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# REGULATIONS ON BID RIGGING IN JAPAN, THE UNITED STATES AND EUROPE

Naoaki Okatani†

*Abstract:* This article provides a comparative perspective on bid rigging in Japan, the United States and Europe. It emphasizes the differences in both institutional structure as well as policy and business culture in the three jurisdictions, particularly in terms of antitrust and criminal law enforcement. It notes the greater tolerance of bid rigging in Japan in the case of construction contracts for public works.

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## I. INTRODUCTION

In Japan, the procedures used for government procurement and work contracts are set forth in article 29-3, article 29-5, and article 29-6 of the Accounts Law.<sup>1</sup> This law requires the determination of the contracting parties at the conclusion of the bidding process. (In the case of local public

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<sup>1</sup> Kaikei hō (Accounts Law), arts. 29-3, 29-5, 29-6, Law No. 35 of 1947 [hereinafter Accounts Law].

authorities, article 234 of the Local Autonomy Law<sup>2</sup> contains a similar provision.) Bid rigging is a practice conducted among bidders during the bidding process for public works contracts and other projects offered by the government and municipal offices. Bidders collude and decide which companies should get public works orders and the expected contract price. Each bidder then bids in such a manner that the pre-determined contract winner and contract price become, respectively, the successful bidder and the successful bid price. There are two methods of bid rigging. In the first method, a winning bid is determined for each contract. In the second method, construction firms take turns to become successful bidders according to certain rules.

Today in Japan, corruption cases involving bid rigging by construction firms are known as the "general contractors scandal," and are drawing widespread attention as they spotlight graft and adhesion among politicians, business and bureaucrats. On March 6, 1993, Tokyo prosecutors arrested Shin Kanemaru,<sup>3</sup> former vice president of the Liberal Democratic Party, on charges of tax evasion. As a result of this arrest, the prosecutors discovered that several general contractors had doled out under-the-table political donations to Kanemaru. The special investigation squad of the Tokyo District Public Prosecutor's Office moved in earnest to probe into the "general contractors scandal." Since June 1993, Tokyo prosecutors have arrested a bevy of high-ranking incumbent local government officials on charges of accepting bribes, including Toru Ishii, mayor of Sendai, Fujio Takeuchi, governor of Ibaraki Prefecture, and Shuntaro Honma, governor of Miyagi Prefecture. At the same time, they arrested the chairmen and vice presidents of several large Japanese construction firms on bribery charges. The companies involved included Shimizu Corp., Kajima Corp., Taisei Corp., and Hazama. In addition, on March 11, 1994, the special investigation section of the Tokyo District Public Prosecutor's Office arrested former

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<sup>2</sup> Chihō jichi hō (Local Autonomy Law), art. 234, Law No. 67 of 1947 [hereinafter Local Autonomy Law].

<sup>3</sup> Shin Kanemaru had been one of the most influential figures in Japanese politics as leader of Keiseikai, the largest faction in the Liberal Democratic Party, until he was arrested on charges of massive tax evasion, which led to revelations of back-door donations. At the same time, Kanemaru reigned as the don of the *kensetsu zoku gi'in* (literally, 'construction Diet men'), a group of special-interest politicians closely linked to the construction industry, and received huge under-the-table donations from construction firms. In the construction industry of Yamanashi Prefecture, Kanemaru's constituency, there was intense political strife in the gubernatorial election. As a rule, the construction interests that supported the winning candidate monopolized public works contracts given by the newly elected governor. The bid-winning construction companies gave unlawful contributions to the newly elected governor on the basis of the successful bid price.

Construction Minister Kishiro Nakamura<sup>4</sup> on charges of “intermediary bribery,” as provided for in article 197-4 of the Penal Code.<sup>5</sup> This was the first time in twenty-six years, since the 1968 arrest of Upper House member Seiichi Okura (Social Democratic Party), that an incumbent Diet member had been arrested for intermediary bribery.

Bid rigging in the construction industry is the root cause of corruption among politicians and public servants. It produces adverse effects by forcing taxpayers to bear the burden of high construction costs. Moreover, bid rigging runs counter to the competition rules, which are internationally common these days. This article aims to elucidate the root cause and background of the illegal practice of bid rigging and find ways to remedy this situation in order to prevent bid rigging. Specifically, it addresses five major points: 1) regulations on bid rigging in Japan; 2) major construction bid rigging cases in Japan; 3) regulations on bid rigging and major cases in Europe and the United States; 4) problems with Japan’s construction industry and the bidding contract system for public works projects; and 5) measures to prevent bid rigging in the construction industry. In particular, this article focuses on the question of how to toughen legal sanctions and improve bidding contract systems for public works projects.

