

**Report Concerning the Study Meetings on the Measures and Promotion of
Reform in Public Procurement
(Summary)**

May 9, 2008
Japan Fair Trade Commission

1. Preface

Bid rigging is closely related with the system of public procurement in many ways. As such, the Japan Fair Trade Commission (“JFTC”) has conducted surveys in each year between FY 2003 and 2006 through questionnaires issued to the local public bodies and other procuring organizations concerning reforms in the bid tendering systems and the status of measures taken to enhance compliance. The JFTC has compiled survey results and expressed its ideas concerning the optimum direction for competitive measures related to public procurement.

In FY 2006, a succession of governors and treasurers of local governments were indicted on charges of accepting bribes and bid rigging charges related to public works. In response, in December 2006, the National Governors’ Association adopted guidelines to promote measures to eradicate bid rigging, especially collusive bidding at the initiative of government officials. Measures are also underway to enhance compliance and to reform the bid tendering systems at various procuring organizations.

However, these measures are basically being studied independently by each procuring organization, apparently through repeated trial and error.

The JFTC has therefore decided to hold information exchange meetings concerning the circumstances surrounding enhanced compliance with and reforms of the bid tendering system by procuring organizations, to which officers in charge at national, prefectural and city governments and government-funded corporations were invited. The meetings studied the issues and problems that the procuring organizations faced in the course of implementing these measures, assisted by the advice of experts, to promote effective measures to achieve the objectives. The meetings were referred to as “Study Meetings on Reform Measures and the Procurement Promotion Measures in Public Procurement” (“the Study Meetings”), and the results of the meetings have been compiled into the report.

2. Outline of the Study Meetings

(1) People participating in the Study Meetings

The Study Meeting was held three times in all. The main members who participated in all three meetings and subordinate members who participated in one of the three

meetings were selected.

A. Main members

Procuring organizations:

Ministry of Land, Infrastructure, Transport and Tourism, Saitama Prefecture, Nagoya City, Central Nippon Expressway Company Limited

Experts:

Mr. Noriyuki Yanagawa: Associate Professor, Graduate School of Economics, University of Tokyo

Mr. Shigeki Kusunoki: Associate Professor, Faculty of Law, Sophia University

B. Subordinate members

First meeting: Osaka Prefecture, Niigata City

Second meeting: Yamagata Prefecture, Yokosuka City

Third meeting: Okayama Prefecture, Akashi City

(2) Study Meetings held

	First meeting	Second meeting	Third meeting
Date and time	November 26, 2007 2:00 to 4:00 p.m.	December 19, 2007 1:00 to 3:00 p.m.	January 30, 2008 1:30 to 3:30 p.m.
Topics for discussion	Compliance measures for procuring organizations and associated issues	Reforms of the bid tendering systems and measures to deal with associated problems	Same as the second meeting
Report on examples	-Ministry of Land, Infrastructure, Transport and Tourism -Osaka Prefecture -Niigata City -Central Nippon Express Company Limited	-Yamagata prefecture -Saitama Prefecture -Yokosuka City	-Okayama Prefecture -Nagoya City -Akashi City

3. Measures to enhance compliance at procuring organizations (First Study Meeting)

(1) Examples of measures to enhance compliance

- A. Establishment of a division in charge of compliance
- B. Development of compliance manuals
- C. Implementation of compliance training
- D. Establishment of contact points for whistleblowers
- E. Revision of the re-employment of retired officers

(2) Issues identified

- A. What measures should be taken to prevent illegal activity from being concealed?
- B. What measures should be provided for preventing compliance measures from losing the substance?

(3) Major opinions on the issues from participants

A. What measures should be taken to prevent illegal activity from being concealed?

It has been made widely known to personnel that concealing illegal activity aggravates the damage to the organization.

It has been made widely known to personnel to deal appropriately with all internal complaints that have been filed, anonymously or otherwise, by conveying the results of the survey to the whistleblowers and posting anonymous complaints on the organization's website.

To encourage a person involved in an illegal activity to become a whistleblower, the person is subject to reduced disciplinary action or the act of whistleblowing is considered a mitigating factor.

Where a person involved in an illegal activity becomes a whistleblower, there is as yet no indication of the degree of leniency that will be shown. One opinion is that it is questionable whether leniency will actually be offered to the whistleblower, and the issue needs further study.

It is important to obtain information about illegal activity as quickly as possible. For obtaining the information as quickly as possible, incentives such as the system of leniency need to be offered to whistleblowers.

Although it is important to have personnel provide information, the major point is whether a system can be built to prevent problems from occurring when feedback concerning the problem were provided.

