

PRICE FIXING & BID RIGGING - THEY HAPPEN: What They Are and What to Look For

AN ANTITRUST PRIMER FOR PROCUREMENT PROFESSIONALS

I. INTRODUCTION

American consumers have the right to expect the benefits of free and open competition, i.e., the best goods and services at the lowest prices. Public and private procurement professionals often rely on a competitive bidding process to achieve that end. The competitive process only works, however, when competitors set prices honestly and independently. When competitors collude, prices are inflated and the customer is cheated. Price fixing, bid rigging, and other forms of collusion are illegal and are subject to criminal prosecution by the Antitrust Division of the United States Department of Justice.

In recent years, the Antitrust Division has successfully prosecuted regional, national, and international conspiracies affecting construction, agricultural products, manufacturing, service industries, consumer products, and many other sectors of our economy. Many of these prosecutions resulted from information reported by alert and dedicated purchasing professionals. With such help, the protection of your right to free and open competition will continue to be a top priority of the Antitrust Division.

This Primer is designed primarily for purchasing professionals. It contains an overview of the federal antitrust laws and the penalties that may be imposed for their violation. It briefly describes the most common antitrust violations and outlines those conditions and events that indicate anticompetitive activity so that purchasing professionals might better detect and report suspicious activity.



The competitive process only works, however, when competitors set prices honestly and independently. When competitors collude, prices are inflated and the customer is cheated.

II. FEDERAL ANTITRUST ENFORCEMENT

Enacted in 1890, the Sherman Act is among our country's most important and enduring pieces of economic legislation. The Sherman Act prohibits any agreement among competitors to fix prices, rig bids, or engage in other anticompetitive activity. Criminal enforcement of the Sherman Act is the responsibility of the Antitrust Division of the United States Department of Justice.

Violation of the Sherman Act is a felony punishable by a fine of up to \$10 million for corporations, and a fine of up to \$350,000 or 3 years imprisonment (or both) for individuals. In addition, collusion among competitors may constitute violations of the mail or wire fraud statute, the false statements statute, or other federal felony statutes, all of which the Antitrust Division prosecutes.

In addition to receiving a criminal sentence, a corporation or individual convicted of a Sherman Act violation may be ordered to make restitution to the victims for all overcharges. Victims of bid-rigging and price-fixing conspiracies also may seek civil recovery of up to three times the amount of damages suffered.

III. FORMS OF COLLUSION

Most criminal antitrust prosecutions involve price fixing, bid rigging, or market division or allocation schemes. Each of these forms of collusion may be prosecuted criminally if they occurred, at least in part, within the past five years. To prove such a crime, it is not necessary that the conspirators entered into a formal written or express agreement. Price fixing, bid rigging, and other collusive agreements can be established either by direct evidence, such as the testimony of a participant, or by circumstantial evidence, such as suspicious bid patterns, travel and expense reports, telephone records, and business diary entries.

Under the law, price-fixing and bid-rigging schemes are per se violations of the Sherman Act. This means that where such a collusive scheme has been established, it cannot be justified under the law, for example, by arguments or evidence that the agreed-upon prices were reasonable, that the agreement was necessary to prevent or eliminate price cutting or ruinous competition, or that the conspirators were merely trying to make sure that each got a fair share of the market.

A. Price Fixing

Price fixing is an agreement among competitors to raise, fix, or otherwise maintain the price at which their goods or services are sold. It is not necessary that the competitors agree to charge exactly the same price, or that every competitor in a given industry join the conspiracy. Price fixing can take many forms, and any agreement that restricts price competition violates the law. Other examples of price-fixing agreements include those to:

- (1) establish or adhere to price discounts;
- (2) hold prices firm;
- (3) eliminate or reduce discounts;
- (4) adopt a standard formula for computing prices;
- (5) maintain certain price differentials between different types, sizes, or quantities of products;
- (6) adhere to a minimum fee or price schedule;
- (7) fix credit terms; or
- (8) not advertise prices.