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<sup>4</sup> Kishiro Nakamura, like Kanemaru, was an influential politician belonging to the Keiseikai Party and one of the “bosses” in the “construction tribe.” He was also deputy chairman of the Special Investigation Committee on the Antimonopoly Law. Nakamura received a bribe of ¥10 million from Shinji Kiyoyama, then vice president of Kajima Corp., and, in response to Kiyoyama’s request, pressured the FTC Chairman, Umezawa, to not bring criminal charges against the “Saitama Saturday Society.”

<sup>5</sup> Article 197-4 of Japan’s Penal Code defines the crime of intermediary bribery as follows:

A public officer who, in response to an entreaty, causes another public officer to commit improper acts, acts as an intermediary for the facilitation of such wrongdoing, or receives, demands or contracts to receive a bribe in exchange for committing such acts shall be sentenced to a penal servitude of not longer than five years.

## II. REGULATIONS ON BID RIGGING IN JAPAN

### A. *Regulations on Bid Rigging under the Antimonopoly Law*

In article 2.6 of the Antimonopoly Law,<sup>6</sup> bid rigging is defined as “the restriction of business activities through mutual cooperation between companies and the substantial restraint of competition in certain business areas against public interests (cartel).” Bid rigging is controlled in accordance with regulations that prohibit the unfair restriction of business, as prescribed in the latter part of article 3 of the Antimonopoly Law.<sup>7</sup> When trade associations are involved, bid rigging is controlled in accordance with regulations that prohibit a substantial restraint of competition by trade associations, as stipulated in article 8.1.1.<sup>8</sup>

The question then is what specific behavior among companies is deemed a case of “mutual restriction.” Naturally, if there is an explicit agreement among companies on the price and contract winner, then such behavior is illegal. Moreover, even a gentleman’s agreement is considered an explicit agreement, regardless of whether any effective measures are secured to impose sanctions on parties that violate the agreement. Furthermore, if, as a result of the exchange of information between companies, they reach a tacit understanding on the price and contract winner, this would constitute a violation of the law even when an explicit decision is not made at that point.

In particular, trade associations frequently become a hotbed of bid rigging. For this reason, the Fair Trade Commission (“FTC”) has announced two sets of guidelines to control the activities of trade associations. In 1979, the FTC released the “Guidelines under the Antimonopoly Law for Activities of Trade Associations.” The FTC presented regulatory guidelines to prevent trade associations from acting as coordinators of bid rigging and other behavior that hinders competition.

Furthermore, in 1984, the FTC issued “Guidelines under the Antimonopoly Law for Various Activities of Trade Associations in the Construction Industry Involved in Public Works Projects” (Construction Industry Guidelines) for the construction industry. The construction indus-

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<sup>6</sup> *Shiteki dokusen no kinshi oyobi kōsei torihiki no kakuho ni kansuru hōritsu* (Law Concerning the Prohibition of Private Monopoly and the Maintenance of Fair Trade) art. 2.6, Law No. 54 of 1947 [hereinafter Antimonopoly Law].

<sup>7</sup> *Id.* art. 3.

<sup>8</sup> *Id.* art. 8.1.

try, which takes part in public works projects, is an industry that subcontracts work on a single contract basis, mostly to medium and small-scale companies. Because competition is intense, some of these companies enter into contracts without taking profitability into account. Given these special characteristics of the construction industry, the likelihood of companies engaging in bid rigging is high. Moreover, in most cases, trade associations make arrangements for bid rigging. Thus, the FTC drew up the Construction Industry Guidelines and presented examples of legitimate behavior by trade associations in order to deter wrongdoing. The examples cited allow public works trade associations to provide information and managerial guidance in compliance with the Antimonopoly Law unless the expected contract winner or the bid price is determined in violation of rules ensuring competitive bidding. In other words, a general exchange of information is deemed legitimate, while the exchange of information on individual bids is illegal even if no agreement was reached on a successful bidder. The Construction Industry Guidelines were abolished as a result of the July 1994 formulation of "Guidelines under the Antimonopoly Law for Activities of Contractors and Trade Associations Involved in Public Bids" (Guidelines on Public Works Projects).

#### 1. *Regulatory Measures by the FTC*

The FTC controls bid rigging by taking the following actions. First, it orders the elimination of the violating measures.<sup>9</sup> In particular, it requires offenders to annul the bidding agreement made by companies and to disclose rigged bids in newspapers and other media. In addition, the FTC issues a cease and desist order to prevent repeat offenses and requires wrongdoers to report certain items to the FTC.

Second, surcharges are imposed.<sup>10</sup> To eliminate unfair profits, the FTC levies surcharges equal to the product of the successful bid price stemming from bid rigging at a certain rate computed according to the law. The rate is six percent of the successful bid price for large companies and three percent for medium and small-scale companies.

