

# Study on Government Procurement

Study for Evidence Based Competition Advocacy

## Procurement Cycle



*Devika Malhotra*

January 2012

# Table of Contents

Executive Summary.....	1
1. Context and Objectives of the Study:.....	1
2. Legislative Inventory Reviewed:.....	1
3. Competition Issues in Public Procurement:.....	2
A. Policy Induced Competition Distortions:.....	2
1. Limiting number of suppliers .....	2
2. Limits the ability of suppliers to compete.....	3
3. Barriers to entry in public procurement in India: .....	3
3.1 Limited/Single Tender Enquiry: .....	4
3.2 List of Registered Vendors:.....	4
3.3 Bureaucratic Hassles and Complex Procedures:.....	4
4. Competitive Neutrality:.....	5
B. Competition concerns arising out of Anti-competitive conduct of bidders: .....	5
1. Market Sharing and Cartel formation: .....	5
2. Bid rigging and Collusive bidding: .....	5
3. Abuse of Dominance:.....	5
4. Information asymmetry and its impact on Competition:.....	5
5. Monopsony:.....	6
6. Recommendations:.....	6
7. Advocacy Agenda:.....	9
8. Role of Competition Commission of India in Competition Advocacy:.....	11
Chapter 1: Introduction and Objectives of the Report.....	13
1.1 Introduction .....	13
1.2 Objectives.....	14
Chapter 2: Market Structure and Reported Competition Issues.....	16
2.1 Market Structure .....	16
2.2 Competition Issues.....	16
2.3 Initiatives taken by the government to promote competition in public procurement:.....	21
Chapter 3: Identification and listing of anti-competitive provisions and practices.....	23
3.1 Issues in identification of anticompetitive provisions and practices.....	23
3.2 Observations on the Public Procurement Bill, 2011: .....	35
3.3 Policy Induced Competition Distortions: Case Studies.....	35
3.3.1 The Monopoly Cotton Procurement Scheme (MCPS).....	35
3.3.2 NHAI Move to Restrict Bidders.....	37
Chapter 4: Analysis of the Identified Issues.....	40
4.1 Limiting number of suppliers .....	40
4.2 Limits the ability of suppliers to compete.....	41
4.3 Collusion or corruption having distortionary effect.....	42
4.4 Barriers to entry in public procurement in India: .....	43
4.4.1 Limited/Single Tender Enquiry:.....	43
4.4.2 List of Registered Vendors:.....	43
4.4.3 Bureaucratic Hassles and Complex Procedures:.....	44
4.5 The Commonwealth Games 2010: A Case Study.....	44
Chapter 5: Review of Regulatory framework for public procurement in India.....	46
5.1 Key Issues in Regulatory and Legal framework.....	47
5.1.1 Multiple Guidelines .....	47
5.1.2 Absence of Standard Procedures, Contracts and Tender documents.....	47
5.1.3 Weakness of present monitoring mechanism .....	47
5.1.4 Absence of a Transparent Grievance Reprisal Mechanism .....	48
5.1.5 The Competition Act and its applicability on the demand side .....	48
5.1.6 The Way Forward--Need for a Public Procurement Law.....	48

Chapter: 6 Conclusion, Recommendation and Agenda for Competition Policy advocacy.....	50
6.1 Conclusions: .....	50
6.2 Principles for designing Tender Documents:.....	51
6.3 Recommendations:.....	54
6.4 Advocacy measures: .....	57
REFERENCES.....	60

## **Executive Summary**

### **1. Context and Objectives of the Study:**

The Committee on National Competition Policy (C-NCP) has been constituted by the Ministry of Corporate Affairs, Government of India, with a view to framing of a National Competition Policy (NCP), developing a strategy for competition advocacy with the government and the private sector, fine tuning the Competition Act, 2002 and looking into any other matter in relation to competition issues. It has submitted a draft National Competition Policy and has sought to gain specific inputs and undertake evidence based advocacy to develop a competition advocacy strategy with the government and the private sector. To carry out evidence-based advocacy, sector specific studies have been conducted for which thirteen sectors/themes have been identified and the study on government procurement is one of them. These sector specific studies including the present one on public procurement have focused on reviewing competition distorting provisions in policies, laws, regulations, practices etc. governing the sector. The present study has attempted to provide illustrative examples of those laws, regulations and policies which either exert or have the potential to exert anti-competitive effects, and thus influence the outcomes of the law/regulation/policy concerned. The study focuses on Law/policy induced competition distortions. It has also recommended changes in the regulations and their implementation procedures to address the competition related issues. The study has also highlighted an approach to promote and protect competition in the sector.

### **2. Legislative Inventory Reviewed:**

The following laws, rules, regulations, guidelines, policies governing public procurement in India have been reviewed and critically analysed with a view to bringing out competition distorting provisions contained therein and suggesting necessary changes in the laws to address the competition issues and highlighting an approach to facilitate competition in the sector:

- General Financial Rules, (GFR) 2005.
- State GFRs.
- Delegation of Financial Powers Rules (DFPR), 1978.
- Guidelines issued by the Central Vigilance Commission (CVC).
- Guidelines issued by the Directorate General of Supplies and Disposal (DGS&D)
- Manuals on the procurement of goods, services and works issued by the Department of Expenditure, Ministry of Finance.

- Guidelines on procurement issued by individual ministries/departments, PSUs etc.
- Legislations on procurement enacted by individual states like Tamil Nadu and Karnataka.
- Defence Procurement Procedure, 2008.

The above mentioned list is indicative and there might be some rules or guidelines or legislations which are based on above mentioned analysed rules, thus making no serious lapse in the outcome of conclusions and suggestions of the present study.

### **3. Competition Issues in Public Procurement:**

#### **A. Policy Induced Competition Distortions:**

Competition distortions may take any form including, creation of barriers to new entrants in the market; driving existing competitors out of the market; foreclosure of competition by hindering entry into the market; denial of accrual of benefits to consumers; disallowing improvements in production or distribution of goods or provision of services; or denial or discouragement of promotion of technical, scientific and economic development by means of production or distribution of goods or provision of services. It is globally known now that there are competition distortions caused by government policies and laws.

The yardsticks of fairness, integrity and transparency through competition, efficiency and economy in public procurement practices established by the GFR 2005, have either failed to achieve their objective or have not been very effective. Although five fundamental principles, namely, open tendering, effective advertisement, non-discriminatory tender conditions and technical specifications, public tender opening (bid evaluations based on a pre-disclosed criteria and methodology), and award to the most advantageous bidder without any negotiation on price or any other terms, do seem to exist under the GFR 2005 but equal set of discretionary and vague GFRs mar the contemplated effectiveness of the GFR 2005. Some of the policy induced competition distortions emerging from analysis of the GFRs 2005, Indian Railways Code for Stores Department and DGS&D Purchase manual are discussed hereunder:

#### **1. Limiting number of suppliers**

The number of suppliers in the procurement process may be limited when procurement rules lay down a technical specification in terms of a proprietary product and do not lay down generic specifications. For example, a public authority is procuring fans, motors but it lays down the condition that wiring to be procured for fans and motors must be from ANCHOR wires. The said qualification is not purely technical rather carries proprietary element and significantly reduces number of suppliers, who could have supplied fans and motors of given capacity. Such outcome is obvious from application of Rule 152 of the GFR, 2005 and rules akin to it, although there might be good arguments in favour of this rule yet the impact is anti-competitive.

Similar outcomes are perceivable from rules providing for rate contracts concluded by DGS&D as per Chapter 13 of Purchase Manual, wherein procurement is logged into for the entire year. When numbers of suppliers of a particular product are limited by the public authority by its own rules, it limits its own choice and brings in anticompetitive impact by such limited choice in the whole process.

Similarly, Registration of Suppliers by DGS&D and RDSO vendor approval guidelines are of the nature of discouraging potential bidders from participation because unless vendors are prior approved they cannot participate in the bid. A practice seems to exist which disallows a competent bidder because it is not on the approved list of RDSO or in another case a supplier is not on the list of registered suppliers of DGS&D; this limits the number of potential suppliers of products to Railways and other Government departments. Such a practice restricts competition and enhances the possibilities of formation of a cartel. Similarly, rules of Indian Railways Stores Department and DGS&D relating to single tender and limited tender enquiry also have impact on competition. The said rules hinder competition by limiting number of suppliers of products.

These rules or principles followed in the process of government / public procurement although seemingly designed for getting best value for money often result in anticompetitive outcomes.

## **2. Limits the ability of suppliers to compete**

Given the system of procurement by public authorities, there are issues where procurement is sourced to another public enterprise, which directly limits the ability of suppliers to compete. It is generally seen that wherever available public procurement is sourced to another public enterprise. For e.g. Indian Railways procures rails from SAIL, equipments from other PSEs like BHEL. If value of goods procured and the relevant product market is seen, it may appear that entire relevant product market belongs to one enterprise, which is not acquired by its efficiency rather by its status as a PSE and favourable procurement orders being placed with them.

The available rules of procurement such as GF Rule 147 i.e. Purchase of goods directly under rate contract or Rule 144 stating about reserved items are some of the examples that limit competition in two ways. Firstly, it limits competition between suppliers inter se by not giving them opportunity to compete and secondly it limits the choice of procurer as well.

## **3. Barriers to entry in public procurement in India:**

Restricted entry caused by strict sector regulations is pertinent in every kind of competition case that does not involve a per se offence. There is a tendency among public procurers to restrict participation to chosen big and reputed firms. Often this is done to reduce the cost of evaluating bids or to ensure the stability and quality of supply. However this tendency could raise high entry barriers for new entrants leading to inefficient outcomes. Following are the key practices on the demand side in the procurement process that could restrict competition by raising barriers to entry:

### **3.1 Limited/Single Tender Enquiry:**

In India, procurements are carried out through three channels of tender invitation. Open Tender Enquiry (OTE), limited tender enquiry (LTE) and Single tender enquiry (STE). LTE is recommended in cases of procurement where pool of vendors have been established. STE is recommended under only exceptional circumstances such as national calamities or other emergencies. The choice between these can significantly impact the participation level in the tender.

Numerous Reports have noted that organizations (unknowingly or purposely) fail to utilize this open channel and tend to depend on LTE. A CVC Report on public procurement points out, *"in the process of neglecting OTE, the competition is restricted which in turn results in cartel formation, higher rates and favouritism to select firms"*. There are numerous cases where even in case of generic items, prescribed rules and guidelines are not followed and available channel of OTEs are ignored.

### **3.2 List of Registered Vendors:**

It is a common practice in Ministries /Departments where there are safety, expediency and security concerns to maintain a list of short listed suppliers on technical and financial grounds. Such registered suppliers are exclusively eligible for consideration for procurement through LTE. A detailed analysis of this mechanism reveals various flaws that have led to severe barriers to entry for new participants. Often it has been reported that the approving authority has imposed tedious procedure resulting in abnormal delays in securing approval.

Further, often these lists are not updated regularly even if there is a single supplier in the list over a long period of time. Lack of willingness on the part of the procuring authority to update these lists has resulted in restricting competition.

For example, the System of Vendor Approval followed by Indian Railways in restricting the procurement to vendors approved by Research Design & Standards Organisation (RDSO) is complex and time consuming, besides being restrictive. It discourages potential bidders from participation. As a result it restricts competition and enhances the possibilities of formation of a cartel. Combined effect of the limited approved vendors, time taken in approval and very little volume of supply permitted to a new vendor under approval to Part I status suggests that the system does not encourage competition, economy and effectiveness. This process acts as a barrier to entry and thus, limits the ability of suppliers to compete.

### **3.3 Bureaucratic Hassles and Complex Procedures:**

Excessively tedious process for participation sometimes poses severe barriers to participation. As noted above, it is common for procurement agencies like Railways and DGS&D to keep a list of selected vendors exclusively eligible for LTEs. New firms are dependent on the approving authority within the department concerned for being nominated on the approved vendors list. These firms are required to go through lengthy administrative and procedural requirements. It is often reported that corruption in the public department has made getting approval costly with respect to time and money.

The issues identified and discussed above do suggest that existing rules on public procurement in India have distortionary effect on competition and the relevant market. It must be noted at

this stage that competition distortions creep in through other loopholes such as element of kickbacks and high handedness in supplier selection and order creation (procurement decision). Thus overhauling of rules and creation of an efficient system of public procurement is most desirable.

#### **4. Competitive Neutrality:**

Competitive Neutrality describes the aim of a level playing field in mixed public/private markets, where state owned or quasi-public bodies line up to compete with private sector companies. These markets tend to be distorted as a result of structural advantages enjoyed by public providers and a failure by public buyers to ensure fair process. In today's competition context, the demand and existence of competitive neutrality across public procurement processes is no longer a buzzword and in its absence the distortionary effects on competition and market are well known.

Interviews with stakeholders suggest that Indian Railways (one of the largest procurers), procures high value traction equipment items for ALCO Diesel Locomotives on annual basis from Bharat Heavy Electrical Ltd. (BHEL – a Govt. of India PSU ) by operating their Price List without following the normal tendering process. This is against the spirit of competitive neutrality.

### **B. Competition concerns arising out of Anti-competitive conduct of bidders:**

#### **1. Market Sharing and Cartel formation:**

Market sharing and Cartel formation among the suppliers of various goods and services in India is quite rampant. In many cases, where the same price is quoted by suppliers, the public procurer distributes the quantum of procurement among all of them, either equally or through some discretionary variations. It may also be seen that producers of same/similar goods tend to share the market based on their understanding.

#### **2. Bid rigging and Collusive bidding:**

In public procurements, horizontal agreements i.e. agreement between competing firms are common. Bid Rigging is a form of fraud with the purpose to fix price and share market demand, often adopted where contracts are determined by auction. Bid rigging can be achieved under alternate terms of agreements between the firms and almost always results in economic harm to the public department that is seeking the bids.

#### **3. Abuse of Dominance:**

Dominant firms in the public procurement system may use their incumbent power to prevent any new entrants from entering into the market by indulging in predatory pricing. Predatory pricing is a strategy of selling a product or service at a low price (below cost) with the objectives to drive competitors out of the market or create barriers to new potential competitors. Like many competition laws of many countries, Indian Law also identifies predatory pricing as an anti-competitive activity.

#### **4. Information asymmetry and its impact on Competition:**

It may be seen that there is no projected information available in the public domain suggesting goods or services and their quantum to be procured by the public authorities.

Sudden decision to procure any good or service strains the existing capacity of supply, which creates a price pull factor often leading to inefficient procurement. It is an accepted fact that there are limitations associated with collection of information, its analysis and finally in its application. Life and time are finite; flow of information is unending and varied. Decisions have to be made within the stipulated time period giving due regard to biases of the parties. Therefore, information asymmetry continues to be an essential feature to identify in a market. This signifies that the continuation of market asymmetry keeps the challenge alive for advocacy programmes of competition polices and also that of competition authorities.

#### **5. Monopsony:**

Monopsony reflects market power on the buying side of the market. When monopsony power is exercised, it causes economic inefficiency and a transfer of wealth to the buyer. As a result, competition concerns such as buyer cartels, predatory overbuying, and overbuying strategies designed to raise rivals' costs, and mergers that create or enhance monopsony power arise.

