



**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

**DAF/COMP/WP3/WD(2007)37
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Working Party No. 3 on Co-operation and Enforcement

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

-- Lithuania --

5 June 2007

To be held on 5 June at the OECD Tour Europe, 33 Place des Corolles, 92049 Paris la Défense Cedex, starting at 10am.

Please contact Mrs Wendy Houët if you have any questions regarding Working Party No. 3 [phone number:+33 1 45 24 95 59; Email address: wendy.houet@oecd.org].

JT03227734

PUBLIC PROCUREMENT – THE ROLE OF COMPETITION AUTHORITIES IN PROMOTING COMPETITION

Lithuania

I. Oversight of public procurements and inter-institutional cooperation

1. In Lithuania public procurement tenders in accordance with the Law on Public Procurement are regulated and executed by appropriate institutions and organisations among which the most important are the Public Procurement Office¹, the Central Project Management Agency² and the Lithuanian Business Support Agency³, that within the limits of their respective competence carries out the examination and check-up of such tenders.

2. Public procurement tenders are the vehicles that attract as participants huge numbers of companies and realise significant funds that are increasing on a year-on-year basis. Whereas in 2004, in Lithuania via the public tender procedures the amounts of the funds realised by way of public tenders reached about LTL 3.8 bn⁴, in 2005, the total value of public tenders in 2005 grew to a significant extent and accounted for LTL 5.5 bn⁵, with as much as LTL 1.6 bn during the second quarter of 2006⁶. Naturally, in the course of the last several years competition in the area of public procurement tenders has gained very soon. Accordingly did strengthen the cooperation between the Competition Council of the Republic of Lithuania and all other authorities operating in the area of public procurement. The legal basis for this cooperation has been established in Article 8 of the Law on Public Procurement. On the basis of the information provided by the above institutions and authorities the Competition Council conducted a number of investigations (Resolution No. 2S-9 of 22 June 2006, Resolution No. 2S-3 of 1 February 2007, Resolution No. 2S-6 of 15 March 2007 of the Competition Council and other Resolutions). However, no special training activities tailored for officers in charge of the oversight of public procurement in conjunction with the specialists of the Competition Council have been launched as of today. Lately, the need for this kind of training have become specifically actual, therefore a possibility to launch training of officers of the above institutions and authorities has been provided.

1 <http://www.vpt.lt/index.php?lan=LT>

2 http://www.apva.lt/lt/main/about_us/apva

3 <http://www.lvpa.lt>

4 <http://www.vpt.lt/index.php?lan=LT&pid=1089185360&cid=1143702725>

5 <http://www.vpt.lt/index.php?lan=LT&pid=1089185360&cid=1143702725>

6 <http://www.vpt.lt/index.php?lan=LT&pid=1089185360&cid=1167719431>

Relation of the Law on Public Procurement with the Law on Competition of the Republic of Lithuania

3. The authorities announcing and supervising the public tenders act in accordance with the Law on Public Procurement and a number of the European Union rules governing public procurements. In Lithuania the oversight of the public procurement procedures is executed by the purchasing bodies and the Public Procurement Office. The contracting authority shall ensure in the course of performance of procurement procedures and award of contracts compliance with the principle of equal treatment, the principle of non-discrimination, the principle of mutual recognition, the principle of proportionality and the principle of transparency. In terms of competition the procuring body is obligated to execute such tender documents that establish non-discriminatory selection criteria able to ensure a genuine competition, i.e., the technical specifications provided in the contract documents shall ensure competition and non-discrimination in respect of suppliers, and the qualification selection criteria shall be clear and established in observance of the principles of non-discrimination and equal treatment of suppliers. The minimum levels of qualification requirements for candidates or tenderers fixed by the contracting authority may not have the restrictive effect on competition, and must be reasonable, clear and precise.

4. The procedural issues related to public procurement within the limits of their respective competence shall be addressed by the purchasing organisation and the Public Procurement Office, and the court in cases provided by the law. Upon suspicion of an infringement of the Law on Competition in the course of the public procurement procedures the purchasing organisation shall suspend the procurement course and notify the Competition Council accordingly. However, both the procuring body and the Public Procurement Office may act only within the limits of a specific procurement, i.e., from the moment of announcement of a procurement until the conclusion of the public procurement contract. Therefore, upon the completion of the public procurement procedure these authorities do not have the power to declare the results of the tender non-valid.