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<sup>9</sup> *Id.* arts. 7, 9.2.

<sup>10</sup> *Id.* arts. 7.2, 8.3.

Finally, the FTC can pursue criminal charges for illegal activities violating the Antimonopoly Law. On June 20, 1990, the FTC announced accusation standards titled "Guidelines of the Fair Trade Commission Concerning Accusations of Violations of the Antimonopoly Law," suggesting its intent to make criminal accusations. Subsequently, in November 1991, personnel in charge of marketing at eight makers of wrapping material for industrial use were accused on charges of forming price cartels. Up to that point, the FTC had filed a criminal indictment in only one case — the oil cartel of 1974. It can be said that the FTC is beginning aggressively to make criminal charges in line with its accusation standards.

As for criminal penalties, the offender is subject to either a maximum fine of ¥5 million or sentenced to a maximum three-year prison term.<sup>11</sup> Egregious offenders, on the other hand, are subject to both fines and prison terms.<sup>12</sup> Moreover, the double-penalty provision<sup>13</sup> calls for imposing a maximum fine of ¥100 million on corporations.<sup>14</sup> Trade associations are treated in the same manner as corporations. Furthermore, articles 95.2 and 95.3 stipulate that representatives of corporations and trade associations who, notwithstanding their knowledge of the offenses, fail to prevent and correct the situation are also subject to fines.<sup>15</sup>

## 2. *Damage Remedy Suits*

In addition, the purchaser under the contract (the government) can file a damage remedy suit against companies that engage in bid rigging, pursuant to article 25 of the Antimonopoly Law and article 709 of the Civil Code.<sup>16</sup> In May 1991, the FTC published the "Outline of the Provision of Materials Concerning Damage Remedy Suits against Violations of the Antimonopoly Law." In order to alleviate the plaintiffs' (injured parties') burden of proof, the FTC clarified the standards for submitting materials to the court necessary to prove the existence of violations and damages. As

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<sup>11</sup> *Id.* art. 89.

<sup>12</sup> *Id.* art. 92.

<sup>13</sup> *Id.* art. 95.

<sup>14</sup> The maximum penalty on companies and trade associations was raised from ¥5 million to ¥100 million (effective as of January 1, 1993). Japanese companies, construction companies in particular, strongly objected to the raising of the penalty on corporations to ¥100 million, separately from the penalties on individual offenders.

<sup>15</sup> Antimonopoly Law, *supra* note 6, arts. 95.2, 95.3.

<sup>16</sup> MINPŌ art. 709.

will be discussed later, in the lawsuit filed by residents against the "Saitama Saturday Society," the FTC submitted, upon the request of the Urawa District Court, investigation materials which constituted the basis of the decision on violations of the Antimonopoly Law.

A recent example of a large damage remedy suit is the 1988 bid rigging case concerning the U.S. naval base in Yokosuka. The U.S. naval base headquarters in Japan placed orders for the construction of facilities. The Study Group of U.S. Military Construction Safety Technology, a trade association, consisting of sixty-nine member firms and Kajima Corp., allegedly took part in bid rigging on this construction. To wipe out the wrongdoing, the FTC ordered these seventy firms to pay surcharges totaling ¥290 million, and issued a written warning to the 140 construction companies that engaged in bid rigging. Although Kajima Corp. was not a member of the Study Group, it decided the expected contract winner in tandem with members of the Study Group and adjusted bid prices so that the expected contract winner would be awarded the project. After the FTC took administrative actions, the U.S. Government filed a claim for damages totaling \$37 million, or roughly ¥5 billion, against the 140 construction companies that were involved in bid rigging. The case was settled when the companies agreed to pay nearly ¥5 billion in damages.

Moreover, in bringing damage remedy suits, the fee (stamp fee) that must be paid to the court was previously 0.5 percent of the amount sought by the suit for amounts exceeding ¥3 million. As such, it was difficult to make a claim for a vast sum of damages. Following the Japan-U.S. Structural Impediments Initiative ("SII") talks, article 3.1 of the Law Concerning Costs of Civil Lawsuits<sup>17</sup> was amended, and the fee to be paid to the court was reduced.

#### *B. Illegal Bid Rigging under the Penal Code*

Paragraph 2 of Penal Code 96-3 sets forth regulations concerning illegal bid rigging.<sup>18</sup> It states that there are criminal penalties for participation in a collusion at specific individual biddings aimed at "undermining the

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<sup>17</sup> Minji soshō hiyō nado ni kansuru hōritsu (Law Concerning Costs of Civil Lawsuits), art. 3.1, Law No. 40 of 1971.

