



Briefing 10/26 June 2010

OFT enforcement in construction sector - highlights improvements in awareness and behaviour

To: All housing email contacts

Key issues

Independent evaluation of OFT enforcement activities in the construction sector.
Increased knowledge of OFT decision on bid rigging compared with previous decisions.
9 in 10 firms recognise that bid rigging is serious breach of competition law.
Increase in awareness of fines for cover pricing.
Approximately 2 in 3 procurers introduced new mechanisms in last 2 years to detect or prevent anti-competitive practices.

1. Introduction

The OFT has recently published an independent evaluation of its recent competition enforcement activities in the construction sector which finds significant improvements in awareness and understanding of competition law and changes in business behaviour. It is titled 'Evaluation of the impact of the OFT's investigation into bid rigging in the construction industry' by Europe Economics partnering with GfK NOP.

The research is based on surveys of construction contractors and procurers and was conducted by Europe Economics. The report contains results from a first phase survey conducted in 2008 compared with a second phase survey conducted in 2010.

2. Main highlights

The evaluation highlights a number of positive developments, including:

- Nearly three-quarters of contractors are aware of the OFT's decision of September 2009 on bid rigging in the construction industry in England. In 2008, fewer than a third were aware of earlier infringement decisions in the construction sector.

- Nine in 10 construction firms now recognise that bid rigging, including cover pricing, is a serious breach of competition law with associated penalties.
- Three-quarters of contractors are aware of fines as a penalty for cover-pricing, compared to less than half in 2008.
- Approximately two in three procurers have introduced a new mechanism in the last two years to detect or prevent anti-competitive practices.

In addition, the research provides insights into a number of issues, such as the important role of media reports as sources of information about the OFT's work. Trade associations are also perceived as more important sources of information on competition issues than in 2008.

3. OFT approach to investigation

The OFT's approach to competition enforcement involves a relatively small number of high impact cases in order to create a strong deterrent effect across sectors. The report shows a significant rise in understanding of anti-competitive practices, and marked improvement in business behaviour, amongst construction firms.

4. Research Methodology

The research was based principally on responses to online surveys of construction companies and procurers of construction goods and services. The overall research approach and methodology remained consistent between the surveys. Any firms currently appealing the OFT decision were excluded from the 2010 contractor survey. Aside from these appellant firms, the survey did not exclude other firms with prior involvement with the OFT (whether during the OFT's recent or earlier investigations).

The surveys were designed to explore perceptions of the prevalence of bid rigging, knowledge of and compliance with UK competition law and awareness of OFT activities in the sector. When considering the survey findings, it is worth bearing in mind that the context of the survey (that is, an OFT-sponsored survey on the subject of competition law compliance) may, to some extent, influence responses, for example by influencing willingness to respond and/or the responses given. The survey sought to minimise these effects by careful questionnaire design, by emphasising the independence of the research, the confidentiality of the responses given and the fact that the responses would not be attributable to any individual or firm.

315 contractors and 132 procurers responded to the surveys. In addition the authors carried out in-depth interviews with 19 contractors and 4 contractor representatives and 11 procurers in order to explore the nature of bid rigging and industry awareness in more detail.

5. Main Findings

Perceptions of the prevalence of bid rigging practices in the UK construction sector

In general, a majority of contractors in both phases of the research perceived bid rigging practices to be either non-existent or only seldom occurring in the UK. This finding is in contrast with statements by construction companies and industry bodies that have

referred to the endemic nature of cover pricing in the sector and the findings of the recent OFT investigation and decision. This difference may, in part, be driven by the survey context as outlined above.

There appears to be little change between the 2010 and 2008 surveys in the perceptions of contractors surveyed concerning the prevalence of bid rigging. Where bid rigging does occur, cover pricing is perceived to be the most prevalent form (being cited by 13 per cent of contractors and 17 per cent of procurers as a common practice), a finding that is consistent with the baseline survey.

Nevertheless, the comparison of both surveys points to a sustained decrease in the perceived prevalence of cover pricing among contractors. In the 2010 survey, 44 per cent of contractors report cover pricing to be less common than in 2008. This compares with 28 per cent of contractors in the baseline survey who believed it had become less common since 2005.

With respect to the reasons underlying cover pricing and bid rigging, client retention still appears to be the main reason given by contractors for cover pricing and bid rigging more generally in the sector. 'Business management' is cited as a main reason by a substantially higher proportion of contractors than in the baseline survey.