II. Investigation techniques in public procurement tenders***The activity of the Competition Council in investigating the agreements in the area of public procurement tenders.***

5. Such cases of agreements fall within the scope of Article 5 of the Law on Competition “Prohibited Agreements”⁷. The public procurement tenders constitute a form of direct competition that is sufficiently intense and short-term, in which the awarded companies may shortly enjoy the result of the tender in the form of the awarded tender object. Although the Competition Council does not directly exercise the enforcement of the Law on Public Procurement, the competition behaviour of such companies in the course of the tender, i.e., the method of obtaining the tender award has a potential of affecting competition and distorting it where the tender is awarded to the tendering companies by way of unfair competition through mutual agreements. The Competition Council carried out in total 8 investigations on alleged agreements in the area of public procurement tenders^{8;9}; only two of the cases were examined in courts and won by the Competition Council. In three cases companies presented the admissions and the Leniency programme were applied.

7 <http://www.konkuren.lt/english/antitrust/legislation.htm>

8 <http://www.konkuren.lt/english/cases/cases.htm>

9 <http://www.konkuren.lt/english/antitrust/legislation.htm>

6. The agreements between the companies for the purpose of the participation in the tenders do adversely affect competition in general, both in term of a long-term and the short-term perspective. First, it is a short-term effect of "now and there", where the tendering companies conclude an agreement and win a tender thus dramatically distorting normal competition between the tendering companies in respect of a single specific tender, thus incurring damage to the organisers of the tender and the ultimate consumers especially in cases of increase of the price agreed upon among the tenderers. Second, the long-term affect, since such "successful" tender awards gained through the agreement between the tendering parties may serve as a signal to other participants of the relevant market of a possibility to win a tender through the conclusion of an agreement. Furthermore, certain relevant markets may start serving as a grounds for emerging of permanent company groups on a regular basis tendering for the public procurement awards.

7. For example, in the investigation carried out by the Competition Council in response to the letter of the Government of the Republic of Lithuania concerning a possible agreement for the purpose of a public procurement, *JSC Sobo sistemas*, *JSC Lambertas* and *JSC Termofora* were established to have been participating in the tender announced by 2005-2006 by the Educational institutions services of the Klaipėda city municipality for the public procurement for the general education schools and pre-school educational establishments and had agreed that *JSC Lambertas* will be awarded the tender for the general educational schools and *JSC Sobo sistemas* – for pre-school educational establishments. The companies furthermore had been preparing the tenders in assistance to each other and were establishing the prices in respect of their competitors. In the course of the investigation all companies concerned furnished to the Competition Council admissions that their employees in charge had agreed with the competing companies concerning the sharing of the tenders in question (Resolution No. 2S-6 of 15 March 2007 of the Competition Council¹⁰). In another investigation conducted on the basis of the application filed by the Lithuanian Business Support Agency the Competition Council sought to assess the compliance with the requirements of Article 5 of the Competition Council of companies participating in public tenders for the preparation of projects for the EU structural support for the energy projects procurements. The investigation found out that the tenderers for the building energy audit, investment projects and the drafting of applications for the EU structural support were *JSC Eurointegracijos projektai*, *PE Perspektyvių inovacijų agentūra* and *JSC Apskaitos sprendimai*, that had agreed that 14 tenders will be awarded to *JSC Eurointegracijos projektai* (Resolution No. 2S-9¹¹ of 22 June 2006 of the Competition Council).

The concept of a relevant market in public procurement tenders

8. The tenders carried out on the basis of public procurement are limited in terms of time, location and the number of participants. The tender itself is a certain arena of an extremely intensive and direct competition between the competing companies. In the broad sense of the word the procurement tender is part of the relevant market of the country involving a small share of the companies being part of the relevant market. The companies participating in such tenders remain free from any competitive pressure of other companies not participating in the tender, but nevertheless active in the entire relevant market on the national scale.