<sup>18</sup> KEIHŌ art. 96-3.



fair price or making illegal profits.”<sup>19</sup> This provision was added to the Penal Code in 1941. Participants in illegal bid rigging are sentenced to a maximum two-year prison term or fined a maximum ¥2.5 million. On November 2, 1992, the Tokyo District Public Prosecutor’s Office brought charges of illegal collusion against marketing managers and other personnel of four companies involved in the bid rigging of seals used on various payment slips ordered by the Social Insurance Agency.<sup>20</sup>

According to Supreme Court precedent, a “fair price” does not refer to a fair price that should be measured objectively, separately from the concept of bidding, but generally means the successful bid price resulting from fair and free competition in the concerned bid.<sup>21</sup> For this reason, precedents of the Supreme Court suggest that a “fair price” is unrelated to the successful bidder’s profit, and thus real costs and fair profits do not need to be taken into account in defining “fair price.”<sup>22</sup> However, according to the lower court rulings, as in the Tokyo High Court ruling of July 20, 1953, a “fair price” is a price that includes ordinary profit in the minimum real construction cost.<sup>23</sup> There are precedents where bid rigging aimed at

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<sup>19</sup> *Id.*

<sup>20</sup> Judgment of Dec. 14, 1993, Kōsai [High Court], SHŌJI HANREI, No. 937, Mar. 15, 1994, at 27 (holding all defendants guilty of violating the Antimonopoly Law in a bid-rigging case involving use of seals on various payment slips ordered by the Social Insurance Agency). The FTC lodged charges of illegal collusion as provided in the Penal Code and violation of articles 73-1 and 96 of the Antimonopoly Law.

<sup>21</sup> Judgment of May 28, 1944, Daishinōin [Great Court of Judicature], 23 Daihan Keishū 97 (holding that a “fair price” does not refer to a fair price that should be measured objectively, apart from the concept of bidding, but rather the successful bid price resulting from fair and free competition in the bidding concerned).

<sup>22</sup> Judgment of July 19, 1957, Saikōsai [Supreme Court], 11 Keishū 1966. “Fair price,” as mentioned previously in Penal Code art. 96-3, refers to a successful bid price formed by fair and free competition in the concerned bidding rather than a fair price to be measured objectively, separately from the notion of bidding, or “a price that includes reasonable profit plus the real cost and, at which the party with the most favorable terms wins the contract bid through fair and free competition.” That is, the Supreme Court ruled that collusion aimed at avoiding “bidding at a loss” is also illegal.

<sup>23</sup> Judgment of July 20, 1953, Tokyo Kōsai [High Court]. The Tokyo High Court ruled that “an unfair profit” occurs when that profit undermines the fair price to be determined at a bidding, that is, a price at which a bidder with the most advantageous condition ought to have successfully bid with the sum of the net cost and a proper profit. That is, the Tokyo High Court’s interpretation is that collusion aimed at avoiding bidding at a loss is *not* illegal. *See also* Judgment of Oct. 30, 1954, Osaka Kōsai [High Court]; Judgment of May 24, 1957, Tokyo Kōsai [High Court], 10 Kōkeishū 361. Both the Osaka High Court ruling and the Tokyo High Court ruling share the same interpretation. In particular, in its May 24, 1957 ruling, the Tokyo High Court held that:

If the sole intent of the competitive bidding system is to discover the person that offers the most favorable terms for calculation purposes to the implementing side . . . barriers to free market principles may be seriously hampered and the results of competitive bidding will lead to competition among companies where bidders will not stop at any means. Depending on the

avoiding winning contracts at a price less than the cost was not deemed a crime. Today, the court generally adheres to this interpretation, which does not view all bid rigging as illegal.<sup>24</sup>

“Unfair profits” are found when a promise is made to distribute to bidders, payoffs in excess of what is considered a sign of courtesy generally accepted by society.<sup>25</sup>

### C. *Other Issues*

The Construction Law authorizes the Minister of Construction and prefectural governors to impose a business suspension for not longer than one year on companies that resort to such viciously illegal acts as bribery and intimidation. However, the “Survey Concerning Procedures for Participation in Competitive Contracts,” released by the Management and

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economic situation and other conditions, this will cause bidding to be carried out at so-called ‘dumping prices’ that ignore companies’ economic profits, imperiling the very existence of the companies themselves and giving rise to a situation that may constitute a serious threat to the lives of those who depend on such companies . . . inflicting unexpected losses on the bid implementing party, and, in many cases, may economically harm the state and public . . .