A corporation or individual convicted of a Sherman Act violation may be ordered to make restitution to the victims for all overcharges. Victims of bid-rigging and price-fixing conspiracies also may seek civil recovery of up to three times the amount of damages suffered.

In many cases, participants in a price-fixing conspiracy also establish some type of policing mechanism to make sure that everyone adheres to the agreement.

B. Bid Rigging

Bid rigging is the way that conspiring competitors effectively raise prices where purchasers — often federal, state, or local governments — acquire goods or services by soliciting competing bids.

Essentially, competitors agree in advance who will submit the winning bid on a contract being let through the competitive bidding process. As with price fixing, it is not necessary that all bidders participate in the conspiracy.

Bid rigging also takes many forms, but bid-rigging conspiracies usually fall into one or more of the following categories:

O Bid Suppression — In bid suppression schemes, one or more competitors who otherwise would be expected to bid, or who have previously bid, agree to refrain from bidding or withdraw a previously submitted bid so that the designated winning competitor's bid will be accepted.

O Complementary Bidding — Complementary bidding (also known as "cover" or "courtesy" bidding) occurs when some competitors agree to submit bids that either are too high to be accepted or contain special terms that will not be acceptable to the buyer. Such bids are not intended to secure the buyer's acceptance, but are merely designed to give the appearance of genuine competitive bidding. Complementary bidding schemes are the most frequently occurring forms of bid rigging and they defraud purchasers by creating the appearance of competition to conceal secretly inflated prices.

O Bid Rotation — In bid rotation schemes, all conspirators submit bids, but take turns being the low bidder. The terms of the rotation may vary; for example, competitors may take turns on contracts according to the size of the contract, allocating equal amounts to each conspirator or allocating volumes that correspond to the size of each conspirator company. A strict bid rotation pattern defies the law of chance and suggests collusion is taking place.

O Subcontracting — Subcontracting arrangements are often part of a bid-rigging scheme. Competitors who agree not to bid or to submit a losing bid frequently receive subcontracts or supply contracts in exchange from the successful low bidder. In some schemes, a low bidder will agree to withdraw its bid in favor of the next low bidder, in exchange for a lucrative subcontract that divides the illegally obtained higher price between them.

Almost all forms of bid-rigging schemes have one thing in common: an agreement among some or all of the bidders which predetermines the winning bidder and limits or eliminates competition among the conspiring vendors.

C. Market Division

Market division or allocation schemes are agreements in which competitors divide markets among themselves. In such schemes, competing firms allocate specific customers or types of customers, products, or territories among themselves. For example, one competitor will be allowed to sell to, or bid on contracts let by, certain customers or types of customers. In return, he or she will not sell to, or bid on contracts let by, customers allocated to the other competitors. In other schemes, competitors agree to sell only to customers in certain geographic areas and refuse to sell to, or quote intentionally high prices to, customers in geographic areas allocated to conspirator companies.

IV. DETECTING BID RIGGING, PRICE FIXING, AND OTHER TYPES OF COLLUSION

Bid rigging, price fixing, and other collusion can be very difficult to de-

tect. Collusive agreements are usually reached in secret, with only the participants having knowledge of the scheme. However, there typically are suspicious bidding or pricing patterns, or a vendor may say or do something that arouses suspicion.



A. Bid or Price Patterns

Certain patterns of bidding or pricing conduct seem at odds with a competitive market and suggest the possibility of collusion:

1. Bids

O The same company always wins a particular procurement. This may be more suspicious if one or more companies continually submit unsuccessful bids;

Almost all forms of bid-rigging schemes have one thing in common: an agreement among some or all of the bidders which predetermines the winning bidder and limits or eliminates competition among the conspiring vendors.