Approximately one third of contractors surveyed believe that they have been disadvantaged in some way when their competitors had engaged in bid rigging activities.

Knowledge of and compliance with UK competition law

The increase in awareness of the legality and illegality of various practices between surveys has been marginal. Whilst knowledge levels appear good overall, some 14 per cent of contractors still appear not to be aware that cover pricing is illegal.

However, the survey found that the awareness of penalties applicable if found guilty of cover pricing has improved markedly. The awareness of fines as a penalty has improved the most, rising from 49 per cent in 2008 to 76 per cent in 2010.

Compliance-focused activities and measures aimed at detecting and preventing bid rigging activities are relatively common in the sector. About one third of contractors surveyed have some form of internal mechanism in place to ensure that competition law is complied with across supply-chains. 65 per cent of procurers have introduced a new mechanism over the last two years to detect and/or prevent anticompetitive practices.

Only 7 per cent of contractors with no prior involvement with the OFT have participated in competition law training programmes compared with 51 per cent of contractors with some prior involvement with the OFT. In the case of procurers, competition law training appears to be a higher priority for public sector procurers than for private sector procurers as they are more likely to have undertaken competition training over the last two years.

Only 18 per cent of contractors claim to be aware of any recently created competition codes of conduct in the sector, despite 30 per cent of the contractors surveyed reportedly being a member of one of the trade bodies that have recently introduced a code of conduct of this type in the sector. This may be due to the fact that these codes have only recently been developed.

Procurement method and bid rigging

Competitive tendering remains the most commonly used method of procurement. Attracting high quality bids and facilitating a low price are still considered as the most important factors underpinning this choice of procurement method.

When asked whether they would still invite firms which had failed to provide bids to respond to invitations to tender for other construction projects, 52 per cent of procurers state that they would still do so, while 13 per cent say that they would not. However 35 per cent report that they are unable to provide a clear answer to this question.

Awareness and impact of the OFT's recent investigation and decision on bid rigging in the UK construction sector

The report indicates that there is a high degree of awareness among contractors and procurers with regards to OFT actions in the construction sector.

Around three quarters of respondents are aware of the OFT's decision in September 2009 to fine 103 construction firms. This contrasts with the position in 2008 when only 29 per cent of contractors and 26 per cent of procurers indicated awareness of any of the six earlier OFT cases in the construction sector.

Media reports are by far the most important source of information on the OFT's recent actions in the sector. These are cited as an information source by over 80 per cent of contractors and procurers. Trade and industry bodies are also important channels of communication, particularly for contractors, and have increased in importance since the baseline survey. OFT publications were cited as an information source by 27 per cent of contractors.

The survey also suggested that the recent OFT decision in the sector has had a greater impact on improving the knowledge of procurers about the illegality of a range of bid rigging practices than the earlier OFT infringement decisions in the sector between 2004 and 2006. In 2010 28 per cent of procurers have revised their understanding of the illegality of these practices compared with 16 per cent in 2008.

The findings suggest that the recent OFT decision in relation to bid rigging activities in the construction sector has had a much larger impact on business behaviour and, more importantly, business practices of contractors compared with the OFT's six earlier decisions in the sector.

For contractors aware of the recent OFT decision, the fines imposed by the OFT on 103 construction firms for bid rigging activities appear to have had most impact on business behaviour in the last two years, with 19 per cent citing the imposition of fines as having had the largest impact on their firm's behaviour. The 2010 survey shows that the OFT's earlier roofing cases had a lower impact on firms' recent behaviour, having had an impact on only 2 per cent of this group of contractors.

Further, the research also found that the impact of the OFT's actions in the sector on business behaviour was far greater among those contractors that had had some prior involvement with the OFT; the OFT's actions had impacted on the business behaviour of 64 per cent of contractors surveyed with some prior involvement with the OFT compared with only 19 per cent of those with no previous involvement with the OFT.

Factors that create deterrence

Findings on the perceived effectiveness of various penalties in deterring bid rigging are broadly consistent with the baseline survey findings. Strong penalties, including company fines, exclusion from bidding for further work, and criminal prosecution are still perceived as the most important deterrents, while the proportion of procurers in the 2010 survey believe that increasing incentives to report bid rigging are an important deterrent has fallen by 11 percentage points.