Judgment of May 24, 1957, Tokyo Kōsai, [High Court], 10 Kōkeishū 361. The Tokyo High Court deemed it appropriate, therefore, to exempt collusion aimed at avoiding bidding at a loss from the provisions of Penal Code art. 96-3. Thus, the High Court ruling was squarely opposite to that of the Supreme Court, mentioned in Note 22.

<sup>24</sup> Judgment of Aug. 27, 1968, Otsu Chisai [District Court], 10 Kakeishū 866 (holding that, in the case of bidding that ignores profits, an agreement made with the intent to raise the successful bid price to reach the amount that includes ordinary profits, does not constitute collusion aimed at undermining a fair price).

<sup>25</sup> In *Annotated Penal Code*, compiled by Shigemitsu Dando, “an aim to acquire unfair profits” refers to:

- (1) a case where collusion is carried out without any intent to implement construction work but for the sole purpose of obtaining payoffs to bidders, and
- (2) a case where economic gains are in excess of what is considered a sign of commonly accepted courtesy and are unreasonably high even when a company which has the intention to implement construction work, abandons such an intention and agrees to engage in collusion with other companies in exchange for receiving money and other economic gains.

SHIGEMITSU DANDO, CHŪSHAKU KEIHŌ [ANNOTATED PENAL CODE] (1964). See also Judgment of Jan. 22, 1957, Saikōsai [Supreme Court], 11 Keishū 50. On July 19, 1957, the Supreme Court ruled that “unfair profits as described later in Section 2 of Penal Code 96-3 refer to the case where gains from collusion are in excess of what is considered a sign of courtesy generally accepted by society.” Judgment of July 19, 1957, Saikōsai [Supreme Court], 11 Keishū 1966.

Coordination Agency in December 1993, pointed out that administrative measures taken against companies that engaged in wrongdoing were lenient. For instance, the heaviest of the administrative actions taken under the terms of the Construction Law<sup>26</sup> against twenty-five defendants found guilty of such offenses as bribery, bidding interference and intimidation was suspension of business operations for only fifteen days. In addition, chief executive officers of a company warned by the FTC are held ineligible for decoration for five years.

Recently, companies which engage in bid rigging face the possibility of being sued by stockholders and residents. As a result of the amendment of the Commercial Law<sup>27</sup> in 1993, paragraph 4 was added to article 267. Stockholders can now bring an action as "a claim that is not for property rights" with a stamp fee of only ¥8,200. In October 1993, stockholders filed a lawsuit to claim damages totaling ¥99 million against Shigeru Honda, former chairman of Hazama-Gumi, and four managing directors. Moreover, paragraph 1.4 of section 242-2 of the Local Government Law<sup>28</sup> stipulates that when leaders and employees of local public authorities are found to have paid illegal or unfair public money, residents can make a claim for damages in place of the local public authorities. In the "Saitama Saturday Society" case, sixty-one residents brought action against former Governor Hata of Saitama Prefecture, former prefectural leaders, and sixty-three general contractors who were members of the Saturday Society, and claimed for damages against Saitama Prefecture for awarding the contract at a high price.

### 1. *Major Construction Bid Rigging Cases in Japan*

The following five cases can be cited as major bid rigging cases in the construction industry over the past years. The first instance is the 1981 bid rigging case of the Shizuoka General Constructors Association, Shimizu General Constructors Association, and Numazu Seifukai.<sup>29</sup> In this incident,

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<sup>26</sup> Kensei-gyō hō (Construction Law), Law No. 100 of 1949 [hereinafter Construction Law].

<sup>27</sup> SHŌHŌ art. 267.

<sup>28</sup> Local Autonomy Law, *supra* note 2, art. 242-2.

<sup>29</sup> With regard to construction work for which orders were placed through bidding within the geographical area of each association, a contract winner was decided on the basis of the rules established by the Shizuoka General Constructors Association, Shimizu General Constructors Association, and Numazu Seifukai for determining the contract winner. For instance, the Shizuoka General Constructors Association, in principle, decided the expected contract winner of the concerned construction project through talks held on the day before the bid date in order to prevent a decline in the contract price and

Shizuoka City, Shimizu City, Numazu City and the local federation of construction contractors acted as coordinators for bid rigging on public works contracts. The FTC ordered a total of 111 firms — 44 in Shizuoka, 42 in Shimizu, and 25 in Numazu — to take measures to eliminate violations and pay surcharges totaling ¥290 million. Because the FTC conducted an inspection, social interest in bid rigging in the construction industry was substantially heightened.

The second instance is the 1988 bid rigging case of the Yokosuka U.S. naval base. This case drew widespread attention because it developed into an international scandal. The FTC took administrative action, while the U.S. Government made a claim for damages.