O The same suppliers submit bids and each company seems to take a turn being the successful bidder;

O Some bids are much higher than published price lists, previous bids by the same firms, or engineering cost estimates;

O Fewer than the normal number of competitors submit bids;

O A company appears to be bidding substantially higher on some bids than on other bids, with no apparent cost differences to account for the disparity;

O Bid prices drop whenever a new or infrequent bidder submits a bid;

O A successful bidder subcontracts work to competitors that submitted unsuccessful bids on the same project; or

O A company withdraws its successful bid and subsequently is subcontracted work by the new winning contractor.

2. Prices

O Identical prices may indicate a price-fixing conspiracy, especially when:

- prices stay identical for long periods of time;
- prices previously were different;
- price increases do not appear to be supported by increased costs;

O Discounts are eliminated, especially in a market where discounts historically were given; or

O Vendors are charging higher prices to local customers than to distant customers. This may indicate local prices are fixed.

B. Suspicious Statements or Behavior

While vendors who collude try to keep their arrangements secret, occasional slips or carelessness may be a tip-off to collusion. Additionally, certain patterns of conduct or statements by bidders or their employees suggest the possibility of collusion. You should be alert for the following situations, each of which has triggered a successful criminal antitrust prosecution:

O There are irregularities (e.g., identical calculations or spelling errors) or similar handwriting, typeface, or stationery in the proposals or bid forms submitted by different vendors (indicating that the designated low bidder may have prepared some or all of the losing vendor's bid);

O Bid or price documents contain white-outs or other physical alterations indicating last-minute price changes;

O A bidder requests a bid package for himself and a competitor or submits both his and another's bids;

O A company submits a bid when it is incapable of successfully performing the contract (likely a complementary bid);

O A company brings multiple bids to a bid opening and submits its bid only after determining (or trying to determine) who else is bidding; and

O A bidder or salesperson makes a suspicious statement such as:

- any reference to industry-wide or association price schedules;
- any statement indicating advance (non-public) knowledge of competitors' pricing;
- statements to the effect that a particular customer or contract "belongs" to a certain vendor;
- statements that a bid was a "courtesy," "complementary," "token," or "cover" bid;
- any statement indicating that vendors have discussed prices among themselves or have reached an understanding about prices.

C. A Caution About Indicators of Collusion

While these indicators may arouse suspicion of collusion, they are not proof of collusion. For example, bids

that come in well above the estimate may indicate collusion or simply an incorrect estimate. Also, a bidder can lawfully submit an intentionally high bid that it does not think will be successful for its own independent business reasons, such as being too busy to handle the work but wanting to stay on the bidders' list. Only when a competitor submits an intentionally high bid because of an agreement with a competitor does an antitrust violation exist. Thus, indicators of collusion merely call for further investigation to determine whether collusion exists or whether there is an innocent explanation for the events in question.

Collusion is more likely to occur if there are few sellers. The fewer the sellers, the easier it is for them to get together and agree on prices, bids, customers, or territories.

V. CONDITIONS FAVORABLE TO COLLUSION

While collusion can occur in almost any industry, it is more likely to occur in some industries than in others. An indicator of collusion may be more meaningful when industry conditions are already favorable to collusion.

O Collusion is more likely to occur if there are few sellers. The fewer the sellers, the easier it is for them to get together and agree on prices, bids, customers, or territories. Collusion may also occur when the number of firms is fairly large, but there is a small group of major sellers and the rest are "fringe" sellers who control only a small fraction of the market.

O The probability of collusion increases if other products cannot easily be substituted for the product in question or if there are restrictive specifications for the product being procured.

O The more standardized a product is, the easier it is for competing firms to reach agreement on a common price structure. It is much harder to agree on other forms of competition, such as design, features, quality, or service.

O Repetitive purchases may increase the chance of collusion, as the vendors may become familiar with other bidders and future contracts provide the opportunity for competitors to share the work.

O Collusion is more likely if the competitors know each other well, through social connections, trade associations, legitimate business contacts, or shifting employment from one company to another.