9. For the purpose of the prohibited agreement investigations conducted by the Competition Council of the Republic of Lithuania the public procurement tender is defined as a relevant market in which companies seeking to ensure the award in the tender may participate having made an agreement in this respect. Such relevant market of the public procurement tender is highly concentrated¹² and provides a

10 <http://www.konkuren.lt/nutarimai/bendri.htm>

11 <http://www.konkuren.lt/nutarimai/bendri.htm>

12 Bidding Markets, P. Klemperer, 2005, UK Competition Commission, 2005, <http://www.paulklemperer.org/>; P. Klemperer, Auctions: Theory and Practice, Princeton University Press, 2004, <http://www.paulklemperer.org/>;

potential for the emergence of the relations between companies equivalent to those existing in the general relevant market of the country (dominance, agreements, etc.)

The impact of the position of the companies upon the public procurement tenders

10. The experience accumulated by the Competition Council has shown that the position of the companies in respect of each other in the relevant markets, whether they are strong competitors, their market shares, market power in particular when the companies hold dominant positions may affect the behaviour of other companies in public procurement tenders. In this respect the public procurement tenders exactly in the same way as the in the relevant markets may be affected by the dominance of major companies that may eventually distort normal competition between companies. In such cases other companies should seek possibilities to join their efforts for the purpose of tendering through the formation of a variety of forms of legal combinations. The Lithuanian experience, however, show that such cases in the public procurement tenders are yet not frequent. Such market power effect may often be manifested in the situations where companies apply to the tenders jointly with their satellites, thus monopolising the relevant public procurement tender market, irrespective of whether the tender is an isolated undertaking, or whether there is a series of similar tenders in the same area, i.e., the relevant market (see for comparison^{13,14}).

The impact of the level of linkage between the companies upon their behaviour in the public procurement tenders

11. The behaviour of tenderers for public procurement may also be influenced by the level of the inter-linkage of the participating companies. The participating companies may be related through their cross-holdings. In such cases a natural question arises to what extent companies may be interlinked in order to be able to independently participate in such tenders.

12. The companies do have a right to enter into competition even when they are inter-related. However, for the purpose of the prohibited agreements investigations carried out by the Competition Council, in particular when acting upon a complaint concerning an alleged agreement between related companies, there is a space for legal uncertainty. The Law on Public Procurement of the Republic of Lithuania does not provide for any procedures for the assessment of the inter-linkage of the companies in terms of providing a clear-cut answer as to the possibility of inter-linked companies to participate in the tenders. No such procedures have been made operational equally by other authorities related to the public procurement.

13. In this respect there should be a sufficiently clear cut interrelation between the provisions of the Law on Public Procurement and the Law on Competition. Since in theory one company could be well aware of the tender price offered by one of its branches, the question is whether in this situation the company is still entitled to independently participate in the tender submitting its individual tender. Therefore it is of utmost importance to draw up an unambiguous conclusion on the presence of the legal basis from the point of view of competition for the investigation of possible agreement in view of a suspicion regarding the agreement between companies related up to this degree. The experience of the Competition Council has recorded possible cases where due to an extensive linkage between the companies that in accordance with the Law on Competition exceeds the limit of 25 % investigations concerning the prohibited agreements in case of the participation of the companies in public procurement tenders may be terminated.

13 P. Klemperer, Bidding markets, June 2005, <http://ideas.repec.org/p/wpa/wuwple/0508007.html>

14 P. Klemperer, Auctions: theory and practice, Princeton Univer. Press, 2004; and OECD introductory letter to Roundtable, OECD COMP/2006.69, 3 July 2006

Other factors possibly influencing the agreements among companies in public procurement tenders

14. The larger is the number of tender participants, the smaller is the probability of the agreements between them. Experience has shown that agreements for the purpose of tendering are concluded between 2-3, more rarely between 4-5 tender participants. The impact of the number of participants upon the tenders have been thoroughly analysed and described in analytical studies¹⁵.

15. The issue then is whether in view of a larger number, say 5 or 7, of participants of a public procurement, and having established an agreement to have been concluded by 2 or 3 companies, there is an *a priori* ground for a suspicion that the remaining companies could have also been part of the agreement. Where the purpose of the agreement is to win the tender or increase the tender price, the question arises whether other companies that had not been part of the agreement could have possibly won the tender by having offered a lower price? On the other hand, grounds for a suspicion can be provided by any tender applied to by only two or three companies of which one is a clear market leader, others being smaller players and weak competitors of the leading company.

