

BID RIGGING – A Long Time and Persistent Threat to Municipalities

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On December 28, 1894, the Addyston Pipe & Steel Company, of Cincinnati, Ohio; Dennis Long & Company, of Louisville, Kentucky; the Howard-Harrison Iron Company, of Bessemer, Alabama; the Anniston Pipe & Foundry Company, of Anniston, Alabama; The South Pittsburg Pipe Works, of South Pittsburg, Tennessee; and The Chattanooga Foundry & Pipe Works, of Chattanooga, Tennessee met to allocate pipe production among themselves covering all pipe sales in 36 of the 44 United States at the time. The agreement awarded specific tonnage of pipe to be produced by each of the companies. The companies' production and sales were audited to insure that no one cheated on the agreement.

The agreement further provided that:

'Third. The Addyston Pipe & Steel Company shall handle the business of the gas and water companies of Cincinnati, Ohio, Covington and Newport, Ky., and pay the bonus hereafter mentioned, and the balance of the parties to this agreement shall bid on such work such reasonable prices as they shall dictate.

'Fourth. Dennis Long & Company, of Louisville, Ky., shall handle Louisville, Ky., Jeffersonville, Ind., and New Albany, Ind., furnishing all the pipe for gas and water works in above-named cities.

'Fifth. The Anniston Pipe & Foundry Company shall handle Anniston, Ala., and Atlanta, Ga., furnishing all pipe for gas and water companies in above-named cities.

'Sixth. The Chattanooga Foundry & Pipe Works shall handle Chattanooga, Tenn., and New Orleans, La., furnishing all gas and water pipe in above-named cities.

'Seventh. The Howard-Harrison Iron Company shall handle Bessemer and Birmingham, Ala., and St. Louis, Mo., furnishing all pipe for gas and water companies in the above-named cities; extra bonus to be put on East St. Louis and Madison, Ill., so as to protect the prices named for St. Louis, Mo.

'Eighth. South Pittsburg Pipe Works shall handle Omaha, Neb., on all sizes required by that city during the year of 1895, conferring with the other companies and cooperating with them; thereafter they shall handle the gas and water companies of Omaha, Neb., on such sizes as they make.

The United States sued charging that this agreement to rig bids on municipal water and gas pipe around the country violated the Sherman Antitrust Act passed in 1890. This case went all the way to the United States Supreme Court because the companies argued they were doing

nothing other than trying to avoid engaging in ruinous competition. The Supreme Court found this conduct violated the Sherman Antitrust Act.

We have no doubt that where the direct and immediate effect of a contract or combination among particular dealers in a commodity is to destroy competition between them and others, so that the parties to the contract or combination may obtain increased prices for themselves, such contract or combination amounts to a restraint of trade in the commodity, even though contracts to buy such commodity at the enhanced price are continually being made.

With this decision, the Supreme Court made bid rigging unlawful. Despite the long history of illegality, bid rigging continues. Nearly 100 years after *Addyston Pipe*, the Pennsylvania Attorney General brought suit against road contractors who allocated Pennsylvania municipalities and counties much the same way the pipe manufacturers had done. The Lake Asphalt case, involved nearly an identical scheme including audits on cheating, only this time for asphalt paving jobs instead of pipe.

In 2012, the Federal Trade Commission sued a number of pipe fitting makers for bid rigging and monopolization of the US made pipe fitting market. These fittings are often required by laws such as the Pennsylvania Steel Products Procurement Act to be used on municipal and state publicly awarded contracts.

Even in early March 2014, the United States Department of Justice filed criminal charges against several persons for rigging bids on real estate foreclosure auctions including auctions being held by local governments to collect unpaid taxes.

Bid rigging is a persistent problem for municipalities. The purpose of competitive bidding, which is required under various provisions of the Pennsylvania Code, is to ensure townships get the best goods and services at the lowest prices. The competitive bidding process only works, however, when bidders independently submit bids on contracts. When bidders collude by working together to submit bids, prices are inflated and townships and their residents are cheated, wasting taxpayer dollars.