O Bidders who congregate in the same building or town to submit their bids, have an easy opportunity for last-minute communications.

VI. WHAT YOU CAN DO

If companies are conspiring to collude on prices, the purchasing agent is the last person in the world that they want to know about the scheme. For this reason, even the most conscientious buyer can be victimized. Nonetheless, here are some procedures that can be established to discourage anticompetitive activity.

O Expanding the list of bidders will make it more difficult for bidders to collude. Buyers should solicit bids from as many suppliers as economically possible. As the number of bidders increases, the probability of successful collusive bidding decreases. While there is no magic number of bidders above which collusion cannot

occur, past experience suggests that collusion is more likely to arise where there are five or fewer competitors.

O Ensure that all purchasing department employees are familiar with the indicators of bid rigging, price fixing, and other types of collusion.

O Maintain procurement records, e.g., bid lists, abstracts, and awards. When collusion is suspected, it is necessary for us to review the procurement history of a product to determine if a pattern of bid allocation or rotation is present.

Ask questions. If the prices or bids submitted don't make sense, press your vendors to explain and justify their prices. You may be provided with a reasonable explanation or your suspicions may be heightened by a bogus answer. Either way, you learn more about your markets and demonstrate your interest in competitive prices.

O Know and understand the dynamics of the markets in which you make major purchases. A knowledgeable buyer may correctly suspect collusion from market behavior that may not arouse suspicions in an uninformed buyer.

VII. REPORT YOUR SUSPICIONS

We encourage all buyers to report suspicions of collusion through appropriate channels in your organization. The Antitrust Division cannot promise that every reported suspicion will warrant investigation, but we will carefully consider all information pro-

vided to us. Your observations may add to information we already have about an industry or, together with other reports, indicate a more widespread problem. Your call will always be appreciated and treated in accordance with our confidentiality policy, and, when warranted, we will conduct an investigation.

VIII. COMMON QUESTIONS OR CONCERNS

In talking to thousands of purchasing professionals, we understand that there are some concerns about reporting a suspected antitrust violation. Some of these concerns may be eased, however, by understanding how the Antitrust Division values and treats citizen complaints.

Ask questions. If the prices or bids submitted don't make sense, press your vendors to explain and justify their prices. You may be provided with a reasonable explanation or your suspicions may be heightened by a bogus answer. Either way, you learn more about your markets and demonstrate your interest in competitive prices.

O *But I Just Have a Suspicion*

How could you have anything more? Even the most knowledgeable and conscientious purchasing official could not prove price fixing or bid

rigging. Reported suspicions, however, sometimes on their own or more often coupled with information the Antitrust Division may have from similar complainants, other sources, or previous investigations, may be sufficient to warrant an investigation. Of course, many reported suspicions are not sufficient on their own to start an investigation, but they still provide the Antitrust Division with valuable market intelligence.

O *I Don't Want to Get Anyone in Trouble*

Purchasing professionals may fear that a vendor will be debarred, publicly accused, or even indicted based solely on their suspicions. Be assured that reported information and suspicions are just the first step in an incremental and very thoughtful process before an investigation is begun. Only if sufficient evidence develops will a criminal investigation begin, and criminal charges are never brought unless that investigation uncovers compelling evidence of price fixing, bid rigging, or other collusion.

O *I Don't Want to be Identified*

Purchasing professionals value their relationships with vendors and do not want to be identified, especially because the suspicious conduct may prove to have an innocent explanation. The Antitrust Division fully appreciates this, and your complaint will be handled in accordance with our confidentiality policy.

The attorneys and support staff of the United States Department of Justice, Antitrust Division are here to serve you in enforcing the antitrust laws. You can call on our assistance and help ensure that all consumers enjoy the benefits of the American free enterprise system by reporting suspicious behavior that raises antitrust concerns. Such behavior should be reported by e-mail to:

New Case Unit
e-mail: newcase.atr@usdoj.gov