#### **4. Recommendations:**

1. Firstly, basic reform of the public procurement system is required both in the Legal and Institutional framework governing public procurement in India as well as some of the practices being followed by the procuring departments. There is a need for a dedicated law on public procurement in India in view of the fact that government undertakes public procurement on a very large scale and is susceptible to competition concerns in the absence of a law on the subject. This would set out in clear terms the Government's approach to this important activity. The law should be supplemented by detailed rules and regulations. Such a law would give an enforceable form to key provisions of the policy including penal action against violations by the procurers or the suppliers.
2. To provide effective leadership in public procurement and bring about the reforms, setting up of an Institutional framework preferably of a dedicated department within the Ministry of Finance is recommended. This Department will not have an operational responsibility for direct procurement; it would act as a repository of the law, rules and policy on public procurement and monitor compliance thereof. It would institute best practices, professionalise the public procurement function, arrange for capacity building, create and maintain the overarching public procurement portal and maintain management information systems and statistics pertaining to public procurement.
3. Recognizing the need for standardization including in the procedures, tender documents and general conditions of contract, the specifications set out in the tender documents should be clear, generic as far as possible and provide no advantage to any one party. The procurement process should provide level playing field to all players. Although the need for standardization of tender documents is recommended, the documents thus

standardized should have an ample scope to consider suitable modifications to take care of the special needs of the ministry/department concerned.

With a view to streamlining the procedure and to detect deficiencies in the tender documents submitted by the bidders, it is recommended that a check list of all documents required in proper sequence should be drawn out for convenience of comparison and for ascertaining that all the documents have been received.

4. With a view to professionalizing the function of Public Procurement, it is important to institute an elaborate system for capacity building and training in all aspects of public procurement. The training would not be confined to mere knowledge of extant rules and procedures applied mechanically but also to basic principles and concepts of public procurement, writing of specifications, qualification and evaluation criteria and contract terms etc. The government should seek co-operation of professional training institutes in capacity building of procurement officials.
5. The fundamental principles of effective procurement require that any proposed procurement should be given sufficient publicity, commensurate with its size and nature to attract maximum participation and competition. The laws, rules and subordinate instructions mandate appropriate publicity of the proposed procurement in the public domain through various means such as the media, website and trade journals.
6. Competitive bidding would be the norm for procurement unless permitted and justified in special cases. Evaluation criteria should be clearly spelt out in the tender documents: evaluation should be carried out only on the basis of the declared criteria. Public opening should be mandatory. The result of the tendering process should be put out in the public domain.
7. Using IT can be one of the most effective policy tools in enhancing the level of competition in public procurement. Proper adoption of an e-procurement system can expand transparency in the procurement market and also contribute to the prevention of corruption. Towards this, Department of Expenditure, Ministry of Finance, Govt. of India has taken significant steps by issuing instructions to all Govt. Ministries/ Departments/Organizations to switch over to e-procurement regime. The Korean example which involves third parties to monitor on line contract management would help illustrate better.

The nationwide integrated Korea Online E-Procurement System (KONEPS) enables online processing of all procurement from purchase request to payment. Through the digitalised system, customer organisations and companies are involved in scrutinising the way public funds are managed in the procurement process. The System covers all stages of the procurement process, from the pre-bidding to contract management and payment. For example, the Public Procurement Service releases specifications of procurement items on the KONEPS prior to the bid notice in order to encourage interested suppliers to submit suggestions.

The Korean experience illustrates how new technologies can support the involvement of a third party - an insurance company - that provides a guarantee for the contract between the

administration and the bidder. The successful bidder and the contracting agency establish an e-contract through KONEPS, and in the process, a surety insurance company, as a third party, shares part of that information regarding the contract. In practice, the contracting official receives both the contract documents provided by the contractor and the written guarantee for the contract provided by the surety insurance company, and replies to the guarantee. The contracting officer drafts the final version of the contract after clarification and sends it to the contractor and the end-user organisations. Another feature of the information system is that it helps monitor the payment and prevent risks to integrity during payment. The contractor submits a payment request and receives payment upon receipt, which is sent by an inspector from an end-user organisation. Since the e-payment is connected to the Finance Settlement, the end-user organisation, the contractor and the bank share information in the flow of payment. Payment is automatically completed on line within two working hours upon payment request to avoid overdue payment.<sup>1</sup>

8. Provision of Certificates of Independent Bid Determination (CIBD), require bidders to certify that they have arrived at their tender price absolutely independent of other bidders. CIBDs operate as both a reminder of the relevant legislation and as a commitment by the bidder that these rules have been complied with, and are of particular value in situations where tender participants may be less aware of national legislation prohibiting corruption and collusion. Prosecution of CIBD violations can also be a possibility where absence of proof of an agreement makes it impossible to charge an antitrust violation.
9. A stronger antitrust and anti-competition agency with strong co-ordination with other law enforcement agencies will contribute to reducing the corruption in public procurements. Systematic exchange of information between the antitrust bodies and anti-corruption bureaus is highly desirable in this regard. Drive against corruption and steps towards enforcement to eliminate anti-competitive practices are complementary in nature since improvement in the procedure by which the tender documents are designed and the bidders are ultimately selected will not only reduce corruption but also enhance competition in the procurement market.
10. The risks for competition in public procurement can be reduced by careful consideration of the various auction features and their impact on the likelihood of collusion. Designing auction and procurement tenders with collusion in mind may significantly contribute to the fight against anticompetitive behavior, as it allows the creation of an environment where the bidders' ability and incentives to reach collusive arrangements are significantly reduced, if not eliminated.
11. Reducing collusion in public procurement requires strict enforcement of competition laws and the education of public procurement agencies at all levels of government to help them design efficient procurement processes and detect collusion.
12. Introduction of a Debriefing Procedure would be helpful. Unsuccessful bidders have a right to know why they were not successful, if that is not readily apparent. On request, say, within 7 days of award notification - the purchaser should provide a debriefing, essentially to help the bidder understand the evaluation process and prepare more

---

<sup>1</sup> South Korea, response to the OECD Questionnaire.

responsive bids in future. Once the procedure is in place for some time, bidder confidence in the system will go up.

13. The blacklisting rules for corrupt firms should be revamped and strictly enforced. The supplier firms should be required to adhere to a “code of conduct”. Any infringement should result in sanctions. The blacklisting rules need improvements permitting exclusion from public contracts for a period, or permanently, depending on the seriousness of the offence.
14. Research Design and Standards Organization (RDSO) is the sole R&D organization of Indian Railways and functions as the technical advisor to Railway Board, zonal railways and RPU. One of the key roles of RDSO is quality assurance. It involves vendor approval and purchase inspection of these various items. From the stakeholder discussion the study has gained that RDSO plays a prominent role in restricting entrants into the railways procurement. Concerns like bureaucratic hassles in RDSO have in many ways assisted anti-competitive practices. Complaints such as long approval time periods for any new technology have been reported by some of the stakeholders. Moreover, stakeholders have claimed that over-specification and tedious procedure to get approvals from RDSO has kept away many big vendors. It is important for the policy makers to reduce ‘unnecessary’ entry barriers as this can directly result in increased competition and reduction in the power of the cartels to control the market.
15. It appears that for ensuring competition, we are mainly concentrating on the downstream activities i.e. tender conditions, bid documents, eligibility criteria, bid evaluation, contract awarding etc. It would be worthwhile to point out here that equal attention is also required to be paid to upstream activities like determination of technology, conceptual design, specification, vendor base identification etc. Unless that is done, it would be extremely difficult to control lack of competition only by regulating/ reforming the downstream activities.
16. There is a need to make the procurement function truly cross functional and a part of an end-end supply chain.
17. Separate and comprehensive procurement rules for goods, services and works should be laid down.
18. There should be provisions for institutionalising ‘Integrity Pacts’ or any other enforceable integrity conditions as a legally binding ethical code of conduct to govern the procurement cycle. This needs to be buttressed by provisions penalising violations of the Pact’s terms and conditions.

## **5. Advocacy Agenda:**

A well laid down advocacy agenda is crucial to creating awareness about the risks to competition in procurement procedures and at the same time developing appreciation of the benefits of inculcating competition in public procurement processes.

Three main areas can be identified for competition advocacy activities with respect to public procurement. First, general public education efforts aimed at building support for the institutions of a healthy market economy, including sound public contracting rules and procedures. Second, efforts aimed at modifying or eliminating specific aspects of procurement policy and regulations that may suppress competition. Third, broader efforts to modify or reduce sectoral and/or cross-sectoral policies that are not specifically concerned with procurement but which affect the scope for competition in public procurement markets. This might include licensing or other restrictions to entry or participation in markets and cross-sectoral or framework laws and policies that unnecessarily make it more difficult for firms to compete.<sup>2</sup>

- **General public education efforts aimed at building support for the institutions of a healthy market economy, including transparent and competitive contracting procedures.**

An important aspect of competition advocacy concerns basic public education regarding the institutions of a healthy market economy. To have positive long-lived effects, procurement and other economic policy and legislative reforms ultimately must command public support. A broad range of useful target areas can be identified: education of public officials; of business; of the media; and of the wider community. Effective advocacy can promote a change of culture in State practices and generate public support for enforcement efforts. Business also has a role in this process, in terms of the education of its personnel and the development of internal compliance mechanisms. A particularly important audience for consciousness-raising concerning the importance and maintenance of competition concerns the contracting personnel who should be well informed about the risks of collusion, the harm it causes and measures of preventing it.

- **Advocacy efforts focused on Procurement policies and regulations that can limit competition.**

Public procurement policies can limit competition and even assist firms in behaving anti-competitively in at least two ways. A first way is to restrict entry into procurement markets, particularly by imposing domestic or local content rules that exclude potential bidders. A second area of possible concern includes procedures that aim to increase the integrity of the procurement system but may also have the unintended effects of limiting entry or facilitating supplier coordination. An important example concerns the process for opening bids in sealed bid procurements. Typically, bids are unsealed in public and displayed for all bidders to observe. While widely seen important as an anti-corruption measure, this process can also facilitate collusion by enabling cartel members to determine whether co-conspirators fulfilled promises either not to bid or to submit artificially high cover bids. A possible reform in this regard could be to permit the private inspection of bids by a guardian inside the purchasing

---

<sup>2</sup> Anderson Robert, Kovacic William and Muller Anna, 2010, 'Ensuring Integrity and Competition in Public procurement markets: a dual challenge for good governance.

agency, such as an inspector general. Such a measure could impede efforts by cartel members to detect cheating without undermining the integrity of the award process.

- **Efforts to address regulatory and other obstacles to competition that are not specifically linked to the procurement process, but which nonetheless impact on competition in public procurement markets.**

Regulatory obstacles to competition that are not specifically linked to the procurement process, but which can nonetheless impact on competition in public procurement markets are of two main kinds: (i) industry measures and (ii) cross-sectoral or “framework” laws and policies. Such measures include licensing and other requirements that impede entry into markets, for example by imposing excessive financial solvency requirements. The anti-competitive effects that such requirements can entail are well recognised.

#### **6. Role of Competition Commission of India in Competition Advocacy:**

The Competition Commission of India (CCI) has also been entrusted with the task of undertaking competition advocacy, creating awareness about competition issues, under Section 49 of the Competition Act, 2002 which provides for competition advocacy and inculcating competition culture in the country.

The harm caused by anticompetitive practices by enterprises is so severe, both for the consumer and the economy, that competition law vests the competition authority with enforcement powers to investigate and penalize such practices. Through deterrent use of enforcement powers, the authority hopes to maintain and promote healthy market competition. However, enforcement alone is not enough. Thus, the authority is usually given a more proactive mandate of competition advocacy.

The aim, in part, is to strengthen competition awareness amongst market players, thereby encouraging self-compliance and reducing the need for direct action against erring enterprises. Sensitizing of public agencies is equally important from the point of view of avoiding litigation by private sector agencies against them in procurement. Advocacy is often referred to as compliance without enforcement.

It would be worthwhile to consider the gains made from greater emphasis on competition in public procurement, which in turn reinforces the need for competition advocacy. As per the findings of an OECD survey, savings to public treasuries between 17% and 43% have been achieved in some developing countries through the implementation of more transparent and competitive government procurement regime. Below are some of the instances where the impact of introduction of competition in various procurement processes has been assessed:

In Russia, as a result of the reform in the field of public procurement, in 2008, an amount of \$7 billion of the Russian budget was saved.

Similarly, an independent external study for the European Commission found that increased competition and transparency resulting from implementation of the 'Public Procurement Directives' of the European Commission in the period between 1993 and 2002 generated cost savings of between 5 billion Euros to 25 billion Euros. On the other hand, collusion in public procurement markets has been conservatively estimated to raise prices of the order of 20% or more above competition levels.

# Chapter 1: Introduction and Objectives of the Report

## 1.1 Introduction

Public procurement is the purchase of goods or services by the public sector and it generally accounts for a large share of public expenditure in a domestic economy. The OECD defines public procurement as, "the purchase of goods and services by governments and state-owned enterprises. It encompasses a sequence of related activities starting with the assessment of needs through awards to contract management and final payment."<sup>3</sup> Various international organizations like the World Bank, UNCITRAL, ADB, OECD, WTO etc. have provided guidelines governing public procurement which are followed by countries apart from their own procurement regulations. Existing statistics suggest that public procurement accounts, on an average, for 15% of Gross Domestic Product (GDP) worldwide, and is even higher in OECD countries where that figure is estimated at approximately 20% of GDP. Public Procurement in India constitutes 30% of the GDP. Departments like Defence, Railways and Telecom devote about 50% of their budget to procurement, which happens to be higher than the expenditure of most state governments. About 26% of the health budget is devoted to procurement. The Competition Commission of India has estimated in a paper that annual public procurement in India would be of the order of 8 lac crore while a rough estimate of direct procurement is between Rs. 2.5 lac crore to Rs.3 lac crore. Thus total procurement figure for India is pegged at around Rs.11 lac crore per year.

Considering such huge volumes of purchase, a sound procurement system is therefore crucial for ensuring national security, safety of passengers, health of the citizen and quality of infrastructure and services.<sup>4</sup>

The primary objective of an effective procurement policy is the promotion of efficiency, i.e. the selection of the supplier with the lowest price or, more generally, the achievement of the best value for money. It is therefore important that the procurement process is not affected by practices such as collusion, bid rigging, fraud and corruption. Through bid-rigging practices, the price paid by public administration for goods or services is artificially raised, forcing the public sector to pay supra-competitive prices. These practices have a direct and immediate impact on public expenditures and therefore on taxpayers resources.<sup>5</sup>

There are various competition concerns arising in public procurement. Some of these include collusive bidding, bid rotation, cover bidding, bid suppression, market allocation and

---

<sup>3</sup> OECD Procurement Tool box. Available at: [http://www.oecd.org/document/10/0,3746,en\\_21571361\\_44258691\\_44879818\\_1\\_1\\_1\\_1.00.html](http://www.oecd.org/document/10/0,3746,en_21571361_44258691_44879818_1_1_1_1.00.html)

<sup>4</sup> "Enhancing value in public procurement," special address by Shri Pratyush Sinha, CVC, 'Conference on Competition, Public Policy and Common men.' Available at: [www.cci.gov.in/menu/speechesbypratyushsinhacvc.pdf](http://www.cci.gov.in/menu/speechesbypratyushsinhacvc.pdf)

<sup>5</sup> OECD Policy Roundtables: Public Procurement (2007). Public Procurement: The role of competition authorities in promoting competition. Available at: [www.oecd.org/dataoecd/25/48/39891049.pdf](http://www.oecd.org/dataoecd/25/48/39891049.pdf)

cartelization. Various dimensions of anti-competitive practices in government procurement could be covered by two different Sections of Competition Act 2002 i.e. Section 3 which deals with the anti-competitive behaviour of bidders including bid rigging or collusive bidding, and Section 4 which deals with abuse of dominant position and prohibits unfair or discriminatory conditions in purchase/sale or in purchase/sale price or practices further resulting in denial of market access.