The third instance is the case of the Maritime Earth Filling Sediment Association (“MEFSA”) of 1989. This case involved bid rigging on mountain sand maritime transport work and the pouring of mountain sand into the ocean to create a levee around the peripheral area of the new Kansai International Airport island during construction. MEFSA, a trade association, decided the volume and unit price of orders by companies from which the members received orders, and made the members bid accordingly. The FTC ordered six MEFSA member firms to take measures to eliminate illegal activities and pay surcharges totaling ¥300 million. In addition, MEFSA was broken up in 1989 to prevent future wrongdoing.

The fourth instance is the “Saitama Saturday Society” case of 1992.<sup>30</sup> In this case, sixty-six member firms of the “Saitama Saturday Society” engaged in bid rigging on public works projects ordered by prefectures or municipalities in Saitama Prefecture. This case attracted attention primarily because there had been speculation that the FTC would bring criminal charges as in the case of the industrial-use wrapping material cartel. Although the FTC considered criminal charges, no indictments were

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make the opportunities for contract awarding equal. When an agreement failed to be reached through talks, the Association determined “rules concerning rationalization,” which basically called for the expected contract winner to be decided by the arbitration committee appointed by the association.

Prompted by the disclosure of these three cases, the government in 1984, formulated Guidelines under the Antimonopoly Act for Various Activities of Trade Associations in the Construction Industry Involved in Public Works Projects.

<sup>30</sup> This case led to the crime of intermediary bribery committed by Diet member Kishiro Nakamura. Although the FTC wanted to bring criminal charges against him, it faced difficulty in proving that all of the sales managers of 66 firms had participated in a cartel. Thus, after consulting with the prosecutors, the FTC dropped the idea of pressing criminal charges.

forthcoming. The FTC ordered the sixty-six firms to eliminate the violating practices and pay surcharges totaling ¥1 billion.

The fifth instance is the 1993 case of the Sasebo Naval Base. At the time, the U.S. Department of Justice was planning to file a damage remedy suit in accordance with article 709 of Japan's Civil Code<sup>31</sup> before the FTC took administrative action. This case differs from the case of the Yokosuka U.S. naval base in that the U.S. Department of Justice actually took legal steps prior to the FTC's administrative actions. In the end, an amicable settlement was reached when the U.S. Department of Justice received a total of \$1,055,000 (roughly ¥113 million) from twenty-seven Japanese companies.

From these cases, it can be concluded that one of the salient features of bid rigging in the Japanese construction industry is the involvement of trade associations in determining the expected contract winner and the successful bid price.

#### IV. BID RIGGING IN THE UNITED STATES AND EUROPE

##### A. *The United States*

Europe and the United States also impose strict controls on bid rigging. In the United States, bid rigging is accomplished through the use of cartels, which are per se illegal. The Antitrust Division of the Department of Justice pursues criminal charges in accordance with section 1 of the Sherman Act. Individual violators are fined a maximum amount equal to the largest of either \$350,000, twice the profits acquired from illegal activities, or twice the damage incurred as a result of illegal activities, and/or sentenced to a maximum three-year imprisonment. On the other hand, corporations are fined a maximum amount equal to the largest of either \$10 million, twice the profits acquired from illegal activities, or twice the damage incurred as a result of illegal activities. Furthermore, the Antitrust Division of the Department of Justice can file a suit under equity in accordance with section 4 of the Sherman Act and can request the elimination of violations in the future. In addition, the Department of Justice can bring damage remedy suits as provided in section 4A of the Clayton Act and make a claim for treble damages and compensation for lawsuit costs. The Federal Trade Commission also can take administrative

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<sup>31</sup> MINPŌ art. 709.

measures in accordance with section 5 of the Federal Trade Commission Act. In reality, the antitrust division of the Department of Justice decides whether to bring criminal indictments in most cases.

Based on precedent, bid rigging in the United States can be classified into the following types:

- (a) Refusing to participate in bidding or agreeing to set an unreasonably high bid price;<sup>32</sup>
- (b) Agreeing to compare bid prices before submitting them to the owner;<sup>33</sup>
- (c) Agreeing to submit only moderate individual bids so that the project will be awarded to a joint venture, in which the work and profits can be shared;<sup>34</sup> and
- (d) Engaging in bidding on a rotational basis by obtaining the consent of specific competitors to not participate in bidding in exchange for a promise to make them the successful bidder in a future bid.<sup>35</sup>

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<sup>32</sup> See, e.g., *United States v. Champion Int'l Corp.*, 557 F.2d 1270, 1273 (4th Cir. 1977), *cert. denied*, 434 U.S. 938 (1977). Seven companies, including Champion International, engaged in bid rigging so that they could purchase timber sold by the United States Forest Service at the lowest price the Forest Service could accept. Seven of the defendant firms were found guilty.

