



COMPETITION & PROCUREMENT BULLETIN



UPDATE - THE OFT INVESTIGATION INTO COVER PRICING IN THE CONSTRUCTION SECTOR

In April 2008 the Office of Fair Trading issued statements of objection against 112 construction companies alleging participation in a bid-rigging cartel. The OFT's action follows a three year industry investigation and may have wide-ranging consequences for the industry. For the 112 alleged participants the main concern will be to defend against these allegations in their responses to the OFT. More generally any industry practices which may have led, or contributed, to the OFT's allegations will need to be analysed with a tooth comb by all industry participants to ensure that there are no more skeletons waiting to be unearthed and that all future behaviour is unambiguously compliant with competition law. The practice of cover pricing in particular is likely to come under close scrutiny.

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Bid rigging and cover pricing as infringements of UK Competition Law

Bid rigging, if proven, is clearly caught by the Chapter I prohibition on restrictive agreements contained in the UK Competition Act 1998. In this case the OFT is alleging a variety of bid rigging scenarios including what they term "cover pricing". Cover

pricing occurs where contractors wish to enter a bid but submit a price they intend to be too high. To ensure that they achieve a higher price they may ask competitors what price they intend to submit. It seems very likely that attempts will be made to draw a distinction between cover pricing and bid rigging. Bid rigging is necessarily engaged in by competitors and is seen as having serious anti-competitive effects. Consequently competition authorities will generally view it as a serious offence akin to price fixing or market sharing - essentially it involves competitors sharing opportunities. By contrast cover pricing often occurs where businesses wish to participate in a bid to show interest but may not have time to prepare the bid properly - consequently they aim to enter a price they know will be too high.

An argument may therefore be run that the purpose of cover pricing is not actually to distort competition and thus throw doubt on the presumption that cover pricing is necessarily anti competitive. Such an approach may force the OFT to look closely at the effects of cover pricing to prove that there is an infringement. On the other hand cover pricing involves the exchange of

information in relation to prices and that of itself will cause the OFT to be sceptical of attempts to distinguish it from bid rigging. It is also noteworthy that according to recent press comment the OFT has stated that it does not have any firm figures to assess the impact of the alleged cartel conduct. This may suggest that it will seek to rely on the presumption that cover pricing is a serious infringement and therefore take the position that it does not need to look at the effects of the alleged conduct. In any event the actual effect of the conduct may be taken into account when setting the level of any fines. Arguments may be made that the effects of cover pricing are in fact minimal.

Fines of up to 10 per cent of turnover

The Competition Act 1998 provides that fines of up to 10 per cent of the annual worldwide turnover of each participant may be imposed for a breach of the Chapter I prohibition. Technically this 10 per cent ceiling is calculated not just on the basis of the turnover of the individual business or company that is involved in the cartel but the turnover of the entire corporate group to which that business or company belongs. Whilst it is true that the OFT is generally tending to increase fines for cartel behaviour a large number of the alleged participants have provided information in return for leniency and admitted participation. It appears therefore that the conduct of

leniency and settlement procedures is likely to have a large impact on the level of any fines imposed in this matter.

The possibility of damages actions

Infringements of competition law may also lead to damages actions by those affected by

committed by individuals involved in cartel infringements. If convicted the individual may be imprisoned for up to five years and subject to a potentially unlimited fine. The offence only covers a limited number of the most serious forms of cartel activity although one of those covered is bid rigging.

This offence can only be committed if

subject to the European Union public procurement rules when selecting firms. Under these rules public bodies have the ability to exclude tenders on good grounds and it is conceivable that some may try to apply these provisions to cartel participants. In any event, whether or not such an approach were successful, it is likely that public bodies may well request evidence of compliance with competition laws in the future.

Martineau's Competition Procurement & Regulation Team

Martineau provides a full range of competition law advice including cartel advice both to alleged participants and to those damaged by such activities. We have extensive experience of dealing with the competition authorities during the investigative procedures leading to a decision, ensuring that clients' rights of defence are respected, advising on the possible mitigation of fines and leniency applications. We also provide advice on the associated legal issues raised by cartels such as compliance audits, compliance training and assisting individuals implicated in cartel behaviour.

This bulletin contains summaries of complicated issues and should not be relied upon in relation to specific matters. You are advised to take legal advice on particular problems and we will be happy to assist.

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anti-competitive behaviour. In this case those who commissioned buildings and works from the alleged participants may be in a position to bring claims. Historically such damages actions have been rare. However, given the high value of construction projects, the increasing awareness that damages may be available and the rapid progress that competition authorities are making in encouraging private enforcement of competition law, it seems the actions will be seriously considered in this case. As noted above it seems that the OFT is not able to determine a figure to estimate the damage caused by the alleged activities which may point to similar difficulties in assessing the quantum of any damages claimed in the future.

Possible criminal sanctions

The UK Enterprise Act 2002 provides for a criminal cartel offence which can be

dishonesty is proved. Individuals who are or may be in this position would need to review their directors' and officers' liability insurance policy carefully to check what financial cover is in place. In addition directors shown to have participated in a cartel may be disqualified which would prevent them acting as a director of any company.

PR issues

Increasingly, cartel infringements have serious public relations implications. Participants found to have been in a cartel will need to work hard to resuscitate their market reputations both during and after an investigation by the competition authorities.

Further, if large fines are imposed there could be a significant impact on share prices. One notable characteristic of the construction industry is that there are a large number of public sector buyers which will be