal provision (e.g. inconsistencies in the notion of undertaking, or agreement used by the Penal Code and the Competition Act), the main advocacy effort was to keep the functionality of the leniency policy unharmed. The original draft did not contain any rules on exemption from criminal liability but due to the intervention of the GVH the law maker introduced a section according to which criminal liability is ceased if a perpetrator informs the authorities about the cartel before it have already got known about it. However a general problem remained that no procedural background was created between criminal and administrative procedures (see to that effect the presentation of Hungary on the February 2007 meeting of WP3 on cooperation with public prosecutors).

17. In sum the introduction of the new provision rather constituted the criminalisation of public procurement law than that of the competition law.

5. Raising awareness

18. In line with the efforts of the European Commission the GVH would also like to increase the role of private enforcement in the field of antitrust. Beside making possible the direct initiation of litigation without prior decision of the GVH establishing the cartel, the GVH also insists on the raising of public awareness on the availability of damages claims. Together with other steps related to cartels in general, the President of the GVH sent letters to the entities⁷, which as contracting authorities were damaged by public procurement cartels previously discovered and sentenced by the GVH.

⁷ Ministry of Education, Municipality of Budapest, Paks Nuclear Power Plant, a public undertaking in charge of the construction and maintenance of highways, the public pension fund, the local transport company of Budapest and a number of universities

19. The letters relied on and contained as annex the final decisions of the GVH. They called to the attention that damage claims are limited to five years calculated from the date of the actual occurrence of the damage. The letters also emphasised that as the existence of the cartel was established by the GVH and as its decision is binding on civil courts only the amount of the damage would form subject of the litigation. The GVH also offered professional assistance in case of need.

20. Though sent in March, up till now only one of the former contracting authorities signalled to the GVH that it intends to start litigation for damages. It also asked for legal assistance from the GVH.

21. An other initiative of the President of the GVH for raising awareness was sending a letter the Prime Minister. The document contained a number of suggestions partly of advocacy nature. One suggestion related to bribery. As in some cases it was only suspected, while in other cases it was rather clear for the GVH that an official of the contracting authority colluded with the competitors, the GVH recommended to strengthen the supervision of officials organising the tenders not only in respect of legality but also from the point of view of rationality and efficiency, thereby ensuring that an open and efficient competition serving public interest is actually taking place. Connected to this suggestion it was also recommended that civil and administrative consequences should be strictly applied against officials who willingly or negligently negatively influence the outcome of the procurement procedures.

22. It was also supported to create an electronic database of all public procedures enabling the analysis of the cases based on reliable data.

23. The GVH stressed that the effectiveness of sanctions highly depends on the length of the procedure before the decisions actually become final before court. It was recommended that the Minister of Justice and Law Enforcement should submit a proposal to the National Council of Judicature to the privileged treatment of cases related to the appeals of decisions of the GVH in terms of their time frames.

24. An other recommendation regarding contest organisers was that they should actually apply the sanction of the Act on Public Procurement which allows the exclusion of undertakings from present procedures should they be found to be in breach of the competition act and fined in a previous procurement procedure by the GVH.

25. It is not yet known whether and to what extent these recommendations would be heard.