16. The experience of the Competition Council has shown that tender participants are not equivalent or identical and there are always some companies able to perform the tender works at lower prices (for instance, where the tender object is in the vicinity of the companies' locations) therefore they could easily offer lower prices. Therefore for the purpose of an investigation often an attempt is being made to exclude companies potential winners and compare the analogous tenders in which such companies had been announced the winners. The trend has been particularly evident in targeted public procurement tenders in individual regions. The issues still need to be further examined and analysed with due reference to the experience accumulated in the field.

Analysis of the strategy of participation of the companies in public procurement tenders under agreement

17. Having examined the prohibited agreements in the public procurements tenders the Competition Council has established a number of methods and motives driving the companies in coordination of mutual actions prior to the submission of their tenders

18. The principal issues that the tendering companies seek to agree on are the winner of the tender and a possible ultimate price of the winning tender. Other companies that are not awarded the tender must be also sufficiently motivated not to compete and surrender to the winning company. For that purpose the winning tenderers often undertake to contract works or purchase goods or services from such surrenders.

19. Another method quite frequently observed referred to by the tenderers for the purpose of coming into agreements is a refusal by potential competitors in turn to participate in analogous tenders not applied to by the winner of a previous tender. An opposite situation emerge with a certain sequence of winners or a repeated occurrence (rotation) in series of analogous tenders. In such cases the winner of other tenders play a role of a supernumerary who place a tender with an expressly higher price or containing a range of technical inadequacies in view of which the tender will be knowingly rejected.

20. According to the experience accumulated to date the comparison of the amounts awarded through the public procurement tenders to the winners in particular those dominating in the relevant markets in the

15 P. Klemperer, Auctions: theory and practice, Princeton Univer. Press, 2004 (Chapter 1: A survey of Auction theory), <http://www.paulklemperer.org>

course of a year or in long-term periods remain on more or less similar levels, i.e., the winners ordinarily generate similar or at least comparable profits (the trend has been in particular notable in the relevant markets for construction and road building).

The strategy of tendering in permanent groups

21. This actually represents one of the participation strategies overall prohibited by the Competition Council in relation to the participation in tenders and which is closely related to the position of competing companies in the relevant markets. Such agreements have been noticed as occurring in tenders involving companies from the markets with a few larger companies, often of regional scale and a number of small companies (e.g., in the relevant markets of construction and road building).

22. In such cases one or another major companies will be nearly in all cases participating in the tenders with their permanent “satellites” that for a number of years “have failed to win”. In such cases the tender is being dominated by a group having its own leader, which in essence means that the tender, as a relevant market, is monopolised.

23. It has also become evident that companies that never win in the tenders still benefit from such "regular" or "loyal" participation in the tenders jointly with major participants leading in the markets concerned. This includes contracted works, subsequent minor tenders, the overall “deterrent” effect, since externally it looks like the tenderers are only the best performers of the region, operating in the vicinity of the tender object and for the “outsiders” it is not really worth while even participating in the tender. In theory, entry of a company from the outside is not impossible, but often they prefer not to take the risk knowing that in response the winners of the tender may appear on the stage on the occasion of the next tender in their region.

Methods of establishment of the prices for the agreed tenders

24. When entering into an agreement concerning the tender price companies most often refer to the preparation of a tender price for their competitor. Where the companies prepare their tenders individually, they agree to increase the tender price offered by the competitor by a certain percentage or a coefficient, by multiplying the actual price. Upon the agreement concerning the winner the companies would normally seek to increase the price above the competitive levels, therefore any appearance of a new company that could destroy the “plans” conceived by the participants seeking an agreement, pose a threat to the tender participants. Where the companies tender having formed certain groups, such monopoly effect enable the agreement members to significantly increase the tender prices.

25. Where the purpose is to imitate an “intensive” competition in the tender the companies, members of the agreement may refer to a slightly more elaborated pricing strategy – some will offer lower tender prices while on purpose making certain “errors” of technical character rendering the tenders obviously ineligible.