<sup>33</sup> See, e.g., *United States v. W.F. Brinkley & Son Constr. Co.*, 783 F.2d 1157 (4th Cir. 1986). This was a bid rigging case related to a pipeline construction project undertaken by Elizabeth City (North Carolina) for carrying water from the Pasquotank river. By comparing bid prices in advance, companies with low bid prices found out that other firms were actually no longer competitors and therefore could raise their bid price. This practice was regarded as bid-rigging in violation of the Antimonopoly Law. *Id.* at 1158-60.

<sup>34</sup> See *COMPACT v. Metropolitan Gov't*, 594 F. Supp. 1567, 1577-79 (M.D. Tenn. 1984). COMPACT, a construction company in Tennessee, filed suit against the city for excluding it from subcontracted work on the metropolitan airport facility. The federal district court ruled that the construction company colluded with other companies to form a joint venture in order to acquire the work allocated to the minority group and divide it among themselves. This, the court said, was illegal and interfered with market division and public bidding.

The federal district court also held that joint arrangements are allowed only: 1) when a contract cannot be concluded without a tie-up; 2) when a bidder is to manufacture a product it does not currently manufacture; and 3) when a product cannot be manufactured competitively by only one participant. *Id.* at 1576.

<sup>35</sup> See, e.g., *United States v. Champion Int'l Corp.*, 557 F.2d 1270, 1273 (9th Cir. 1977).

Although the methods used by contractors to coordinate orders are very similar to Japan's bid rigging cases, in the United States politicians and the governmental purchasing body intervene only in rare cases.

### *B. Europe*

Europe has also imposed strict regulations on bid rigging. Bid rigging is prohibited as a cartel activity under article 85.1 of the Rome Treaty. Procedures of prohibition provisions are set forth in article 17 of the 1962 regulations of the board of chairmen. Meanwhile, the EC Commission can issue an order for elimination measures against illegal activities in accordance with article 85.1 of the Rome Treaty. In addition, it can impose on companies which knowingly, or accidentally, violate article 85.1 of the Rome Treaty a fine of ECU 1,000 or more, or an amount less than the higher of either ECU 10 million or 10% of total sales for the previous fiscal year.

In February 1992, the EC Commission levied a fine totaling ECU 22.50 million on twenty-eight groups (4,000 firms) and 300 firms for bid rigging by the Construction Association of the Netherlands.<sup>36</sup>

In Germany, all cartels are, in principle, prohibited by article 1.1 of the Act Against Restraints of Competition. The Federal Cartel Office and State Authorities levy fines on offenders, as provided in article 38.4 of the Act Against Restraints of Competition. The maximum fine is the higher of either DM1 million or three times net sales acquired from illegal activities. Fines are levied on not only individuals and companies that carry out illegal activities but also on officers who neglect their supervisory duties. Furthermore, if bid rigging was carried out, the owner can make a claim for damages against the party which engaged in bid rigging as defined in article 35 of the Act Against Restraints of Competition. Additionally, bid rigging can be controlled as fraud under article 263 of the German Criminal Code. However, there have not yet been any cases where this law was applied to bid rigging.

In the construction bid rigging case of 1975, a fine totaling DM36 million was levied on 343 firms and 483 individuals. In the railroad and

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<sup>36</sup> SPO is an organization in the Netherlands, consisting of twenty-eight construction associations. A total of more than 4,000 leading and medium-sized construction companies are members of the twenty-eight associations.

telephone bid rigging case of 1983, a fine amounting to roughly DM25 million was imposed on sixty-one firms and ninety individuals.

## V. REVIEW OF JAPAN'S CONSTRUCTION INDUSTRY

Bid rigging is rampant in Japan because there are problems with the structure of the construction industry and the system for placing orders for public works projects. Today, the construction industry comprises a menagerie of roughly 520,000 construction companies. Moreover, about 99% of them are medium and small companies with a capital of ¥100 million or less. The industry employs a staggering 6.54 million workers, or roughly 9% of Japan's work force. If construction companies were allowed to freely compete for public works contracts, it is possible that competition between small companies would escalate and thus force some of the companies to go bankrupt and some workers to lose their jobs. For this reason, construction companies generally believe that bid rigging is a rational way to evenly allocate orders received. Further, in some quarters of administrative agencies, it is viewed that the equalization of opportunities for receiving orders and the protection of local companies calls for turning a blind eye to bid rigging. Both views argue that there is no other choice but to approve bid rigging in order to prevent small companies from being weeded out of the market.