There is no central law governing procurement in our country. However, comprehensive rules and directives in this regard are available in the GFR, 2005 and Delegation of financial powers Rules (DFPR), 1978. The General Financial Rules (GFR), framed by the Ministry of Finance, lay down the principles for general financial management and procedures for Government procurement. The rules have the status of subordinate legislation. All government purchases must be in accordance with the principles outlined in the GFRs. The Department of Expenditure, Ministry of Finance has also issued three separate Manuals on Procurement of Goods, Services and Works as guidelines to all central government departments in the matters of procurement. Further, the Directorate General of Supplies & Disposals (DGS&D) and the Central Vigilance Commission (CVC) have also issued guidelines prescribing the procurement procedure to be followed by all Central Ministries.

The State governments/Central Public Sector Units (CPSUs) have their own general financial rules based on the broad principles outlined in the GFR. Some states like Tamil Nadu and Karnataka have introduced legislation for procurement as for example "The Tamil Nadu Transparency in Tenders Act, 1998" and "the Tamil Nadu Transparency in Tender Rules, 2000". The Karnataka Government legislated, "the Karnataka Transparency in Public Procurement Act, 1999".

Sectoral procurement procedures have been developed within the general framework keeping in mind the specific requirements of the sector. Defence Procurement Manual (DPM) 2005 and Defence Procurement Procedures, 2005 provide comprehensive guidelines in this regard. These were revised in 2008 and the Defence Procurement Procedure 2008 came into existence with effect from August 2008.

## **1.2 Objectives**

As a part of its agenda to develop a strategy for competition advocacy with the government and the private sector, the Committee on National Competition policy (C-NCP), constituted by the Ministry of Corporate Affairs, seeks to have specific inputs and undertake evidence-based advocacy. To carry out evidence-based advocacy, a review of distortive provisions in policies, laws, regulations, practices etc. is required. The sector research study on government procurement will provide illustrative examples of those laws, regulations and policies which either exert or have the potential to exert anti-competitive effects, and thus influence the outcomes of the law/regulation/policy concerned. The purpose of the study is to bring out specific instances of policy/ law induced competition distortions. It will also recommend changes in the regulations and their implementation procedures to address the competition

related issues. The study aims to highlight an approach to promote and protect competition in the sector.

In order to achieve the above objectives, the relevant laws, regulations, policies and practices governing public procurement in India i.e. General Financial Rules 2005, State GFRs, Delegation of Financial Power Rules 1978, CVC guidelines, guidelines issued by Directorate General of Supplies and Disposal (DGS&D), manuals on procurement of goods, services and works issued by the Department of Expenditure, Ministry of Finance, procurement guidelines issued by individual ministries/departments, PSUs, separate legislations on public procurement enacted by individual states like Tamil Nadu and Karnataka and the Defence Procurement Procedure 2008 etc. will be critically analysed in line with international best practices and procurement guidelines issued by international organisations to identify provisions therein which can distort competition in the market and suggest necessary changes in the laws with a view to promoting competition.

## Chapter 2: Market Structure and Reported Competition Issues

### 2.1 Market Structure

Market structure of public procurement in India is heavily dependent upon procurement by the Central Government and State Government ministries, their departments and all statutory or public authorities. Given the volume and quantum of their summed up procurement capacity, the market structure of public procurement is of a very big magnitude and has competitive impact on the overall market of goods and services procured.

The GDP for the year 2009-10 in terms of current market prices has been Rs. 6164178 crore, which if converted to the value of total procurement for that year i.e. 2009-10 would come to Rs. 1849253 crore.<sup>6</sup> The value of total public procurement suggests the economic strength of the market which may comprise a number of goods and services procured by public authorities in India.

Apart from the said dynamics of public procurement, the system or structure of public procurement is based on a number of rules, regulations and policies of the government / public authorities. Taken together the market structure of public procurement is very complex given the uncertain facts in demand -supply processes with respect to procured goods.

Public Procurement in India is in its majority done by Public Sector Enterprises. These PSEs have been said to be the victims of domestic and international cartels, which often reflects monopolistic behaviour of the suppliers in the market who co-ordinate the production to maintain high level of prices. In the past, such behaviour has been noticed in sectors like Fertilisers, Sugar, Wheat, Pulses, and Construction Material etc.<sup>7</sup>

### 2.2 Competition Issues

During post-independence era, and before coming into existence of the MRTPC, not much has been seen to exist except the GFR 1963, which stated about public procurement. The constitutional mandate with respect to Article 299 and Article 14 has requires the executive to follow equality clause while granting contracts.

The Supreme Court in Appeal (civil) 5673 of 2006 in the case of *Nagar Nigam, Meerut v. Al Faheem Meat Exports Pvt. Ltd & Ors.* stated a very clear mandate in terms of need and relevance of competition in public procurement.

“We have no doubt that in rare and exceptional cases, having regard to the nature

---

<sup>6</sup> The total value of procurement is calculated @ 30% of GDP as suggested by CVC.

<sup>7</sup> For details see, CCI Background note on, “public procurement: achieving best value through competition.” Available at: [www.cci.gov.in/menu/backgNote091210.pdf](http://www.cci.gov.in/menu/backgNote091210.pdf)

of the trade or largesse or for some other good reason, a contract may have to be granted by private negotiation, but normally that should not be done as it shakes the public confidence.

The law is well-settled that contracts by the State, its corporations, instrumentalities and agencies must be normally granted through public auction/public tender by inviting tenders from eligible persons and the notification of the public-auction or inviting tenders should be advertised in well-known dailies having wide circulation in the locality with all relevant details such as date, time and place of auction, subject-matter of auction, technical specifications, estimated cost, earnest money Deposit, etc. The award of Government contracts through public-auction/public tender is to ensure transparency in the public procurement, to maximise economy and efficiency in Government procurement, to promote healthy competition among the tenderers, to provide for fair and equitable treatment of all tenderers, and to eliminate irregularities, interference and corrupt practices by the authorities concerned. This is required by Article 14 of the Constitution. However, in rare and exceptional cases, for instance during natural calamities and emergencies declared by the Government; where the procurement is possible from a single source only; where the supplier or contractor has exclusive rights in respect of the goods or services and no reasonable alternative or substitute exists; where the auction was held on several dates but there were no bidders or the bids offered were too low, this normal rule may be departed from and such contracts may be awarded through 'private negotiations'. (See *Ram and Shyam Company v. State of Haryana and Others*, AIR 1985 SC 1147).

In *Sachidanand Pandey v. State of West Bengal* AIR 1987, 1109, Justice O. Chinnappa Reddy after considering various decisions of the apex court summarised the legal propositions relating to public procurement in the following terms:-

On a consideration of the relevant cases cited at the bar the following propositions may be taken as well established: State owned or public owned property is not to be dealt with at the absolute discretion of the executive. Certain precepts and principles have to be observed. Public interest is the paramount consideration. One of the methods of securing the public interest, when it is considered necessary to dispose of a property by public auction, or by inviting tenders. Though that is the ordinary rule, it is not an invariable rule. There may be situations where there are compelling reasons necessitating departure from the rule but then the reasons for the departure must be rational and should not be suggestive of discrimination. Appearance of public justice is as important as doing justice. Nothing should be done which gives an appearance of bias, jobbery or nepotism. The public property owned by the State or by an instrumentality of the State should be generally sold by public auction or by inviting tenders. This Court has been insisting upon that rule, not only to get the highest price for the property but also to ensure fairness in the activities of the State and public authorities. They should undoubtedly act fairly. Their actions should be legitimate. Their dealings should be above board. Their transactions

should be without aversion or affection. Nothing should be suggestive of discrimination. Nothing should be done by them which, gives an impression of bias, favouritism or nepotism. Ordinarily, these factors would be absent if the matter is brought to public auction or sale by tenders. That is why the Court repeatedly stated and reiterated that the State owned properties are required to be disposed of publicly.

In absence of a comprehensive legislation on procurement in India, the Supreme Court judgments have guided the procurement processes in India and put checks from time to time on inefficient procurement processes. The following principles developed by the Supreme Court on procurement by public authorities may be summarised below:

- (a) Government organizations are not allowed to work in secrecy in dealing with contracts, barring rare exceptions.
- (b) Reasons for administrative decisions must be recorded, based on facts or opinions of knowledgeable persons again based on facts.<sup>8</sup>
- (c) Adequate publicity is essential.<sup>9</sup>
- (d) Officers engaged in public procurement have to perform fiduciary duty.<sup>10</sup>
- (e) There has to be fair play in the actions for procurement.<sup>11</sup>
- (f) Bid evaluation has to be strictly in accordance with the bid evaluation criteria stated while inviting the bids.<sup>12</sup>

Supreme Court judgments from time to time have guided the procurement processes in India. The following additional principles developed by the Supreme Court on procurement by public authorities are summarised below:

1. In a leading case, *Erusian Equipment and Chemicals v. State of West Bengal*<sup>13</sup>, the Supreme Court laid the foundation of the law by emphasising on the entitlement to equal treatment with others who offer tender or quotations for the purchase of goods and further reiterated that the activities of the Government have a public element and, therefore, there should be fairness in procedure and equality. Thus, the Government cannot act in a whimsical or capricious manner, nor can it act as a private giver may. Its procurement policies must be informed by reason be fair, transparent, non-discriminatory and non-arbitrary, and it is the courts which would safeguard any transgression of the same.

---

<sup>8</sup> *G.B. Mahajan v. Jalgaon Municipal Corporation* JT 1990 (2) SC 401

<sup>9</sup> *Committee of Management of Pachaiyappa's Trust v. Official Trustee of Madras & Another* (1994) SCC 475

<sup>10</sup> *Delhi Science Forum v. U.O.I.* 1996 (2) SCALE 218

<sup>11</sup> *Mahesh Chandra v. Regional Manager, U.P. Financial Corporation and others*, JT 1992 (2) SC 326

<sup>12</sup> *M/s Prestress India Corporation v. U.P. State Electricity Board and others* 1988 (Supp) SCC 716

<sup>13</sup> 1975 (1) SCC at page 70

2. In *G.J. Fernandez v. State of Karnataka*<sup>14</sup>, the Supreme Court was concerned with a tender which set forth certain "minimum qualifying requirements" and also went on to require some documents "along with the application for issue of tender documents". *The court held that if the tendering authority had in its wisdom decided to relax some non-essential or ancillary conditions or to grant extra time for furnishing the same, that would not by itself render its conduct objectionable or the bids received consequent to such deviation bad.. It held that such deviations (if made) should not result in arbitrariness or discrimination or substantial prejudice to any of the parties involved or to the public interest in general.*

3. To a similar effect is another Supreme Court decision in *Raunaq International Limited v. I.V.R. Construction Ltd. & Ors.*<sup>15</sup> where the Court held that if the tender condition permits relaxation and it is granted for bona fide purposes then the court should hesitate to intervene.

After notification of Section 3 and 4 of the Competition Act, 2002, Competition Commission of India acquired jurisdiction to deal with anticompetitive actions of enterprises anywhere in India. This includes cases of public procurement, since government departments do fall within the definition of enterprise under Section 2(h) of the Competition Act, 2002. There are few cases dealing with public procurement investigated by the Director General of the Competition Commission of India (CCI) wherein the investigation report found breach of Section 3 and 4 of the Act. Although no case is reported as on date wherein CCI has by majority found breach of any of the provisions of the Act in a case of public procurement yet some of dissenting opinions in these cases does reveal a great deal of competition issue in public procurements.

In Case No. 4/2010 i.e. *Explosive Manufacturers Welfare Association v. Coal India Ltd. and its officers*, the dissenting order has not only disagreed with majority but also laid down competition implications in public procurement cases. "Whenever public procurement is made without calling for tenders and on nomination basis, it excludes large number of persons who could have participated and got orders. Public procurement by nomination is not only against the law of the land but it is also exclusionary in nature. It kills competition in the market and leads to lower investment, lower development and may be higher expenditure for the public procurer. The agreement for procurement on nomination basis therefore leads to appreciable adverse effect on competition in India. Therefore there is a violation of not only Section 3(1) of the Act and consequently Section 3(2) of the Act. The order further reads that the State and its instrumentalities are not living persons. The purchases/sale of assets of such a person cannot be equated with private purchases where a person has the option to make his own choice. As already discussed, public procurement can lead to make anticompetitive infringements. No general rule can be framed and the facts have to be examined on case to case basis. But in any case the state looks towards the welfare of its citizen. It not only protects the freedom of speech and trade but also sees that there is equality before law, equality of opportunity and economic justice. No minion of the State or its instrumentalities can forget the laudable ideas for which the State exists, and take shelter behind the maxim 'freedom of choice.' Freedom of choice does not work in public procurement because many factors come into play when a decision of procurement is made.

---

<sup>14</sup> (1990) 2 SCC 488

<sup>15</sup> (1999) 1 SCC 492

Similar dissenting but laudable approach on public procurement and competition has been made in some other cases before the CCI as well such as Case No. 10/2010 i.e. *M/s. Pankaj Gas Cylinders Ltd. v. Indian Oil Corporation Ltd.*, Case No. 20/2011 i.e. *Pawan Kumar Agarwal v. Rashtriya Ispat Nigam Ltd.*, Case No. 15/2010 i.e. *Jupiter Gaming Solutions Private Limited v. Government of Goa & Ors.* All these cases reveal one approach of interpretation of the Competition Act, 2002 under which inefficient public procurement is necessarily found to be causing appreciable adverse effect on competition in India thus void under section 3(2) of the Act and remediable under sections 27 and 28 of the Competition Act, 2002.

After considering case laws and principles developed in the light of prevailing laws, rules and regulations governing public procurement in the country, the following may be highlighted as some of the competition issues in public procurement.

- 1. Competitive Neutrality:** Competitive Neutrality describes the aim of a level playing field in mixed public/private markets, where state owned or quasi-public bodies line up to compete with private sector companies. These markets tend to be distorted as a result of structural advantages enjoyed by public providers and a failure by public buyers to ensure fair process. In today's competition context, the demand and existence of competitive neutrality across public procurement processes is no longer a buzzword and in its absence the distortionary effects on competition and market are well known. Interviews with stakeholders suggest that Indian Railways( one of the largest procurers), procures high value traction equipment items for ALCO Diesel Locomotives on annual basis from Bharat Heavy Electrical Ltd. (BHEL – a Govt. of India PSU ) by operating their Price List without following the normal tendering process. This is against the spirit of competitive neutrality.
- 2. Market Sharing and Cartel formation:** Market sharing and Cartel formation among the suppliers of various goods and services in India is quite rampant. In many cases, where same price is quoted by suppliers, the public procurer distributes the quantum of procurement among all of them, either equally or through some discretionary variations. It may also be seen that producers of same/similar goods tend to share the market based on their understanding. For example, if there is a tender in south India the north Indian producer will not bid for it and vice-versa. Although such sharing or understanding defies the logic that any producer will go for more market share yet given the Indian economic scenario, such practices of market sharing are obvious and known.<sup>16</sup>
- 3. Entry Barriers created by policies and parties in procurement:** There are entry barriers for suppliers of goods and services in the public procurement processes which make the cost of procurement high and inefficient. In order to elaborate this issue, a reference may be drawn on requirement to supply a proprietary product rather than prescribing standards/specifications for goods to be procured. A system of procurement like this eliminates a number of players who could have given a competitive price for supplying goods of the provided specifications or standards.