B. What measures should be provided for preventing compliance measures from losing the substance?

It is necessary to implement monitoring and checking by third parties.

Senior management should indicate their seriousness about the compliance issue in the course of daily business.

Long-term measures need to be implemented until personnel no longer believe that there are things that take priority over compliance.

If we concentrate too much on compliance, there may be adverse effects in other aspects. Some organizations have made public the planned price of public works to prevent personnel from leaking the planned price, making it easier for vendors to bid at the lowest price. As a result, some vendors bid at a price as close as possible to the lowest price, without making appropriate estimates. The model for the bid tendering system and that for compliance need to be reconciled to some degree.

Any system needs to be backed up by effectiveness, and it needs to be made widely known that there is nothing to be gained through dishonest activity.

Some personnel seem to believe that compliance that relates to public procurement and compliance that relates to dishonest activity are different, and that there are essential benefits in bid rigging. Personnel need to be trained to make them fully aware that there are advantages that come about through competition that results in good-quality work at low prices.

(4) Policies based on the study results

Measures to enhance compliance need to be developed by linking those to prevent collusive bidding at the initiative of government officials and other illegal activities with those that enable procuring organizations to deal with the illegal activity as quickly as possible when it occurs. When providing measures to enhance compliance, it is important to develop systems for the purpose by establishing divisions in charge of compliance, by compiling manuals, by establishing a whistleblower system, and suchlike. However, it is also expected that, in addition to the development of systems, these systems would be utilized effectively and that each employee would increase their awareness of compliance.

The JFTC has conducted surveys on the actual circumstances concerning the measures to enhance compliance provided at the procuring agencies organizations. The JFTC has also sent lecturers to give seminars organized by the procuring organizations covering the Antimonopoly Act and Act Concerning Elimination and Prevention of Involvement in Bid Rigging, etc. The JFTC intends to continue support measures to enhance compliance by procuring organizations.

4. Reforms of the bid tendering system and dealing with accompanying issues (The Second and Third Study Meetings)

(1) Examples of major reforms with the bid tendering system

- A. Expansion of general competitive bidding
- B. Introduction of a comprehensive evaluation method
- C. Expansion of electronic bidding
- D. Promotion of the disclosure of information
- E. Strengthening of penalties issued to violating business entities
- F. Development of local business entities and the assurance of fair competition
- G. Securing quality in construction work
- H. Making the clerical work for bidding appropriate and efficient

(2) Issues identified

- A. Introduction of a comprehensive evaluation method
- B. Development of local business entities and the assurance of fair competition

C. The issue of bidding by a single company and non-materialized bidding

(3) Major opinions of participants concerning the issues

A. The introduction of a comprehensive evaluation method

It is necessary to select between assuring quality by introducing a comprehensive evaluation method and making the qualification requirements for participating in bidding more rigid to ensure quality at the initial stage.

Measures that work well for one procuring organization do not necessarily work well for another. Since public works are directed at developing social capital, there are many aspects involved, such as policy measures concerning competition, labor and society. The way to approach these issues are to be decided in accordance with what each procuring organization prefers and emphasises.

If the price of a property is high and there are very many business entities wishing to receive the order, it is worthwhile implementing a comprehensive evaluation method.

Concerning the expansion of the comprehensive evaluation method, the increase in the amount of work that needs to be performed by the procuring organization in relation to the examination has been an issue.

It is difficult to evaluate things like construction plans where there is no guarantee that they will become reality.

When a business entity who offers a price above the minimum bidding price is successful in the bid, it is difficult to explain that the work offered by the successful bidder is worth the difference in price.

In the case of an exceptionally simple comprehensive evaluation method in which only past achievements are evaluated, it is possible to predict the score given to one's own company. As such, there is concern that business entities with low scores will submit bids at even more stringent prices.

As a result of introducing the comprehensive evaluation method, the outcomes of construction work improved and the successful bidding ratio dropped. Participants seem to have competed aggressively over engineering capabilities and prices in an effort to win orders.

In reality, business entities that offer the best prices and that have the best engineering capabilities are often the successful bidder. As such, the number of cases of "reversals," in which entities that offer prices above the lowest price become the successful bidder, is not so large.

B. Development of local business entities and the assurance of fair competition

Regional requirements are set for general competitive bidding, for projects that involve industries and classes with relatively large number of business entities that are headquartered in the city. In spite of the fact, the number of non-materialized bidding has increased since the start of general competitive bidding and electronic

bidding.

As a result of conducting general competitive bidding where regional requirements are imposed, the number of bidders declined compared to designated competitive tenders but the ratio of successful bidding has declined. This is because business entities no longer participate in bidding just because they are designated. Instead enthusiastic business entities who are very keen to win the order now participate, and as such, competition is believed to have intensified.