III. Further strengthening of competition in the public procurement area

26. Public procurement tenders involve large numbers of companies therefore it is absolutely necessary, in conjunction and cooperation with other authorities governing the public tender procedures, to develop a joint programme not only establishing the procedures and requirements of public procurement, but also contain an explanation of competition peculiarities in relation to such tenders, the possibility of enforcement of the Law on Competition and the possible statutory sanctions.

The methods of establishment of the fine for companies participating in tenders having concluded an agreement

27. The examination of cases concerning the participation in the tenders under an agreement raises a number of issues that could play a role in the setting up of a final amount of the fine. In public procurement cases the duration of the infringement is defined as the duration of the tender itself from the moment of its announcement to the conclusion date, normally 2-3 months. The tenders thus shall not be attributed to long-term undertakings, therefore the fine excludes the component thereof that could be otherwise imposed for the duration of the infringement.

28. Normally in addressing the issue of the fine imposition the Competition Council is being guided by a practical consideration that the amount of the fine must ensure the recovery of the illegitimate income gained by the "successful" tenderer, i.e., the amount of the tender order awarded through an unfair competition. Naturally, the imposition of the fine shall take into account the economic position of the infringer, its market share and the market pore in the entire relevant market, which actually shows the damage that can be possibly incurred to competition in such market by the behaviour in tenders by the company concerned.

Possible imposition of a non-participation sanction upon members of the agreement

29. As seen from the experience of a number of foreign organisations (e.g., the World Bank, and others, Competition Council Case No. 16/b¹⁶), there is a practice where the companies having been punished for tendering in agreement are deprived of a right to participate for a certain time (1-2 years) in tenders announced by the same authority. The experience of the Competition Council¹⁷ shows that the expediency of the imposition of such sanctions by all authorities responsible for the public procurement oversight, in particular considering information on repeated attempts of companies that had once been sanctioned for prohibited agreements under the Law on Competition, again to conclude agreements in other public tenders.

IV. Conclusions

30. Additional disciplinary and deterring measures must be introduced in the area of public procurement tenders to be imposed upon the tender participants concluding agreements. Such sanction could be in the form of a depriving of the infringing companies of the right, for a certain period of time, to participate in public procurement tenders announced by a certain institution.

31. It is necessary to further increase the awareness of the peculiarities of the application of the competition law in public procurement tenders. The participants of such tenders should well comprehend that competition law is in an increasing extent being applied in public procurement procedures and the fines for the agreements for the tendering purposes are sufficient to serve as an efficient deterrent factor to enter into such agreements.

32. Provisions should be sought to ensure a closer and clearer link between the Law on Competition and the Law on Public Procurement. The public procurement tenders carried out in accordance with the public procurement procedures should involve the analysis of the links between the participating companies. In the event the companies are related to the extent that from the point of view of concentration

16 <http://www.konkuren.lt/english/cases/cases.htm>

17 <http://www.konkuren.lt/english/antitrust/legislation.htm>

provisions laid down in the Law on Competition such companies should be regarded as one entity, they should be required to submit one joint tender. In an opposite case such related companies for the purpose of the investigation of prohibited agreements should be treated as independent companies able to conclude prohibited agreements.

33. Efforts are being taken to further strengthen cooperation with other institutions and authorities organising and supervising public procurement tenders, including the Public Procurement Office. A conclusion offers itself that the bilateral contacts and cooperation between the Competition Council and the other authorities have not been adequate in order to be instrumental in identifying as many as possible cartel agreements in the area of public procurement. With the purpose to strengthen the prevention of agreements in public procurement tenders the Competition Council intends to develop a special data base to accumulate and analyse the information about all the previous and current public procurement tenders in Lithuania.

34. Further the cooperation with all organisations in charge of organising and supervising the public procurement tenders; with reference to the experience accumulated by the Competition Council, it is necessary to organise and launch workshops and training sessions for officers of such authorities to enable them to notify as promptly as possible of any detected irregularities related to the companies' participation in public procurement tenders. It is also necessary to seek that sanctions for the infringements of competition law in combination with the sanctions imposed in relation to the public procurement procedures would result in a single infringement prevention system.