---

<sup>16</sup> See presentation on Competition issues in Regulated Industries: Case of Indian Transport Sector. Available at: [www.cci.gov.in/images/.../presentations/1.../4competitionissues\\_transport.pdf](http://www.cci.gov.in/images/.../presentations/1.../4competitionissues_transport.pdf)

4. **Bid rigging and Collusive bidding:** In public procurements, horizontal agreements i.e. agreement between competing firms are common. Bid Rigging is a form of fraud with the purpose to fix price or/and share market demand, often adopted where contracts are determined by auction. Bid Rigging can be achieved under alternate terms of agreements between the firms and almost always results in economic harm to the public department that is seeking the bids.
5. **Abuse of Dominance:** Dominant firms in the public procurement system may use their incumbent power any new entrants in to the market by indulging in pre-datory pricing. Predatory pricing is a strategy of selling product or service at a low price (below cost) with the objectives to drive competitors out of the market or create barriers to new potential competitors. Like many competition laws of many countries, Indian Law also identifies predatory pricing as an anti-competitive activity.
6. **Information asymmetry and its impact on Competition:** It may be seen that there is no projected information available in public domain suggesting, goods or services and their quantum to be procured by the public authorities. Sudden decision to procure any good or service strains the existing capacity of supply which creates a price pull factor, often leading to inefficient procurement. It is an accepted fact that there are limitations associated with collection of information, its analysis and finally in its application. Life and time are finite; flow of information is unending and varied. Decisions have to be made within the stipulated time period giving due regard to biases of the parties. Therefore, information asymmetry continues to be an essential feature to identify in a market. This signifies that the continuation of market asymmetry keeps the challenge alive for advocacy programmes of competition polices and also that of Competition Authorities.
7. **Monopsony:** Monopsony reflects market power on the buying side of the market. When monopsony power is exercised, it causes economic inefficiency and a transfer of wealth to the buyer. As a result, competition concerns such as buyer cartels, predatory overbuying, overbuying strategies designed to raise rivals' costs, and mergers that create or enhance monopsony power arise.

### **2.3 Initiatives taken by the government to promote competition in public procurement:**

Some positive steps taken by the government to enhance competition in public procurement and increase transparency in the process are as follows:

- E-Procurement of stock items has been introduced in Indian Railways to the extent of over 70 per cent. This step has significantly enhanced transparency, reduced chances of corruption and minimised delays in the process.
- Threshold limit for issue of open tenders has been reduced to Rs. 10 lacs as against the corresponding limit of Rs.25 lacs laid down in GFR, 2005. This has increased the number of open tenders considerably thereby enhancing the participation of new

entrants who would otherwise have been left out because of higher threshold limit prescribed in GFR, 2005.

- Government of India has started Indian Government Tender Information System- [www.tenders.gov.in](http://www.tenders.gov.in) which details tenders floated by Central government ministries/departments, PSUs, State governments, public sector banks and other organisations separately for goods, services and works. It lists all relevant information in respect of active tenders and tenders in archives. It is a major step towards increasing transparency and also to ensure that no prospective bidder misses an opportunity to participate in the tenders.

## **Chapter 3: Identification and listing of anti-competitive provisions and practices**

The sequence of given events for an effective competition regulation may appear different in India because the Competition Act, 2002 came first and design of competition policy followed thereafter (it is generally believed as per legal sequence that law follows policy). It may be of significant debate and discussion that majority of laws in India belong to the pre-independence era and therefore need a necessary competition scrutiny. However, rules relating to government procurement have shown clearly their impact on the economy. Such rules have been found to be deficient from the competition angle. An example may be taken from an area outside procurement in order to examine it from the point of view of competition; The G.O.Ms. 110 dated 19.02.2009 issued by the Government of Andhra Pradesh in exercise of powers under Section 11(2) (a) of the Andhra Pradesh Cinema Regulation Act, 1970 and Rules 11C and 17A of the Andhra Pradesh Cinemas (Regulation) Rules, 1970 purports to create a regime of exclusive rights in favour of one or more enterprises relating to online ticketing for cinemas in Andhra Pradesh. On plenary perusal any common man may state that this is not a good system. However, some may opine that the State has to see who can provide best services in the interest of people.

Considering the perception of common man on this issue it may be found that the given State law is has some provisions, which authorise the Government to take a decision as it has taken. But viewing the same from the competition angle, it may be seen that the concerned law has gone against the spirit of competition in the given sector ,has limited choice of people and also created unnecessary entry barriers for competitors.

Similar instances may be seen in Government procurement as well, however well-intentioned the provisions of GFR, 2005 or CVC guidelines may be anticompetitive impacts are writ large through the operational regime of these rules and guidelines. The same may be a relevant point for other laws/rules/regulations relating to Government procurement in India.

### **3.1 Issues in identification of anticompetitive provisions and practices**

As already stated, laws, rules and regulations relating to public procurement in India may contain anticompetitive elements.

Methodically it is pertinent to pick up publically available statutes and scrutinise them for provisions relating to public procurement and scanning the same for their anticompetitive nature or impact. A particular rule or guideline or provision of an Act may look highly discretionary and an opinion may be formed that possibility of an abuse of discretion in cases of public procurement is anticompetitive. Such opinion may not

find any corroborative practice to create evidence that the said provision is anticompetitive, thus, needs legislative changes.

The matrix below gives the anticompetitive effect or possible effect of given provisions.

Provisions/ Laws/ Rules/ Regulations/ Guidelines	Detailed Provision (text) of Laws /Rules / Regulations / Orders / Guidelines	Effect or possible effect including through practices of existing rules /laws	Changes suggested to make impact of given rules competitive
<b>Chapter 6 of GFR, 2005 – Procurement of Goods and Services.</b>	GFR Rules 135 to 185: Rules from 135 to 162 relate to Procurement of Goods and those from 163 to 185 relate to Procurement of Services.	Rules are generally and very broadly worded, which are open to vagaries of interpretation and discretionary choices. Thus, competitiveness in the procurement process may be compromised.	Although GFR was overhauled in 2005, however, in the absence of a full-fledged law on procurement and legislative mandate on fixation of accountability of those involved in discretionary use of authority causing loss to exchequer, GFR 2005 may be suitably modified.
- do -	Rule 137. Fundamental principles of public buying - The procedure to be followed in making public procurement must conform to the following yardsticks :- (i) the specifications in terms of quality, type etc., as also quantity of goods to be procured, should be clearly spelt out keeping in view the specific needs of the procuring organizations. (ii) offers should be invited following a fair, transparent and reasonable procedure;	Rule 137 (i) is open ended. Possibility of preparation of specific supplier oriented specifications must be ruled out to avoid compromising competition by propagating exclusionary conditions of procurement thereby limiting ability of suppliers to compete.	The rule should be amended to include the mandate that no specification should be directly derived or based from a particular producer. Generic specifications must be prescribed.  If given product conforms to any standard in such a case standard must be also prescribed in the specification requirement.

	(iii) the procuring authority should be satisfied that the selected offer adequately meets the requirement in all respects etc.		
- do -	Rule 141. Rate Contract: The Central Purchase Organization (e.g. DGS&D) shall conclude rate contracts with the registered suppliers, for goods and items of standard types, which are identified as common user items and are needed on recurring basis by various Central Government Ministries or Departments.... And rule 142 lays down registration of suppliers.	Such Rules limit the number and range of suppliers. Rate contracts are demand driven and not supply driven, thus, procurer limits its choice of suppliers in the long run. Such a situation adversely affects competition in the given relevant market. This is further facilitated by registration of suppliers. The process of registration of suppliers in terms of Rule No.142 and Chapter 5 of DGS&D Manual 1999 itself limits the number and range of suppliers. It acts as a barrier to entry for new entrants and also for innovation.	Rate contract limits the choice of procurers to the items listed on the rate contract. At times, it may so happen that an item on the rate contract is available in the open market at a cheaper price but existence of rate contract binds the procurer to go in for the item operating the rate contract at a higher rate. Either the possibility of purchase of goods in special circumstances outside the rate contract should be permitted, so as to derive best value for money or the contractor be bound by a framework agreement to reduce the rates to bring it at par with the lower rates at which a particular department of the Central or state government is procuring the item. General Conditions of Contract of Government of Rajasthan have this provision included in the agreement.
- do -	Rule 144. Reserved Items: The Central	Such system undermines the	One has to bear in mind that due to trade

	<p>Government, through administrative instructions, has reserved all items of handspun and hand-woven textiles (khadi goods) for exclusive purchase from Khadi Village Industries Commission (KVIC). It has also reserved all items of handloom textiles required by Central Government departments for exclusive purchase from KVIC and/or the notified handloom units of ACASH (Association of Corporations and Apex Societies of Handlooms). The Central Government has also reserved some items for purchase from registered Small Scale Industrial Units. The Central Departments or Ministries are to make their purchases for such reserved goods and items from such units as per the instructions issued by the Central Government in this regard.</p>	<p>substitutability of goods, limiting choices of procurer. This may be a policy barrier created in the process of procurement. SMEs may be made competitive by other processes but not by safeguarding their interest and compromising competition in the given sector and the relevant market.</p>	<p>liberalisation large number of goods made by domestic SMEs face tough competition from foreign suppliers. Hence, SME reservation itself has become hopeless. Such policy induced distortions (reservation in procurement) must be resorted to on a minimal basis on proper justification to advance public interest.</p>
- do -	<p>Rule 147. Purchase of goods directly under rate contract: (1) In case a Ministry or Department directly procures Central Purchase Organization (e.g. DGS&amp;D) rate</p>	<p>While a rate contract gives predictability of prices, avoidance of cumbersome tendering processes etc., the incentive to bargain for a lower price is dampened.</p>	<p>Such a situation i.e. "In case a Ministry or Department directly procures Central Purchase Organization (e.g. DGS&amp;D) rate contracted goods from suppliers, the prices to</p>

	contracted goods from suppliers, the prices to be paid for such goods shall not exceed those stipulated in the rate contract.		be paid for such goods shall not exceed those stipulated in the rate contract," must be covered under the framework agreement so that it becomes binding on the firm and no loss to the procurer is caused.
- do -	Rule 150. Advertised Tender Enquiry. (i) Subject to exceptions incorporated under Rules 151 and 154, invitation to tenders by advertisement should be used for procurement of goods of estimated value Rs. 25 lakh (Rupees Twenty Five Lakh) and above....	The rule could be made more competitive as it restricts the number of suppliers. Ceiling lower than Rs. 25 lakh could bring in more competitive character in procurement process. Some of the government departments have already brought down such ceilings. Need to streamline.	Advertised tender enquiry should be the norm for all public procurements to optimise competition. Threshold limit of Rs. 25 lakhs be systematically brought down to Rs. 10 lakhs to increase the degree of participation as has been done in the Indian Railways.
- do -	Rule 151. Limited Tender Enquiry. (i) This method may be adopted when estimated value of the goods to be procured is up to Rupees Twenty-five Lakhs. Copies of the bidding document should be sent directly by speed post/registered post/courier /e-mail to firms which are borne on the list of registered suppliers....	Such a system limits number of suppliers, which may result in information asymmetry and loss to procurer due to lack of choice available. It may lead to price rigging or area distribution by suppliers. Such provisions may have high anticompetitive effect.	While open competitive bidding should be the norm, limited tendering should be used in exceptional circumstances as it limits the number and range of suppliers and can lead to loss to the exchequer. This can be the cause of collusive behaviour by the bidders.
- do -	Rule 157 and 158	Bid security or	Rule 157 should allow a

	stating about bid security (up to 5%) and performance security (up to 10%).	performance security must not operate as barriers to entry, which have the potential to thwart competition in the given segment. 15% upfront provision of money in a big ticket tender may operate as a restrictive condition.	bank guarantee and not upfront payment of security amount.
- do -	Rule nos. 163 to 185: - Procurement of Services	Rules pertaining to procurement of services are no different in their interpretation and outcome vis-à-vis rules relating to procurement of goods. Thus, similar anti-competitive impact may be observed through operation of these rules as well.	Rules 163-185 are based on earlier rules so these need similar tweaking or changes.
- do -	Rule 179 Lays down broad criteria for preparing a list of likely and potential contractors on the basis of formal and informal enquiries from other ministries or departments and organizations involved in similar activities including scrutiny of yellow pages and trade journals etc.	Rule 179 is open ended which may lead to formation of limited contractor base thus compromising competition. These contractors would be meeting frequently and thus possibility of formation of cartel would be high which could lead to avoidable loss to the procurer.	Procedure of listing out likely and potential contractors should be more broad based and exhaustive based on their past performance and credentials so that possibility of capable contractors with a good track record and credentials being left out of participation in the tender is ruled out.
- do -	Rule 181(a) Lays down	Procedure for first	In the case of value of work or service costing

	<p>procedure to be adopted for issuing Limited tender enquiry (for works or service costing up to Rs.10 lakhs) to <i>prima facie</i> eligible and capable contractors after scrutinizing the list of likely and potential contractors as identified as per Rule 179 above.</p>	<p>listing likely contractors and then scrutinising the list to decide <i>prima facie</i> eligible and capable contractors for issue of Limited Tender prohibits competition in the given relevant market. Such a system limits choice of procurer and affects competition in the segment. In the case of value of work or service costing up to Rs.10 lakhs also, Advertised Tender enquiry should be issued to promote competition and obtain good value for money. Refer Rule 181(b).</p>	<p>up to Rs.10 lakhs also, Advertised Tender enquiry should be issued to promote competition and obtain good value for money. Refer Rule 181(b).</p>
- do-	<p>Rule 184. Describes the procedure for outsourcing a job to a specifically chosen contractor in an exceptional situation. Enlistment of Indian Agents: As per the Compulsory Enlistment Scheme of the Department of Expenditure, Ministry of Finance, it is compulsory for Indian agents, who desire to quote directly on behalf of their foreign principals.</p>	<p>Although safeguards have been provisioned in Rule 184 before outsourcing a job to a specifically chosen contractor, however, such rules stifle competition in the market place and are a hindrance in providing good value for money.</p>	<p>Resorting to such Rules should be rare and existence of adequate safeguards should be pre-determined.</p>
<b>Indian</b>	Chapter III. Purchase	Rules are generally	