Bid rigging is unlawful under both the Federal Antitrust laws and Pennsylvania's Anti-Bid Rigging Act, 62 Pa.C.S.A. § 4501. That Act defines bid rigging as "the concerted activity of two or more persons to determine in advance the winning bidder of a contract let or to be let for competitive bidding by a government agency." Bid-rigging is punishable either by criminal fines and imprisonment or by a civil action brought by the Pennsylvania Attorney General for civil penalties and other relief including, suspension or debarment from participating in public contracts and liability for increased costs.²

At the Pennsylvania Office of Attorney General, complaints about bid rigging on government contracts take two forms. One is the traditional circumstance of the bidders meeting

² The Antitrust Division of the United States Department of Justice also brings bid rigging actions under federal antitrust laws.

before a bid opening to submit collusive bids, either by allocating territories or by some other method. The other is on rigging specifications, so that only one entity can win.

Traditional bid rigging has several forms. The United States Department of Justice has described the following types of bid rigging³:

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.

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.

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.

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.

Market Division: Market division or allocation schemes are agreements in which competitors divide markets among

³ Source: Price Fixing, Bid Rigging, and Market Allocation Schemes: What They Are and What to Look For, *An Antitrust Primer*. Available at <http://www.justice.gov/atr/public/guidelines/211578.htm>.

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.

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.

Bid rigging is discovered one of two ways: an insider⁴ discloses the existence of the conspiracy to law enforcement authorities, or the entity seeking bids sees something unusual about the bids its receives.

Detecting bid rigging can be very difficult as the agreements between the bidders are usually reached in secret and only the participants have knowledge of the conduct. There are, however, certain red flags townships can look for when competitively bidding contracts. The United States Department of Justice and the Pennsylvania Office of Attorney General have tips on determining whether bid rigging may be occurring.

1. The absence of an expected bidder;
2. The same bidder winning always winning;
3. A wide disparity in bids especially for commodities;
4. Similar errors in bids (i.e., two or more bids contain the same misspelling).
5. Bidders winning bids in a rotation;
6. Bidders appearing as subcontractors on each other's bids;
7. Bids greater than engineer's estimates.

Additionally, Townships can take certain steps to discourage anticompetitive activity including, expanding its list of bidders, since it is harder for bidders to collude when they are larger in number. Townships can also educate their purchasing department employees on indicators of bid rigging and maintain procurement records including, bid lists, abstracts and awards. Finally, Townships can learn as much as they can about the goods and services they intend to purchase and ask questions when the prices or bids submitted do not make sense. By being proactive in detecting and preventing bid rigging on competitively bid contracts, townships can ensure they are being good fiscal stewards of public monies and making the most of their limited resources.

⁴ In fact, the 2009 movie, *The Informant*, is about a bid rigging scheme being revealed by an insider.

The second type of complaint the office receives and the one the Office has received persistently most recently, is about specification rigging. In a specification rigging situation, the township seeks bids for an item such as a heating ventilation and air conditioning system (HVAC), but requires that the system be of specific brand. In many circumstances, manufacturers of brand name product are limiting the number of distributors and authorized installers of their products. Often this means that only one contractor is authorized to install the product in a given geographic area. This will mean that a township which uses brand specific specifications for an HVAC system, for example, may only receive a single conforming bid. In such a situation, the township will always pay more than if the specifications had been written in a way to encourage as many bids as possible.

Brand specific bid specifications are often pitched as a way to save engineering costs because the township's engineer is not designing a system from scratch and is not evaluating different methodologies for handling some process like cooling a building or treating sewage. But it is important to note that the person making this argument is often the manufacturer or the manufacturer's authorized representative. Additionally, any short term savings on engineering costs may be eaten up by higher prices for a system selected from one conforming bid instead of from a number of competitive bids.

Pennsylvania law does not explicitly prohibit the use of a restrictive specification. Use of these specifications however, will dramatically increase taxpayer costs.

If Townships suspect or uncover information that bidders are working together to pre-determine the winning bidder on contracts, Townships can contact the Attorney General's Office at 717-787-4530 to discuss their concerns. This information will be kept confidential by the Attorney General's Office while it conducts its investigation.