C. The issue of bidding by a single company and the failure of the bidding process to attract bidders

(Background to bidding by a single company and the failure of the bidding process to attract bidders)

In the case of designated competitive bidding, companies might be participating because of a sense of duty that they have been designated. This does not apply to general competitive bidding.

Business entities are now selective about whether the planned price determined by the procuring organization by summing the unit prices of ordinary quotations would create benefits for them.

The ratio of successful bidding and the number of participating bidders differ according to the industry and the work details.

When setting the planned price, reference has also been made to the quotations prepared by business entities.

In the case of large-scale projects, no regional requirements are set to begin with. As such, there is no way of making the requirements more lenient and it has been difficult to deal with the situation.

(Collection of information on bidding)

Since the same electronic bidding system has been used by the prefecture and by municipalities, it is possible to view the information on bidding for both the prefecture and municipalities. It is difficult to search for information unless it has been integrated.

In the case of small municipalities, most projects assume that local business entities will participate. As such, information on bidding is always conveyed even for small-scale projects. The situation differs with that of prefectures and designated large cities in this regard.

The business entities must all search themselves for business opportunities. Competition also involves this aspect. Maybe procuring organizations can provide information on bidding, and not just to some of the business entities. If information is to be disclosed, it must be disclosed to all parties concerned.

(Opinions on the issue of bidding by a single company and the failure of the bidding

process to attract bidders)

Even if only one company made a bid in competitive bidding, it is an outcome in hindsight. There is potential competition. If this arrangement is maintained, there is no problem in theory even if only one company made a bid. However, there are three possible problems, namely, that there is a monopoly in the market, that bid rigging might be operating and that the planned price needs to be reviewed.

Some business entities are able to move with the times, and others are not. A judgment needs to be made regarding how many advantages systematic reform brings to procuring organizations, whether business entities that are not able to move with the times should be helped, and whether we should assume that the true sense of competition means the survival in the movement with the times.

(4) Policies based on the study results

A. Introduction of a comprehensive evaluation method

An important issue in the area of the public procurement is to establish systems that enable procuring organizations to appropriately evaluate quality elements other than the price.

For this reason, the national government has promoted the introduction and expansion of a comprehensive evaluation method not only for procurement by the national government itself but also by promoting various measures for local public bodies. These measures include revising the comprehensive appraisal manual for local public bodies and the nationwide standardization of the system to support the procuring organizations by engineers.

The JFTC believes it is important to ensure fairness and transparency concerning examination and appraisal in a comprehensive evaluation method. When the system is introduced, it is desirable that procuring organizations are prepared to appropriately evaluate quality elements other than price. Procuring organizations should also implement the method objectively so that participating bidders do not have any suspicions that the evaluation is arbitrary or suchlike.

B. Development of local business entities and the assurance of fair competition

When a procuring organization sets regional requirements, if the bidding procedures were managed in a manner not only to ensure that local business entities have the opportunity to receive an order but also to ensure that local business entities do receive an order as a result, the competitive nature of local business entities may decline, and the local business entities may not develop in the optimum way. As such, the JFTC has indicated an opinion that regional requirements need to be managed to ensure that the bidders that participate are not predetermined and that a certain number of bidders participate. For example, regional requirements should be imposed only when the

number of business entities expected to participate in the bid exceed a certain threshold.

The examples offered by the procuring organizations at the Study Meetings all reflected schemes for ensuring competition when regional requirements are set. It is expected that these efforts will continue.

C. The issue of bidding by a single company and the failure of the bidding process to attract bidders

As pointed out during the exchanges of opinion at the Study Meetings, the factors behind the issue of bidding by a single company and the failure of the bidding process to attract bidders are believed to result from a discrepancy between the planned price and quotation by participating entities and the failure to fully disseminate information on the bidding process among business entities.

The expansion of general competitive bidding has enabled business entities to select the project for which they will bid. As such, differences are now found between projects that provide advantages for business entities and those that do not. It is possible to see potential competition even when there was only one participating entity or when bids failed to materialize. However, procuring organizations are expected to provide measures that provide competition and make bidding more competitive by analyzing the circumstances surrounding the project in more detail before issuing an order and determining the planned price, the construction period and other conditions for bidding appropriately for each of the projects.

Concerning the entry by only one company and the failure of the bidding process to attract bidders due to information on bidding being inadequately disseminated, business entities should change their attitudes about obtaining information on bidding themselves. However, procuring organizations are also expected to implement measures that include developing a system that make it easier for business entities to obtain information on bidding.