<b>Railway Code for Stores Department. Vol .1</b>	of stores : policy and rules purchase policy	and very broadly worded. Thus competitiveness is compromised and competition may not exist in the procurement process.	
- do -	Rule 324: Open Tender System: used, in all cases in which the estimated value of purchase is (i) over Rs. 10 lakh in normal circumstances, for procurement of items other than safety items (ii) over Rs. 2 Crore in cases of emergencies and (iii) over Rs. 2 Crore in cases of procurement of safety items and procurement of items whose approved list of vendors is issued by Centralized approving agency i.e. RDSO/PU/CORE etc.	Although it is called Open or Advertised tender, in fact, at least 95 per cent of the indented quantity is covered on the approved vendors of RDSO, PUs/CORE etc. leaving aside only 5 per cent quantity that can be covered on the unapproved vendor whose bid is otherwise found suitable. Thus the system of restricting 95 per cent coverage on approved vendors, can by no stretch of imagination be called an Open or Advertised Tender.	Rationale behind Railways limiting 5% coverage of quantity on unapproved vendors is appreciated in view of highly critical and complex nature of application of such items. Since these vendors who today are eligible for 5% quantity will in due course of time become eligible for cent per cent order through RDSO vendor approval process, there is a need to streamline and expedite the process of approval of vendors by RDSO as the delay in the process acts as a disincentive to the prospective vendors who are otherwise well equipped and capable.
- do -	Rule 328: Criteria for issue of Limited tender Enquiry up to Rs.10 lakh except in case of procurement of safety items, in case of procurement in emergency and in case of procurement of items whose approved list is issued by	As it may be tested on the competition parameters, the said rules seems highly restrictive and leads to formation of very limited vendor base thus stifling competition as the procurement of safety & other critical items	Railways rationale of procuring critical and complex safety items through limited tenders is based on sound principles since ultimate objective is to procure quality material on time. If critical items having bearing on safety in train operations are procured through open

	centralized agency i.e. Research Design & Standards Organisation (RDSO), Production units (PUs) & Central Organisation for Railway Electrification (CORE) in which case estimated value of purchase should not exceed Rs. 2 Crore.	required in emergency is restricted to the approved vendors of RDSO/PUs/CORE. This is nothing less than indulging in unfair practices and denial of access to the market thereby creating conditions conducive to anti-competitive activities.	bidding without ascertaining their capability, it can surely lead to disaster. Only remedy is to expedite process of vendor approval by RDSO/CORE/PUs etc.
<b>RDSO Vendor Approval Process Guidelines-- Detailed from QO-D-7, 1-1 to QO-F-7,1-3 (MRF No. 0401) of the Quality Standards documents.</b>	Process is a part of Quality Standards covered in 20 documents. hence is being covered briefly: A Firm that approaches RDSO is first subjected to a detailed scrutiny, inspections etc. before it is approved as a developmental vendor which entitles the firm to bid for up to 5 per cent of the purchase of a particular item. Subsequently, the status of the firm can be upgraded to Part II vendor who becomes eligible for 25 per cent of the total requirement of an item. After 3 years, a Part II vendor can be categorised as Part I vendor, eligible for full quantity order for supply of an item.	The System of Vendor Approval is complex and time consuming, besides being restrictive. It discourages potential bidders from participation. As a result it restricts competition and enhances the possibilities of formation of a cartel. Combined effect of the limited approved vendors, time taken in approval and very little volume of supply permitted to a new vendor under approval to Part I status suggests that the system does not encourage competition, economy and effectiveness. This process acts as a "Barrier to Entry" and thus limits the ability of suppliers to compete.	Approval system needs to be mechanised and made time bound, discretionary elements in the approval process must give way to objective criteria.
<b>DGS&amp;D Purchase</b>	Chapter 5 describes the Process of	Unless certain improvements are	

<p><b>Manual Effective from 1st Oct. 1999</b></p>	<p>registration of Suppliers by DGS&amp;D</p>	<p>brought about in the process, it will act as a barrier to entry for the new potential bidders.</p>	
<p>Chapter 5 of the DGS&amp;D manual, 1999, describes process of Registration of Suppliers in detail.</p>	<p>With a view to establish reliable sources of supply for government purchases, firms are registered by DGS&amp;D as approved contractors for supply of stores. Firms are registered for a fixed period depending on the category of registration. Registration of firms for supply of indigenous items is made in the categories of Manufacturers, Assemblers, Converters, Sole Selling Agents of Indian Manufacturers, registration of suppliers who supply imported stores, foreign manufacturers and their Indian agents. The application forms can be obtained from any of the 20 designated Registration centres of QA Wing or from the Registration Branch at DGS&amp;D, New Delhi. The authorities competent to deal with the applications and grant registration are as per the delegation of authority. In cases which survive preliminary scrutiny, arrangements are made to obtain Bankers Report, Annual Turnover, Inspection report of</p>	<p>Such Rules limit the number and range of suppliers. Besides, certain relevant details like calendar for invitation of applications along with list of items or group of items for which registration is being processed and the model time frame for conclusion of the registration process etc. are missing. Unless the process is made more transparent, wide publicity is given and reasonable time frame is made public, it will act as a barrier to entry for new entrants thereby stifling competition.</p>	

	<p>Manufacturers facility for assessing their capability and capacity as a manufacturer and past Performance by the QA Wing and Test report of their products like Oil Paints, Varnish etc from a laboratory at their own expense. On receipt of inspection reports recommending registration, such cases are processed by the Registration centre and Registration Certificates are issued with the approval of the competent authority.</p>		
<p>Chapter 13 of the DGS&amp;D Purchase Manual 1999 details procedure followed for concluding Rate Contract for procurement of standard items and Items of common use with an estimated annual withdrawal of Rs.25 lakh or more directly by the user departments.</p>	<p>A Rate Contract is an agreement between the Purchaser and Supplier to supply stores at specified prices during the period covered by the contract. The rate contract is in the nature of a standing offer from the supplier firm. A legal contract would come into existence with the placement of individual order (Supply Order) and each such supply order will constitute a separate contract. The supply orders can be placed on any of the rate contract holding firm(s) either directly by the authorized</p>	<p>Procurement of goods by operating Rate Contract is considered anticompetitive as it limits the range of suppliers and choice of common user items by the indentors. Moreover, possibility of certain items under rate contract being available at a lower rate outside the rate contract is not ruled out in which case procurer will suffer financial loss since he is bound by the terms of the rate contract. Besides, since rate contract can only be concluded on firms registered with DGS&amp;D, it not only</p>	<p>As suggested against Rule nos. 141&amp;147, if a particular item is being procured by some departments of Central or State Governments at a rate lower than at which rate contract is concluded, it should be binding on the firm under rate contract to reduce rates to be at par at which a particular item is available outside rate contract. This should form a clause of the frame work agreement as per the policy followed by Government of Rajasthan.</p>

	<p>officers of the indenters (known as Direct Demanding Officers) or by the DGS&amp;D. The decision to bring or delete an item on / from rate contract will be taken by the Standing Review Committee (SRC) under the Chairmanship of DG(S&amp;D). SRC has representatives from major indenting departments like Defence, Railways, Home Affairs, Health, Telecommunications, State Governments and Trade organizations and is assisted by a Sub-Committee under the Chairmanship of ADG(Supplies) with Director (CDN) as Member-Secretary. Rate contract is awarded to the firms registered with DGS&amp;D/ NSIC. The firms getting registered within 90 days from the date of tender opening are also considered if their offer is otherwise eligible. The past performance of a firm is one of the considerations in awarding fresh rate contract to the firm.</p>	<p>acts as a barrier to entry, it also creates conditions conducive to cartel formation.</p>	
--	---	--	--

### **3.2 Observations on the Public Procurement Bill, 2011:**

An analysis of the draft Public Procurement Bill, 2011 has been found to be well drafted and covering the entire gamut of public procurement in sufficient details. It has been found lacking on two counts viz.-

- ✓ It does not recommend the creation of an independent regulatory authority that would maintain an oversight on compliance of the Act and the rules made thereunder, in addition to discharging the quasi-judicial functions of settling disputes. The Authority would also advise the Government on diverse matters relating to public procurement. The appointment of an independent regulator is considered necessary to maintain an oversight over the procurement of goods, services and works to ensure compliance with the applicable laws, policies, guidelines and procedures. The setting up of an independent regulator is also considered essential to investigate any complaint relating to procurement and direct the relevant procuring entity to take necessary action.
- ✓ The draft Public Procurement Bill, 2011 does not recommend the establishment of a Department of Procurement Policy under the Ministry of Finance. The establishment of a separate Department of Procurement Policy is considered necessary to exercise the powers to promote probity, transparency, economy, quality and competition in procurement. Formation of a separate department is important to prescribe the procurement rules for application to all procuring entities or to any particular department, statutory entity or public sector undertaking and for procurement of works, goods and services respectively. Besides, it could institute best practices, professionalise the public procurement function, arrange for capacity building, create and maintain the overarching public procurement portal.

### **3.3 Policy Induced Competition Distortions: Case Studies**

#### **3.3.1 The Monopoly Cotton Procurement Scheme (MCPS)**

This scheme was governed by the Maharashtra Raw Cotton (Procurement, Processing, and Marketing) Act, 1971, which was defined as "An Act to provide for carrying on for a certain time all trade in raw cotton by the state of Maharashtra."

The Monopoly Cotton Procurement Scheme (MCPS) has been in operation since 1972-73 in Maharashtra. Under this scheme, Cotton procurement was the monopoly of the MSCCGMF and the farmer was not only assured of the MSP, but also received a bonus if MSCCGMF made profit. The aim of the scheme was to capture the whole economic value for the farmer i.e. from growing cotton to selling finished cloth. The state government proposed to do this by helping farmers get a fair price for their produce, make available unadulterated cotton to consumers at reasonable prices, produce textiles and distribute bonus (profit on operations) to farmers. Therefore, the CMS allowed politicians to control the state's cotton industry. It was in 1984 that the state government set up The Maharashtra State Cooperative Cotton Growers Marketing Federation Ltd (MSC), an Apex cooperative society. It administered the CMS for the state

government and was responsible for procurement, processing, storage and sale of cotton. Under the CMS cotton produced in the state had to be pressed within the state only. MSC purchased cotton from farmers at a minimum support price (MSP). Payment was in installments and often delayed due to non-availability of funds. At the time of payment the Kharidi Vikri Sangh (sub agent of MSC) deducted loans taken by farmers from co-operative banks (up to a maximum of 50% of payment) and paid the balance. MSC entered into conversion contracts with G&P units and then sold cotton in the open market. Since only MSC units could buy cotton in the State entrepreneurs were compelled to set up G&P units in border towns of adjoining states e.g. Burhanpur in Madhya Pradesh. Thus cotton was illegally sent out to other states. As a result Value Addition took place outside the State with adverse impact on employment/economic activity.

Over time, a plethora of problems were identified with the scheme. The bonus was converted to additional advance price that was also guaranteed. The payment of additional price was de-linked from the actual market scenario leading to instances when Cotton was purchased dear and sold at a cheaper rate. This led to a loss that cumulated over time. In addition to this, poor storage facilities led to mixing of different grades of Cotton and destruction by fire and rain. Office bearers involved in grading and weighing took to rent seeking activities. The farmers paid commission to middlemen at the procurement centres. There emerged a class of traders in the guise of farmers. The farmer sold his produce to trader-farmer at a lower price who in turn sold it to the MSCCGMF. The payment to farmers was delayed and staggered.

**Impact of CMS on state finances & production:** The scheme worked well till 1993-94 when Politics took over. See table.

Year	Loss (Rs. Crores)
2004-05	1620
1999-00	913
2001-02	861
1998-99	623
1995-96	515
1996-97	383
<b>Cumulative Loss till 31/8/06</b>	<b>5728</b>

Loss was funded by loans from the State government Rs. 4,678 crores, Mumbai Metropolitan Region Development Authority (MMRDA) Rs. 596 crores and balance through internal accruals. As the State's fiscal condition worsened it stopped funding MSC.

The Scheme had a negative impact on state's cotton production. See table.

### Maharashtra

	2005-06	2000-01	1996-97	1991-92	2005-06	2000-01	1996-97	1991-92
Cotton production lakh bales of 170kgs	244	140	178	119	36	18	33	12.5
Yield kgs./ hectare	468	278	331	266	212	101	182	79

%					14.8	13.0	18.5	10.5
India production								

Source: Confederation of Indian Textile Industry.

From the table it can be seen that yields are less than 50% of national average, production has hovered around 33 lakh bales during the decade starting 1996-97. Since growing cotton was not financially rewarding area under cultivation has stagnated at app 30 lakh hectares between 1995-96 and 2005-06. If things were always that bad why did the British develop an extensive rail network in Vidharbha's Amravati district so they could ship cotton to Manchester.

Today CMS is virtually redundant. Market play has resumed. Farmers sell their produce to the best bidder. Any entrepreneur can set up a G & P unit. Until procurement was opened to private traders in 2003, all cotton in Maharashtra, India's second-largest producing state, had to be sold at fixed prices. While protecting farmers against low prices in some years, the policy also led to lower returns in years of high market prices and in delayed payments to farmers when the scheme ran large financial deficits. The 2003 reform, in addition to reducing financial costs, has clarified and strengthened price signals to farmers. Cotton production in Maharashtra has almost trebled in the last five years. From a mere 35 lakh bales in 2005-06, the production has increased to 92 lakh bales in 2010-11, a growth of 162 per cent, according to the figures released by the Cotton Advisory Board.

Government officials and industry experts attribute this rise in production to the termination of Cotton Monopoly Act of Maharashtra Government. The Act, which came into force in 1972, ensured that only the State Government could procure cotton from farmers, at a predetermined price. The act was repealed in 2004, after heated discussions in the State Assembly.

### 3.3.2 NHAI Move to Restrict Bidders

The National Highways Authority of India (NHAI) has imposed a ceiling on the number of applicants eligible to bid for engineering, procurement and construction (EPC) projects. In two projects being bid out, the authority stipulated that not more than seven bidders would be shortlisted even if more firms are qualified for the project.

As per the changes introduced through two EPC projects put out for bidding in September 2011, a bidder should have completed work totalling five times of the total cost of the project bid for. In comparison, a standard build-operate and transfer (BOT) project requires the bidder to have completed work equivalent in value of the current project. The threshold capacity of a bidder has to be Rs. 3,460 crore for the Rs. 692-crore project of two-laning of highway from Tanda to Rae Bareilly in Uttar Pradesh. In the R525-crore Rae Bareilly-Banda stretch, the threshold is kept at Rs. 2,625 crore.

NHAI has also raised the net worth eligibility by seeking bids only from those bidders who have a net worth of at least 50% of the project cost. A standard BOT project demands a net worth of 25% of project cost. In case of joint ventures or consortia, the authority would consider the technical and financial capacity of only the lead member.

These conditions deprive most of the applicants even after meeting the qualification criteria prescribed in the bidding documents for these projects and may lead to lack of transparency in the bidding process. Also, the decision of shortlisting only seven bidders is in gross violation of competition rules as no equality is ensured in the bidding process.



## Chapter 4: Analysis of the Identified Issues

The yardsticks of fairness, integrity and transparency through competition, efficiency and economy in public procurement practices established by the GFR 2005, have either failed to achieve their objective or have remained ineffective. As may be seen in the analysis of aforesaid GFRs relating to procurement of goods and services, that the five fundamental principles, namely, open tendering, effective advertisement, non-discriminatory tender conditions and technical specifications, public tender opening (bid evaluations based on a pre-disclosed criteria and methodology), and award to the most advantageous bidder without any negotiation on price or any other terms, do seem to exist under the GFR 2005 but equal set of discretionary and vague GFRs as highlighted above mar the desired effectiveness of the rules.

In the Indian context, competition effects from procurement are mostly negative today. In the initial era of industrialization, the impacts might have been positive due to rise of PSEs and growth in production and consumption levels in the economy. The public sector, by virtue of its overall demand in certain markets, may be having a distortionary effect on competition. A general defence may be taken by big PSEs in India that they protect and promote competition, for example, by maintaining a competitive market structure through deliberately sourcing their requirements from a range of suppliers, by providing incentives to suppliers to invest and innovate, or by helping firms to overcome barriers to entry. Specific case of Indian Railways and Steel Authority of India Limited (SAIL) may be considered wherein all requirements of rails of Indian Railways is met by SAIL, their main pro competition argument may be that they are creating demand, promoting innovation and efficiency). It may, however, also restrict and distort competition, e.g. by adopting procurement practices that have the effect of restricting participation in public tenders and that might even discriminate against particular types of firms. Last but not the least, the public sector may fail to contribute towards an improvement of competitive conditions where it could in principle do so.

### 4.1 Limiting number of suppliers

The number of suppliers may be limited when procurement rules lay down a technical specification in terms of a proprietary product and do not lay down generic specifications. For example, a public authority is procuring fans, motors but it lays down the condition that wiring to be procured for fans and motors must be from ANCHOR wires. The said qualification is not purely technical, it rather carries a proprietary element and significantly reduces number of suppliers, who could have supplied fans and motors of given capacity. Such outcome is obvious from application of Rule 152 of the GFR, 2005 and rules akin to it, despite the fact that there might be good arguments in favour of this rule, yet the impact is anticompetitive. Similar outcomes are perceivable from rules providing for rate contracts, wherein procurement is logged into for the entire year. When numbers of suppliers of a particular product are limited by the public authority by its own rules, it limits its own choice and brings in anticompetitive impacts by such limited choice in the whole process.