6. Report conclusions

The findings in this report are based on industry views collected in 2010 after the OFT issued its Statement of Objections in April 2008 against 112 construction firms and after its decision in September 2009 to fine 103 construction firms for bid rigging activities. These views have been compared with those gathered in a baseline survey, conducted in 2008 (prior to the April SO), examining the impact of six earlier OFT decisions on bid rigging in the construction sector between 2004 and 2006. Summaries of the main findings have been set out in earlier sections and these are drawn together here to provide an overview.

7. APSE Comment

APSE welcomes the approach taken by OFT to engage an independent organisation to look into this issue. It is beneficial for all in the industry, both providers and clients, that the level of awareness of the OFT investigation and outcomes has risen.

It is concerning that the report found that “a majority of contractors in both phases of the research perceived bid rigging practices to be either non-existent or only seldom occurring in the UK”. OFT evidence gathered throughout the investigation exists which contrasts with this view. Such attitudes will hamper efforts to change the culture within the industry and OFT and other organisations must continue to highlight the existence of illegal activities in an attempt to address this kind of attitude.

The awareness of fines as a penalty has improved the most, rising from 49 per cent in 2008 to 76 per cent in 2010. Clearly the threat of fines (if set at a relevant level) should appear on the radar of commercial firms and lead to appropriate changes in behaviour. Fines are ofcourse a stage which should not be reached – firms should follow existing regulations but fines will hit the bottom line and the adverse publicity will also dent reputation, so the rise in awareness is understandable.

The report notes that about one third of contractors surveyed have some form of internal mechanism in place to ensure that competition law is complied with across supply-chains and that 65 per cent of procurers have introduced a new mechanism over the last two years to detect and/or prevent anticompetitive practices. Although these figures are improving both should ideally be at 100%. Contractors and procurers should have procedures in place which ensure illegal or inappropriate activities do not take place and if they do are identified as early in the procurement process as possible.

APSE welcome the point raised in the report that competition law training appears to be a higher priority for public sector procurers than for private sector procurers, as they are

more likely to have undertaken competition training over the last two years. There is a duty placed upon councils to ensure Best Value in all its activities and this includes procuring construction work. The fact that the report noted that in 2010 28 per cent of procurers had revised their understanding of the illegality of these practices compared with 16 per cent in 2008, reflects the need for procurers to remain up to date with developments. APSE has stated before that it feels that tendering practices and procedures needed to tighten significantly in the light of the OFT's findings. It appears that moves in this direction are happening.

A common reason put forward for cover pricing (and stated within this report) was that procurers would stop inviting firms which had failed to bid for work, to bid for subsequent tenders. However when asked whether they would still invite such firms to provide bids for further work, 52 per cent of procurers state that they would still do so, 35 per cent could not provide a clear answer whilst only 13 per cent say that they would not. This does not appear to back up the reason given.

There has been a dramatic increase from 26 per cent (procurers) and 29 per cent (contractors) in 2008 knowing about any of the six earlier OFT cases in the construction sector to around three quarters of respondents who are aware of the OFT's decision in September 2009 in 2010. Media reports, trade and industry bodies, OFT publications and local government organisations such as APSE all have a role to play in ensuring these kind of issues retain a high profile.

Future reductions in budgets will inevitably put more pressure on councils to identify savings and best use of resources and they must ensure they are not victims of illegal activities in any sphere. They will be expected to ensure their skills and knowledge of procurement issues are appropriate and that they have adequate procedures in place to avoid getting into a position which cannot be justified as best value.

Previous relevant briefings by APSE

10/23 'Cover pricing in the Construction Sector – Current Position and Implications' (with Stewarts Law LLP)

09/35 'Confessing to cartels in Scotland'

08/23 'OFT publish statement of objections detailing alleged collusion by construction companies'

07/47 'Making competition work for you – a guide for procurers of construction'

07/42 'Firms identified in OFT investigation'

07/22 'OFT details investigations into construction cartel'

06/41 'OFT report on waste competition'

06/18 'OFT cartel busters unit investigation into Mowlem'

03/59 'Action against cartels (prepared by Eversheds)

Two OFT press releases also provide information on the investigation – 'OFT closes door on cartel leniency in construction bid rigging cases in England' (50/07) and 'OFT makes 'fast track' offer in biggest ever UK cartel investigation' (49/07).

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