More recently, it has been pointed out that the bidding contract system for public works projects is flawed and gives rise to illegal activities. In particular, the system of designated competitive bidding is being criticized. Under this system, the Ministry of Construction and local public authorities rate construction companies according to their construction capacity and other factors. They then designate three to twenty eligible bidders according to type and scale of individual public works projects, and enter into a contract with the company that presents the most favorable terms during bidding. Yet, the criteria for designating companies are unclear, and the process of decision lacks transparency. That is to say, administrative agencies, which are the owners, designate companies to engage in bidding largely on the basis of arbitrary decisions. Meanwhile, because companies cannot participate in bidding unless they are designated, they are in a very weak position in relation to administrative agencies.



Thus, companies offer public servants from the Ministry of Construction and local public authorities cushy jobs to cement ties with administrative agencies. In order to be included in the list of designated bidders, construction companies also make prodigious political donations to big-name politicians such as Shin Kanemaru, who has vast influence over the Ministry of Construction and heads of local public authorities who have official powers to place orders for public works projects. Furthermore, construction companies bribe and ask heads of local public authorities and big-name politicians to act as coordinators of bid rigging to help them win public works contracts.

A series of "general contractors corruption" was exposed with the March 1993 arrest of Shin Kanemaru, former vice president of the Liberal Democratic Party. Prompted by this, the designated competitive bidding system has been drawing criticism as a system that facilitates bribes to heads of local public authorities and prominent Diet members.

In addition, the "expected bid price system" is used by construction companies as a criterion for agreeing on the successful bid price through bid rigging. Under this system, the owner estimates in advance the construction cost and treats this expected price as the upper limit on the bid price. Therefore even if bid rigging is carried out, the successful bid price will never exceed the expected price. But in bid rigging, the rigged price is very close to the expected price, and consequently, the realization of a lower price which would have resulted under fair and free competition is hindered.

In short, the construction industry has been coordinating orders between companies through bid rigging because it is beset with problems concerning its structure and the bidding contract system for public works projects. The adverse result is that even small business owners, who lack competitiveness in technology and management, are sustained at the expense of taxpayers.<sup>37</sup>

## VI. CONCLUSION

The following two measures are effective for preventing bid rigging in the construction industry. First, illegal activities can be prevented if the FTC and the Public Prosecutors Office work together closely and step up regulations. These agencies should make it clear that all collusive activities

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<sup>37</sup> It is said that in municipalities which introduced general competitive bidding, the cost of public works declined roughly 20%.

are illegal. Specifically, it is essential to stiffen penalties against bid rigging through such administrative means as elimination measures, surcharges, and criminal accusations by the FTC, as well as criminal indictments by the Public Prosecutors Office against bid rigging under the Antimonopoly Law and Criminal Code. On March 4, 1994, the FTC published the draft of "Guidelines under the Antimonopoly Act for Activities concerning Public Bidding by Companies and Trade Associations" and indicated the regulatory standards under the Antimonopoly Law for procuring public works contracts and materials bidding in the public sector. On the other hand, it is necessary for the FTC to restrict bidding at prices below cost as unfair underselling in order to forestall cut-throat bidding, not to mention bid rigging. Local public authorities are taking measures to prevent bidding at prices below cost by setting the minimum price at 80 to 85% of the expected price.<sup>38</sup> Nevertheless, it is said that there are cases where local public authorities underestimate the expected price because they do not fully take price changes into account. In this sense, it is questionable as to how effective these measures are in preventing bidding below cost. Thus, it would be effective to require the disclosure of the breakdown of the cost to the successful bidder so that companies with objections can file a complaint to the FTC about unfair underselling.

Second, the public works bidding contract system needs to be improved. In December 1993, the Central Council on Construction Contracting Business, an advisory body to the Minister of Construction, recommended the reform of the bidding contract system in a report titled "Reform of the Bidding Contract System for Public Works Projects." The centerpiece of the report consists of four points concerning reform. First, it calls for the adoption of a system that does not allow the owner to make arbitrary decisions and for an increase in the objectivity of procedures by enacting and disclosing various standards. Second, the Council suggests stepping up monitoring, particularly by a third party, in order to enhance the transparency of procedures. Third, the Council recommends the elimination of bid rigging and other illegal activities by establishing conditions that facilitate competition. Fourth, it calls for stiffening penalties to enforce fair rules. In the future, it will be vital for the Ministry of Construction to

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<sup>38</sup> Local Autonomy Law, *supra* note 2, art. 234(3).

accept the recommendations of the Council and enhance the objectivity and transparency of bidding contract procedures for public works projects. In particular, it will be increasingly important to switch from the designated competitive bidding system, which is largely affected by the arbitrariness of the owner, to an open-bidding system, and to allow a third party to conduct qualification screening even if bidding eligibility is restricted.