As may be seen in chapter 3, that RDSO vendor approval guidelines are of the nature of discouraging potential bidders from participation because unless vendors are prior approved they cannot participate in the bid. A practice seems to exist which disallows a

competent bidder because it is not on the approved list of RDSO; this limits the number of potential suppliers of products to Railways. Such practice as a result restricts competition and enhances the possibilities of formation of a cartel. Similarly rules of Indian Railways Stores department relating to single tender and limited tender enquiry also have impact on competition. The said rules hinder competition by limiting number of suppliers of products.

The characteristic of these rules or principles followed in the process of government / public procurement although seemingly designed for getting best value for money but over time its impact has been anticompetitive.

#### **4.2 Limits the ability of suppliers to compete**

Given the system of procurement by public authorities, there are issues where procurement is sourced to another public enterprise, which directly limits the ability of suppliers to compete. It is generally seen that wherever available public procurement is sourced to another public enterprise. For e.g. Indian Railways procure rails from SAIL, equipments from other PSEs like BHEL. If value of goods procured and the relevant product market is seen, it may appear that entire relevant product market belongs to one enterprise, which is not acquired by its efficiency rather by its status as a PSE and favourable procurement orders being placed with them.

The available rules of procurement such as GF Rule 147 i.e. Purchase of goods directly under rate contract or Rule 144 stating about reserved items are some of the examples that act in two ways to limit competition. Firstly, it limits competition between suppliers inter se by not giving them opportunity to compete and secondly, it limits the choice of procurer as well. As far as reserved items are concerned, in any free market, products must not be reserved to be supplied from specific sources as it will be having distortionary effect on competition. However, an argument that the said rules in the process of procurement result in undermining of substitutability of goods, limiting choices of procurer may be countered by stating that such rules are in the interest of SMEs. In such a situation, such rules amount to a policy barrier created in the process of procurement. SMES may be made competitive by other processes but not by safeguarding their interest and compromising competition in the given sector and the relevant market

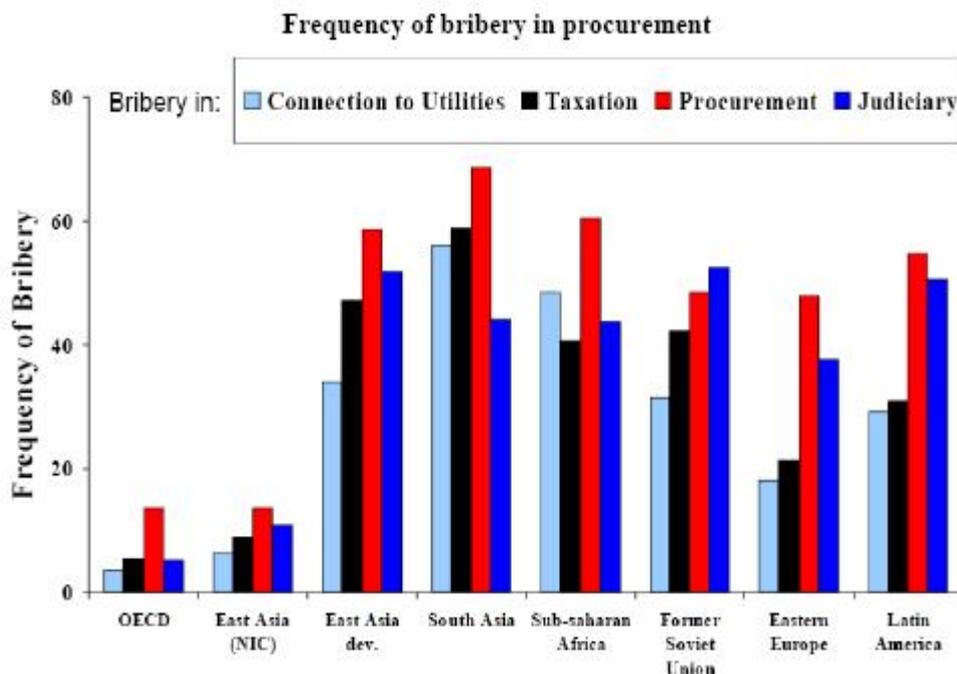
One significant factor to evaluate the degree of competition in case of PSEs is the exercise of buyer power by the PSEs, considering that their demand of products is higher in the relevant market and they have un-fragmented and coordinated system of procurement. In such a situation suppliers would be having no say in price determination, leaving no incentive to compete. If public sector demand is fragmented, and if different public sector bodies act in an un-coordinated fashion, there may not be any significant public sector buyer power, which may lead to more competitiveness amongst the suppliers in the given relevant product segment. It is also seen that public sector procurement decisions are not driven by a desire to maximise profits, which suggest that public sector is less likely to engage in the exercise of buyer power with the

objective of gaining unfair advantage over other buyers of similar goods and services. This aspect of buyer power may depend on a particular procurement case.

It may be seen from Rule 143 of the GFR that it creates a system of commission by enlisting of Indian agents of foreign suppliers. Such agents are paid commissions or they act as middlemen between procurer and supplier. Such a system results in undesirable overhead expenditure and inflates the price of product or services to be procured. International competitive bidding may be an answer to such existing system, which will bring in more competitiveness. Present system limits number of suppliers, thus limiting their ability to compete.

### 4.3 Collusion or corruption having distortionary effect

The scenario of public procurement in India is also subject to corrupt practices by procurement officials. Such practices of bribery are very frequent in almost every part of the world. In one of the World Bank studies, frequency of bribery has been reported in public procurement from 117 countries across the world. The highest frequency is seen in South Asia and the lowest in OECD and East Asian countries. The bar chart below shows the frequency of bribery in public procurement.



*Source:* Kaufmann, World Bank (2006), based on Executive Opinion Survey 2005 of the World Economic Forum covering 117 countries. Question posed to the firm was: In your industry, how commonly firms make undocumented extra payments or bribes connected with permits / utilities / taxation / awarding of public contracts / judiciary?

It may be seen in the bar chart above that apart from procurement there are other instances such as connection to utilities, taxation, and judiciary wherein kick-backs are rampant worldwide. However, for the purpose of the present study the focus is on procurement only.

Generally understood, collusive bidding covers corrupt practices as well as other facets of bid rigging. However, in India the scenario is different, collusive bidding is not defined and it may be taken as an alternate to bid rigging. In the absence of a clear definition of bid rigging, the scope of application of section 3 of the Competition Act, 2002 has been limited.

#### **4.4 Barriers to entry in public procurement in India:**

Restricted entry caused by strict sector regulations is pertinent in every kind of competition case that does not involve a per se offence. As discussed above, there is a tendency among public procurers to restrict participation to chosen big and reputed firms. Often this is done to reduce the cost of evaluating bids or to ensure the stability and quality of supply. However, this tendency could raise high entry barriers for new entrants leading to inefficient outcomes.

Following are the key practices on the demand side in the procurement process that could restrict competition by raising barriers to entry:

##### **4.4.1 Limited/Single Tender Enquiry:**

In India, procurements are carried out through three channels of tender invitation. Open Tender Enquiry (OTE), limited tender Enquiry (LTE) and Single tender Enquiry (STE). LTE is recommended in cases of procurement where pool of vendors have been established. STE is recommended under only exceptional circumstances such as national calamities or other emergencies. The choice between these can significantly impact the participation level in the tender.

Numerous Reports have noted that organizations (unknowingly or purposely) fail to utilize this open channel and tend to depend on LTE. A CVC Report on public procurement points out "*in the process of neglecting OTE, the competition is restricted which in turn results in cartel formation, higher rates and favoritism to select firms*". There are numerous cases where even in case of generic items, prescribed rules and guidelines are not followed and available channel of OTEs is ignored.

##### **4.4.2 List of Registered Vendors:**

It is a common practice in Ministries /Departments where there are safety, expediency and security concerns to maintain a list of short listed suppliers on technical and financial grounds. Such registered suppliers are exclusively eligible for consideration for procurement through LTE. A detailed analysis of this mechanism reveals various flaws that have led to severe barriers to entry for new participants. Often it has been reported that the approving authority has imposed tedious procedure resulting in abnormal delays in securing approval.

Further, often these lists are not updated regularly even if there is a single supplier in the list over a long period of time. Lack of willingness on the part of the procuring authority to update these lists has led to restricting competition.

#### **4.4.3 Bureaucratic Hassles and Complex Procedures:**

Excessively tedious process for participation sometimes poses severe barriers for participation. As noted above, it is common for procurement agencies to keep a list of selected vendors exclusively eligible for LTEs. New firms are dependent on the approving authority within the department concerned for being nominated on the approved vendors list. These firms are required to go through lengthy administrative and procedural requirements. It is often reported that corruption in the public department has made getting approval costly with respect to time and money.

The issues identified and discussed above do suggest that existing rules on public procurement in India have distortionary effect on competition and the relevant market. It must be noted at this stage that competition distortions creep in through other loopholes such as element of kickbacks and high handedness in supplier selection and order creation (procurement decision). Thus overhauling of rules and creation of an efficient system of public procurement is most desirable.

#### **4.5 The Commonwealth Games 2010: A Case Study**

The Commonwealth Games 2010 have been subject to numerous charges of anti-competitive practices in its procurement process. The CAG has estimated the cost of creating venues and city infrastructure as well as the operational expense of hosting the Games at Rs. 12,888 crore. There have been irregularities made by the Organizing Committee (OC) in the procurement of various items for the CWG which include the hiring of treadmills for 45 days for Rs. 9, 75,000 when such machines can be bought for Rs. 7 lakh, hiring of cross trainers for Rs. 8.8 lakh, procurement of air-conditioners and generation of diesel power at Rs. 80 per unit as against a prevailing rate of less than Rs. 8 per unit. There has been subversion of fair procurement practices on the following grounds:

1. Tenders were awarded bypassing usual bidding norms.
2. In many cases there was no written contract, nor was there a tendering process.
3. There was no tendering made for the hiring of vehicles for example.
4. In some cases, the successful bidder was allowed to tamper with the figures post auction.
5. In the construction of flyovers, stadiums, lane strengthening and widening, upgrading street light, power plants, sewage plants, water treatment plants and bus parking lots, bidding norms were bypassed.
6. Works have been awarded at higher rates despite which there have been poor site management, delays and quality compromises.
7. In the bid of L1, rates of some items were overwritten in the price bid after opening in order to avail the difference between the next higher quoted amounts without changing the overall status.

There has been usage of sub-standard material, rigging of bids, gold plating and sanctioning of projects that were not needed at all and submission of phony bids. According to the CVC report, there has been scanning of sixteen Games projects and

there has been discovery of competition issues with one or more of the scenarios manifesting themselves:

- a) Either open tender has not been floated.
- b) Either bidders have colluded among themselves or both bidders and procurers have colluded.

The Common Wealth Games Case shows, how unguarded procurement leads to bad quality works and loss to exchequer. A competitive procurement process, guided by rules and legislative framework not only provides good quality work but also gives value for money. Thus it may be inferred as learning from this case that procurement process whether distorted by corruption or otherwise, they necessarily have diminishing returns for money spent and competition brings increasing returns for money spent in the procurement process.

## Chapter 5: Review of Regulatory framework for public procurement in India

The Constitution of India does not contain any direct provision dealing with public procurement. However article No.299 stipulates that all contracts made in the exercise of executive power of the union or state shall be supposed to be made by the President or by the Governor This article does not deal with as the case may be. This article does not deal with the issue of how the power to enter into contract has to be exercised but the Judiciary has laid down rules regarding this.

There is no national legislation on public procurement in India. Certain States like Tamil Nadu and Karnataka have framed legislations on public procurement. There is no entry in the seventh schedule directly dealing with the public procurement: There are certain studies which mention that as the subject is not covered by any of the lists in the seventh schedule, it has to come within the residuary power of the union. But this view does not seem to be correct .It seems that the subject is covered under entries 42 and 7 of the concurrent list which mention 'Acquisition and Requisitioning of property' and 'Contracts' respectively. The Karnataka and Tamil Nadu Legislatures seem to have exercised the concurrent powers in enacting their legislations.

Public procurement in India is a major activity within the Government, not merely for meeting its day today needs but also for underpinning various services that are expected from the government e.g., infrastructure ,national defence and security, utilities, economic development ,employment generation social service and so on. Thus, apart from ministries and departments vast amount of procurements are undertaken by the PSEs and other subordinate organizations of the government at the level of both Central and State Governments. In addition to this horizontal spread, vertically procurement is undertaken at all levels of the hierarchy. Public Procurement is thus all pervasive function across the government machinery.

Public procurement has grown phenomenally over the years-in volume, scale, variety and complexity. No definitive estimates of total size of India's public procurement are available at any place; an OECD quick estimate puts the figure for public procurement in India as 30 per cent of India's GDP. The Competition Commission of India had estimated in a paper that annual public procurement in India would be of the order of Rs. 8 lac crore while a rough estimate of direct procurement is between Rs. 2.5 lac crore to Rs.3 lac crore.. Thus total procurement figure for India is pegged at around Rs.11 lac crore per year.

Though procurement is a major and widespread activity in government, it is noted that the regulatory and institutional framework for public procurement is in several respects weak and incomplete, so that it does not provide a sufficient basis for ensuring its

essential qualities: transparency, accountability, efficiency, economy competition and professionalism.

The OECD has drawn up a matrix of items that enables a quick assessment of the state of procurement practices in a country. It suggests that India may be lagging behind in many of the items contained in the matrix such as a legislative framework including subordinate legislation, model documents, general conditions of contract, procedures for contracting, multiyear planning, integration with budget, timely procurement payments, conflict of interest, quality control, performance evaluation, contract administration and dispute resolution & appeals etc.

## **5.1 Key Issues in Regulatory and Legal framework**

### **5.1.1 Multiple Guidelines**

There is no single central body that is dedicatedly responsible for defining procurement policies and procedures. General Financial Rules (GFR) 2005 is a voluminous document which contains 293 rules, 16 appendices and a number of forms for different purposes. In addition, a set of guidelines is issued by Ministry of Finance (Manual on Policy and procedures on Purchase of Goods). The CVC has also issued numerous guidelines and instructions dealing with model procurement practices.

This has led to a multiplicity of rules, guidelines, procedures, directives, model tender /contract documents and orders issued by various departments. To add to the problem not all these documents and guidelines are available at a single source. This may firstly complicate and confuse procurement officials about their roles and duties and secondly leave enough loopholes and gaps for manipulation. Further, the rules and guidelines are not backed by law and are thus not enforceable in a court of law.

### **5.1.2 Absence of Standard Procedures, Contracts and Tender documents**

Absence of a Central/State Act specific to Public Procurement allows Public Departments to tweak the guidelines and principles intentionally or unintentionally to benefit stakes. According to an estimate, more than 150 contract formats are being used by the public sector. Even for similar work different agencies use different tender documents in terms of prequalification criteria, process of selection, settlement of dispute, financial terms and conditions etc. Such variations in tender documents and contracts lead to confusion and complications among bidders. Many Countries like Germany and USA have devised uniform guidelines and procedures.

### **5.1.3 Weakness of present monitoring mechanism**

CAG audits the expenditures (Tendering Process). However; these audits are carried out well after the damage is done. External audits fail in their effectiveness as the findings often do not attract the requisite attention of the Parliamentary Accounts Committee. Although, CAG has powers to demand Action Taken Report (ATR), there is no clause in the CAG's Act that makes it mandatory for the concerned departments/ ministries to revert back with action taken reports in a time bound manner. Such loopholes are exploited resulting in delayed or no responses at all.

#### **5.1.4 Absence of a Transparent Grievance Reprisal Mechanism**

In case of a grievance against an award of a contract, complaint can be lodged with the procuring agency. However, it leaves very little scope for transparency. In case where the procuring officials have participated in the manipulation of the outcome, chances are very low that the aggrieved bidder will get a fair hearing. If not satisfied with the decision of the procuring body, the aggrieved bidder can appeal in the court. Given the high number of pending cases in the Indian Courts, any legal remedy could only be found after a long delay which is costly for small firms since long delays may make remedy insignificant with respect to the tender concerned.

#### **5.1.5 The Competition Act and its applicability on the demand side**

Often the incidences of anticompetitive conduct are facilitated by corrupt practices in the public departments. This is done by raising unnecessary barriers to participation, rejecting bids of competitors on unfair grounds or by manipulating tender documents /bids post submission to suit a chosen firm.

In the case of India, the applicability of Competition Act, 2002 to public procurement is an interesting area. Sections 3 and 4 can be applied in the case of suppliers of goods, if they resort to anti-competitive practices and abuse of dominant position. However, it has to be seen whether a procuring agency can be brought under the ambit of the Act? Two Preliminary orders by the Competition Commission clearly indicate that it could not be done under section 3 of the Act<sup>17</sup>. Under the relevant provisions of the Act, when a firm indulges in anti- competitive conduct with the public officials, the Competition Commission lacks the enforcement powers / provisions against public officials involved<sup>18</sup>.

#### **5.1.6 The Way Forward--Need for a Public Procurement Law**

There is no Public Procurement Policy or Public Procurement law in India. The States of Tamil Nadu and Karnataka have enacted simplistic versions of transparency laws for public procurement but these may be regarded as rather rudimentary and lacking in teeth. There is no separate department or division in Central Government to which the public procurement authorities can refer any matter for guidance. At present many such references are being made to the CVC by the procuring authorities mostly as a measure of abundant precaution from the vigilance angle. The CVC sometimes issues clarifications and circulars even though such work should normally be done by the Government. Though the Department of Expenditure is the repository of the GFR, it is saddled with more urgent and pressing issues, as a result public procurement does not get the priority it deserves under the present arrangement.

A review of procurement systems and procedures being followed across ministries and organizations has revealed that some of the practices are at odd with the GFR. However

---

<sup>17</sup> See Case No. 10/2010, *M/s. Pankaj Gas Cylinders Ltd. v. Indian Oil Corporation Ltd.*, and Case No. 20/2011, *Pawan Kumar Agarwal v. Rashtriya Ispat Nigam Ltd.*, Competition Commission of India.

<sup>18</sup> Case No. 15/2010, *Jupiter Gaming Solutions Pvt. Ltd. v. Government of Goa and others*, Competition Commission of India.

such violations do not attract penal action since GFR is not backed by law .GFR cannot be a substitute for a comprehensive law in this area.

Accordingly, basic reform of the public procurement system is required both in the Legal and Institutional framework governing public procurement in India as well as some of the practices being followed by the procuring departments. There is a need to enunciate a Public Procurement policy that would set out in clear terms the Government's approach to this important activity. The Policy should be backed by a public procurement law that would give an enforceable form to key provisions of the policy including penal action against violations by the procurers or the suppliers.

To provide effective leadership in public procurement and bring about the reforms, setting up of an Institutional framework preferably of a dedicated department within the Ministry of Finance is recommended. This Department will not have an operational responsibility for direct procurement; it would act as a repository of the law, rules and policy on public procurement and monitor compliance thereof. It would institute best practices, professionalise the public procurement function, arrange for capacity building, create and maintain the overarching public procurement portal and maintain management information systems and statistics pertaining to public procurement.

## Chapter: 6 Conclusions, Recommendations and Agenda for Competition Policy advocacy

### 6.1 Conclusions:

In the previous chapters an identification of supposedly anticompetitive rules, regulations etc. has been done along with an evidence based analysis to figure out anticompetitive character of those rules, regulations etc. It is worthwhile to point out that public authorities might be required at times to act in a way which appears to be anticompetitive but for reasons of governance. Example may be taken from PSEs or Government Companies, such companies or enterprises may enter into long term exclusive agreements denying market access to a number of enterprises, it may also be found that price of procurement is often higher than price in a competitive market. At times for securing employment to citizens or to revive not so well performing PSEs, Government might be required to take steps, which appear to be anticompetitive in their approach and impact, yet competition authority may not be in a position to take any remedial measures .

Such situations should not exist in the market once an effective competition regime is in place. Considering the area of public procurement, it gives a tough call to nascent competition authority to take remedial actions for anticompetitive outcomes of public procurements in India. What might be expected at this stage is a rigorous competition advocacy within an effective and implementable competition policy framework. A well laid down advocacy agenda is very crucial for creating awareness about the risks to competition in procurement procedures and at the same time developing appreciation of the benefits of inculcating competition in public procurement processes.

As part of the conclusion, after analysing the entire gamut of procurement and studying the framework of Competition Act, 2002 and other relevant legislations pertaining to public procurement in India, it may be stated that the Competition Act, 2002 does not give a *mandamus* type of remedial authority to the Competition Commission of India. Thus at the most Competition Commission can go for vigorous advocacy and convince States or Central Government to review the legislations causing anticompetitive impact on the market. The following might be very effective part of competition advocacy in public procurement cases as well:

- (i) persuading public authorities not to adopt unnecessarily anticompetitive measures and help them to clearly delineate the boundaries of economic regulation.
- (ii) increasing awareness about the benefits of competition, and of the role of competition law and policy in promoting and protecting welfare, enhancing competition among PSEs, Government Companies, and Departments.

- (iii) wherever possible, competition awareness must reach among economic agents, public authorities, the judicial system and the public at large.

Another issue that may be highlighted here is the element of corruption in public procurement. Generally understood corruption and anticompetitive effects in public procurement are considered separate and dovetailing both into one in order to streamline procurement and rid it off anticompetitive element is not considered a feasible course of action. However in one of the desenting orders of the Competition Commission of India i.e. in Case No. 15/2010 – *Jupiter Gaming Solutions Pvt. Ltd. v. Government of Goa and others*, it has been stated:

“Public procurement is a key economic activity of governments, accounting for a large proportion of Gross Domestic Product worldwide. Effective public procurement avoids mismanagement and waste of public funds. Reducing collusion in public procurement requires strict enforcement of competition laws. It is a known fact that corruption is rampant in Public Procurement. According to the OECD corruption arises in procurement when the agent of the procurer in charge of the procurement is influenced to design the procurement process or alter the outcome of the process in order to favour a particular firm in exchange for bribes or other rewards. Public procurement policy therefore has to be particularly careful to avoid instances where corruption may occur. Corruption of public officials is not just a regrettable thing as such, but it has an impact on the efficient allocation of procurement. By definition, corruption in procurement involves an allocation of contracts which is not the same as that that would have been obtained through the competitive process. Corruption either leads to the allocation of the contract to a firm which was not the bidder with the lowest price but rather to the firm who has offered the bribe. In this sense, corruption in public procurement implies a distortion of competition. Thus the fights against corruption and anticompetitive practices are highly complementary policies. In practice, therefore, there are trade-offs between enhancing competition and the desire to minimize collusion.”

If this view is accepted then Competition Commission of India may dovetail corruption and anticompetitive aspects involved in public procurement and remedy the situation through the processes and mechanisms of the Competition Act, 2002.

## **6.2 Principles for designing Tender Documents:**

There are many steps that procurement agencies can take to promote more effective competition in public procurement and reduce the risk of bid rigging as regards designing of tenders. Some of these are as follows:<sup>19</sup>

---

<sup>19</sup> Refer OECD: Designing tenders to reduce Bid-rigging. Available at: <http://www.oecd.org/dataoecd/36/40/42594504.pdf>

Also refer OECD: Guidelines for fighting Bid-rigging in Public Procurement. Available at: <http://www.oecd.org/dataoecd/27/19/42851044.pdf>

1. The procuring agencies should be well-informed before designing tenders. Collecting information on the range of products and/or services available in the market that would suit the requirements of the purchaser as well as information on the potential suppliers of these products is the best way for procurement officials to design the procurement process to achieve the best “value for money”. Towards this end, the following steps may be taken:
  - ✚ Collection of information on potential suppliers, their products, their prices and their costs and if possible making a comparison of prices offered in B2B procurement.
  - ✚ Collection of information about recent price changes. The procuring entity should be aware of prices in neighbouring geographic areas and about prices of possible alternative products.
  - ✚ Collection of information about past tenders for the same or similar products.
  - ✚ Coordinating with other public sector procurers and clients who have recently purchased similar products or services to improve its understanding of the market and its participants.
  
2. The Tender process should be designed to maximise the potential participation of genuinely competing bidders. Effective competition can be enhanced if a sufficient number of credible bidders are able to respond to the invitation to tender and have an incentive to compete for the contract.
  - ✚ For example, participation in the tender can be facilitated if procurement officials reduce the costs of bidding, establish participation requirements that do not unreasonably limit competition and devising ways of incentivising smaller firms to participate even if they cannot bid for the entire contract.
  - ✚ It is also considered necessary to avoid unnecessary restrictions that may reduce the number of qualified bidders, specifying minimum requirements that are proportional to the size and content of the procurement contract.
  - ✚ Similarly, it is important to not specify minimum requirements that create an obstacle to participation, such as controls on the size, composition, or nature of firms that may submit a bid.
  - ✚ It must also be kept in mind that requiring large monetary guarantees from bidders as a condition for bidding may prevent otherwise qualified small bidders from entering the tender process. Care should be taken to ensure that amounts set are only so high as to achieve the desired goal of requiring a guarantee.
  - ✚ Constraints on foreign participation in procurement should be reduced whenever possible.
  - ✚ It is significant to avoid a very long period of time between qualification and award, as this may facilitate collusion.
  - ✚ Reducing the preparation costs of the bid is also considerably important. This can be accomplished in a number of ways:
    - By streamlining tendering procedures across time and products (e.g. using the same application forms, asking for the same type of information, etc.).
    - By keeping official lists of approved contractors or certification by official certification bodies.
    - By allowing adequate time for firms to prepare and submit a bid. For example, publishing details of pipeline projects well in advance using trade and professional journals, websites or magazines.

- By using an electronic bidding system, if available. Whenever possible, allowing bids on certain lots or objects within the contract, or on combinations thereof, rather than bids on the whole contract only. For example, in larger contracts the procurement agency should look for areas in the tender that would be attractive and appropriate for small and medium sized enterprises.
3. Definition of requirements should be clear to avoid predictability: Drafting the specifications and the terms of reference (TOR) is a stage of the public procurement cycle which is vulnerable to bias, fraud and corruption. Specifications/TOR should be designed in a way to avoid bias and should be clear and comprehensive but not discriminatory. They should, as a general rule, focus on functional performance, namely on what is to be achieved rather than how it is to be done. This will encourage innovative solutions and value for money. The clearer the requirements, the easier it will be for potential suppliers to understand them, and the more confidence they will have when preparing and submitting bids. Clarity should not be confused with predictability. More predictable procurement schedules and unchanging quantities sold or bought can facilitate collusion. On the other hand, higher value and less frequent procurement opportunities increase the bidders incentives to compete. The specifications should be designed allowing for substitute products or in terms of functional performance and requirements whenever possible. Alternative or innovative sources of supply make collusive practices more difficult.
  4. Designing the tender process to effectively reduce communication among bidders: When designing the tender process, procurement officials should be aware of the various factors that can facilitate collusion. Transparency requirements are indispensable for a sound procurement procedure to aid in the fight against corruption. They should be complied with in a balanced manner, in order not to facilitate collusion by disseminating information beyond legal requirements. Open tenders enable communication and signalling between bidders. A requirement that bids must be submitted in person provides an opportunity for last minute communication and deal-making among firms. This could be prevented, for example, by using electronic bidding. The procuring agency must carefully consider what information is disclosed to bidders at the time of the public bid opening. When publishing the results of a tender, the procuring agency must carefully consider which information is published and avoid disclosing competitively sensitive information as this can facilitate the formation of bid-rigging schemes, going forward.
  5. The procuring entity must carefully choose its criteria for evaluating and awarding the tender: All selection criteria affect the intensity and effectiveness of competition in the tender process. It is therefore important to ensure that qualitative selection and awarding criteria are chosen in such a way that credible bidders, including small and medium enterprises, are not deterred unnecessarily. Whenever evaluating bidders on criteria other than price (e.g., product quality, post-sale services, etc.) such criteria need to be described and weighted adequately in advance in order to avoid post-award challenges. When properly used, such criteria can reward innovation and cost-cutting measures, along with promoting competitive pricing. The extent to which the weighting criteria are disclosed in advance of the tender closing can affect the ability of the bidders to coordinate their bid.

### 6.3 Recommendations:

1. Firstly, basic reform of the public procurement system is required both in the Legal and Institutional framework governing public procurement in India as well as some of the practices being followed by the procuring departments. There is a need to enunciate a Public Procurement policy that would set out in clear terms the Government's approach to this important activity. The Policy should be backed by a public procurement law that would give an enforceable form to key provisions of the policy including penal action against violations by the procurers or the suppliers.
2. To provide effective leadership in public procurement and bring about the reforms, setting up of an Institutional framework preferably of a dedicated department within the Ministry of Finance is recommended. This Department will not have an operational responsibility for direct procurement; it would act as a repository of the law, rules and policy on public procurement and monitor compliance thereof. It would institute best practices, professionalise the public procurement function, arrange for capacity building, create and maintain the overarching public procurement portal and maintain management information systems and statistics pertaining to public procurement.
3. Recognizing the need for standardisation including in the procedures, tender documents and general conditions of contract, the specifications set out in the tender documents should be clear, generic as far as possible and provide no advantage to any one party. The procurement process should provide level playing field to all players. Although the need for standardization of tender documents is recommended, the documents thus standardized should have an ample scope to consider suitable modifications to take care of the special needs of the ministry/department concerned.

With a view to streamlining the procedure and to detect deficiencies in the tender documents submitted by the bidders, it is recommended that a check list of all documents required in proper sequence should be drawn out for convenience of comparison and for ascertaining that all the documents have been received.

4. With a view to professionalizing the function of Public Procurement, it is important to institute an elaborate system for capacity building and training in all aspects of public procurement. The training would not be confined to mere knowledge of extant rules and procedures applied mechanically but also to basic principles and concepts of public procurement, writing of specifications, qualification and evaluation criteria and contract terms etc. The government should seek co-operation of professional training institutes in capacity building of procurement officials.
5. The fundamental principles of effective procurement require that any proposed procurement should be given sufficient publicity, commensurate with its size and nature to attract maximum participation and competition. The laws, rules, and subordinate instructions mandate appropriate publicity of the proposed procurement in the public domain through various means such as the media, website and trade journals.

6. Competitive bidding would be the norm for procurement unless permitted and justified in special cases. Evaluation criteria should be clearly spelt out in the tender documents: evaluation should be carried out only on the basis of the declared criteria. Public opening should be mandatory. The result of the tendering process should be put out in the public domain.

7. Using IT can be one of the most effective policy tools in enhancing the level of competition in public procurement. Proper adoption of an e-procurement system can expand transparency in the procurement market and also contribute to the prevention of corruption. Towards this, Department of Expenditure, Ministry of Finance, Govt. of India has taken significant steps by issuing instructions to all Govt. Ministries/ Departments/Organizations to switch over to e-procurement regime. The Korean example which involves third parties to monitor on line contract management would help illustrate better.

The nationwide integrated Korea Online E-Procurement System (KONEPS) enables online processing of all procurement from purchase request to payment. Through the digitalised system, customer organisations and companies are involved in scrutinising the way public funds are managed in the procurement process. The System covers all stages of the procurement process, from the pre-bidding to contract management and payment. For example, the Public Procurement Service releases specifications of procurement items on the KONEPS prior to the bid notice in order to encourage interested suppliers to submit suggestions.

The Korean experience illustrates how new technologies can support the involvement of a third party - an insurance company - that provides a guarantee for the contract between the administration and the bidder. The successful bidder and the contracting agency establish an e-contract through KONEPS, and in the process, a surety insurance company, as a third party, shares part of that information regarding the contract. In practice, the contracting official receives both the contract documents provided by the contractor and the written guarantee for the contract provided by the surety insurance company, and replies to the guarantee. The contracting officer drafts the final version of the contract after clarification and sends it to the contractor and the end-user organisations. Another feature of the information system is that it helps monitor the payment and prevent risks to integrity during payment. The contractor submits a payment request and receives payment upon receipt, which is sent by an inspector from an end-user organisation. Since the e-payment is connected to the Finance Settlement, the end-user organisation, the contractor and the bank share information in the flow of payment. Payment is automatically completed on line within two working hours upon payment request to avoid overdue payment.<sup>20</sup>

8. Provision of Certificates of Independent Bid Determination (CIBD), which require bidders to certify that they have arrived at their tender price absolutely independent of other bidders. CIBDs operate as both a reminder of the

---

<sup>20</sup> South Korea, response to the OECD Questionnaire.

relevant legislation and as a commitment by the bidder that these rules have been complied with, and are of particular value in situations where tender participants may be less aware of national legislation prohibiting corruption and collusion. Prosecution of CIBD violations can also be a possibility where absence of proof of an agreement makes it impossible to charge an antitrust violation.

9. A stronger antitrust and anti-competition agency with strong coordination with other law enforcement agencies will contribute to reducing the corruption in public procurements. Systematic exchange of information between the antitrust bodies and anti-corruption bureaus is highly desirable in this regard. Drive against corruption and steps towards enforcement to eliminate anti-competitive practices are complementary in nature since improvement in the procedure by which the tender documents are designed and the bidders are ultimately selected will not only reduce corruption but also enhance competition in the procurement market.
10. The risks for competition in public procurement can be reduced by careful consideration of the various auction features and their impact on the likelihood of collusion. Designing auction and procurement tenders with collusion in mind may significantly contribute to the fight against anticompetitive behavior, as it allows the creation of an environment where the bidders' ability and incentives to reach collusive arrangements are significantly reduced, if not eliminated.
11. Reducing collusion in public procurement requires strict enforcement of competition laws and the education of public procurement agencies at all levels of government to help them design efficient procurement processes and detect collusion.
12. Introduction of a Debriefing Procedure would be helpful. Unsuccessful bidders have a right to know why they were not successful, if that is not readily apparent. On request, say, within 7 days of award notification - the purchaser should provide a debriefing, essentially to help the bidder understand the evaluation process and prepare more responsive bids in future. Once the procedure is in place for some time, bidder confidence in the system will go up.
13. The blacklisting rules for corrupt firms should be revamped and strictly enforced. The supplier firms should be required to adhere to a "code of conduct". Any infringement should result in sanctions. The blacklisting rules need improvements permitting exclusion from public contracts for a period, or permanently, depending on the seriousness of the offence.
14. Research Design and Standards Organization (RDSO) is the sole R&D organization of Indian Railways and functions as the technical advisor to Railway Board, zonal railways and RPU's. One of the key roles of RDSO is quality assurance. It involves vendor approval and purchase inspection of these various items. From the stakeholder discussion and questionnaire survey the study has gained that RDSO plays a prominent role in restricting entrants into

the railways procurement. Concerns like bureaucratic hassles in RDSO have in many ways assist anti-competitive practices. Complaints such as long approval time periods for any new technology have been reported by some of the stakeholders. Moreover, stakeholders have claimed that over-specification and tedious procedure to get approvals from RDSO has kept away many big vendors. It is important for the policy makers to reduce 'unnecessary' entry barriers as this can directly result in increased competition and reduction in the power of the cartels to control the market.

15. It appears that for ensuring competition, we are mainly concentrating on the downstream activities i.e. tender conditions, bid documents, eligibility criteria, bid evaluation, contract awarding etc. It would be worthwhile to point out here that equal attention is also required to be paid to upstream activities like determination of technology, conceptual design, specification, vendor base identification etc. Unless that is done, it would be extremely difficult to control lack of competition only by regulating/ reforming the downstream activities.
16. There is a need to make the procurement function truly cross functional and a part of an end-end supply chain.
17. Separate and comprehensive procurement rules for goods, services and works should be laid down.
18. There should be provisions for institutionalising 'Integrity Pacts' or any other enforceable integrity conditions as a legally binding ethical code of conduct to govern the procurement cycle. This needs to be buttressed by provisions penalising violations of the Pact's terms and conditions.

#### **6.4 Advocacy measures:**

As highlighted above, government procurement is riddled with two vices one inefficient rules, regulations etc. and second corruption. There has been cumulative effect on competition and both the issues do not get remedied under the Competition Act, 2002. A very limited remedy under section 3 and 4 of the Competition Act, 2002 is available in cases of anticompetitive conduct of parties in procurement cases. Thus, what may be suggested is strong advocacy measures to prune rules and regulations which are carrying discretionary elements and therefore lead to anti -competitive outcomes.

A broad range of target areas can be identified i.e. education of public officials; of businessmen and market players; of the media; and of the wider community to sensitize and aware them as pernicious effects on anticompetitive conduct in government procurement. Effective advocacy can promote competition culture in State practices and generate public support for enforcement efforts. More generally, enforcement agencies such as Competition Commission of India should identify and advocate for the removal of any public procurement rules or procedures that facilitate or foster collusion or corruption. Business also has a role in this process, in

terms of the education of its personnel and the development of internal compliance mechanisms.

Procuring agencies can organise regular bid rigging educational programs for procurement officials. They can also conduct ad hoc seminars and training courses. These awareness enhancing efforts may include imparting knowledge about collusion and bid rigging, the forms it can take and how to detect it. These outreach programs may prove extremely useful as they will help competition and public procurement officials to develop closer working relationships, educate procurement officials about what they should look for in order to detect bid rigging, such programmes can provide training to procurement officials to collect evidence that can be used to prosecute better and more effectively bid rigging conduct, they will help educate public procurement officials and government investigators about the cost of bid rigging on the government and ultimately on the taxpayers; and, finally, they warn procurement officials not to participate in bid rigging and other illegal conduct which undermines competition in procurement tenders.

To sum up following measures need to be applied to weed out anticompetitive issues present in the government procurements in India.

- (1) Collecting evidence of anticompetitive impact of Acts, rules, regulation etc. which form the basis of public procurement. It may be seen in the present study that a number of rules have been identified with their consequential anticompetitive impacts.
- (2) Corruption issues vitiating government procurement and bringing in inefficiency need to be examined by the Competition commission of India for its anticompetitive effect and corruption remedy against corrupt officials and parties be left on the relevant law governing corruption.
- (3) Effective advocacy for suggesting and requiring changes in Acts, rules or regulations relating to government procurement having anti-competitive effect.

It may be suggested from the aforesaid details that in case of public procurement in India, there are not significant barriers to entry in the relevant markets, except in cases of high sunk cost. However, some of the prescriptions by rules do create entry barrier for new entrants, such as rules relating to empanelment of suppliers or rules relating to pre tender qualifications etc. These definitely have negative effects on competition.

Competition neutrality is recommended for operation of state-owned enterprises, because they have significant role in public procurement. The role played by PSEs is so significant that their preferential treatment to one another not only destroys competition in the given product segment but also causes consumer harm.

It may be appreciated that international best practices are one of the most important sources to bring in efficiency in public procurement in India. European Bank of Reconstruction and Development (EBRD), World Bank and other international institutions have insisted on eliminating bribery in public procurement by giving clear

mandates on disbursement of funds and funds may be withheld, if instances of bribery are found.

Another system in public procurement which might be suggested to be followed is the Swiss Challenge method of award of contract, in which the proposer has the first right of refusal after a bidding process; such a system is not followed in mature or developed jurisdictions wherein demand supply conditions are ascertainable with efficient system of bidding. Jurisdictions which follow swiss challenge system require a public authority which has received an unsolicited bid for a public project (such as a port, road or railway) or services to publish the bid and invite third parties to match or exceed it. If we see the 3G auctions/bidding, which have been a far better system of award of contractual rights by the public authority, it appears to be an upgraded and technologically dovetailed bidding system.

A number of States in India such as Andhra Pradesh, Maharashtra, Rajasthan, Madhya Pradesh, Chhattisgarh, Gujarat, Uttarakhand and Punjab etc. are going the Swiss way for awarding contracts. Recently the Supreme Court has also approved the swiss challenge system, while overturning Bombay High Court order which struck down swiss challenge system. Applying the Swiss Challenge method, the Maharashtra Housing and Area Development Authority (MHADA) had awarded a contract to Ravi Development for development of government land at Mira Road, a deal that had run into controversy and corruption angle was also highlighted. The Bombay High Court quashed the award to Ravi Development, the original proposers of the project, faulting the Swiss Challenge method. In appeal the Supreme Court has stated that the Swiss Challenge method was a perfectly valid way of awarding contracts, especially when the bidders were told beforehand and had consented to it. The Court has noted, "Swiss Challenge method was being applied by the state government only on a pilot basis. The method is transparent in as much as all the parties were well aware of 'the right of first refusal' accorded to the 'originator of proposal'.

The aforesaid suggestions are based on international best practices and many jurisdictions in the world are applying systems akin to the aforementioned processes. It must be noted that many issues talked about in the process of public procurement in India such as corruption or inefficiently designed rules of procurement or transparency issues are not only an Indian phenomenon and many countries in the world are facing similar circumstances. Such countries have followed procurement systems as discussed above along with some delicate interconnect with competition law and other laws to weed out inefficient practices in award of government contract or in the processes of public procurement.

## REFERENCES

1. Public Procurement Guidelines- Competitive Process. Available at: [www.etenders.gov.ie](http://www.etenders.gov.ie),
2. Manual on Policies and Procedures for Purchase of Goods. Published by Department of Expenditure, Ministry of Finance, Government of India. Available at <http://www.persmin.nic.in>
3. Enhancing Integrity in Public Procurement: A Checklist -OECD 2008. Available at: <http://www.oecd.org/dataoecd/54/41/41760991.pdf>
4. Regulation in Public Procurements and Competition Issues (India). Published by Competition Commission of India (CCI) and The Energy and Resource Institute (TERI) 14<sup>th</sup> of September, 2010, Cairo. Available at: [www.cci.gov.in/menu/backgNote091210.pdf](http://www.cci.gov.in/menu/backgNote091210.pdf)
5. Public Procurement: Achieving Best Value through Competition -The Public Procurement Capacity Development Guide (UNDP 2010). Available at: [www.unpcdc.org](http://www.unpcdc.org).
6. DGS&D Manual (Effective from 1<sup>st</sup> October 1999). Published by Directorate General of Supplies & Disposals, New Delhi. Available at: [dgsnd@dgsnd.gov.in](mailto:dgsnd@dgsnd.gov.in)
7. Indian Railways Code for Stores department, (Revised Edition). (Embodying all advance correction slips up to No. 32 dated 06-02-2009).Published by Ministry of Railways. Available at: [http:// www.indianrailways.gov.in/railwayboard/uploads/codesmanual/StoreDept-](http://www.indianrailways.gov.in/railwayboard/uploads/codesmanual/StoreDept-)
8. OECD-Public Procurement: The Role of Competition Authorities in promoting Competition. Series Roundtables on Competition Policy, No. 71, OECD, Paris. The full set of material from this roundtable discussion is also available at: <http://www.oecd.org/dataoecd/25/48/39891049.pdf> .
9. Fighting Cartels in Public Procurement—Policy Brief-OECD 2008. Available at: [www.oecd.org/](http://www.oecd.org/) or contact [dafcomp.contact@oecd.org](mailto:dafcomp.contact@oecd.org).
10. Competition Assessment Toolkit -Volume I: Principles - Version 2.0 –OECD. Available at: <http://www.oecd.org>
11. Competition Assessment Toolkit—Volume II: Guidance- Version 2.0 –OECD. Available at: <http://www.oecd.org>.
12. Competition issues in regulated Industries: Case of Indian Transport Sector-Railways and Ports-- Final Report -Prepared for the Competition Commission of India March 2009 -The Energy and Resources Institute (TERI). Available at: [www.cci.gov.in/menu/backgNote091210.pdf](http://www.cci.gov.in/menu/backgNote091210.pdf)

13. Verma Sandeep, 2007, 'Electronic Government Procurement in India: A Framework Analysis of Access to knowledge and Access to Opportunity.'
14. Favley Rod, Chima, Morrissey and Zgouvi Eviou, 'Competition Policy and Public Procurement in Developing Countries,' Centre for Research in Economic Development and Trade, University of Nottingham.
15. Anti-corruption policies in Asia and the Pacific: Thematic review on provisions and practices to curb corruption in public procurement –Self-assessment report India. Available at: <http://www.oecd.org/daf/asiacom/stocktaking.htm#trpp>.
16. 'Detecting Bid Rigging in Public Procurement: Helping Governments Achieve the Best Value for Money', OECD 2008. Available at: <http://www.oecd.org/dataoecd/36/38/42594486.pdf>
17. Mukhopadhyay Bappaditya, 2010, 'Evaluating Public Procurement.' Available at: <http://rmi.sagepub.com/content/3/1/21.abstract>
18. The Right to Information Act, 2005 - More details may be seen at <http://www.persmin.nic.in> and [www.pariivartan.com/rti](http://www.pariivartan.com/rti).
19. The Competition Act, 2002 -No. 12 of 2003, as amended by The Competition Amendment) Act, 2007. Available at: [www.cci.gov.in/images/media/competition act/act2002.pdf](http://www.cci.gov.in/images/media/competition_act/act2002.pdf)
20. 'Collusion and Corruption in Public Procurement' –OECD Round Tables-2010. Available at: <http://www.oecd.org/dataoecd/35/16/46235399.pdf>
21. OECD Procurement Tool box. Available at: [http://www.oecd.org/document/10/0,3746,en\\_21571361\\_44258691\\_44879818\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/10/0,3746,en_21571361_44258691_44879818_1_1_1_1,00.html)
22. Delegation of Financial Powers Rules (DFPR), 1978, framed by Department of Expenditure, Ministry of Finance, Government of India. Available at <http://www.persmin.nic.in>.
23. The General Financial Rules (GFR) 2005, framed by Department of Expenditure, Ministry of Finance, Government of India. Available at <http://www.persmin.nic.in>
24. OECD: Guidelines for fighting Bid-rigging in Public Procurement. Available at: <http://www.oecd.org/dataoecd/27/19/42851044.pdf>
25. OECD: Designing Tenders to reduce Bid-rigging. Available at: <http://www.oecd.org/dataoecd/36/40/42594504.pdf>

26. Anderson Robert, Kovacic William and Muller Anna, 2010, 'Ensuring Integrity and Competition in Public procurement markets: a dual challenge for good governance.