

REDACTED REPORT

National Roads Improvement and Management Program (Phase 1)

Republic of the Philippines



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EXECUTIVE SUMMARY

This Report provides the findings of an Integrity Vice Presidency (INT) investigation into suspected collusion among a group of local and foreign companies, as well as allegations regarding the involvement of politicians and government officials in that collusion, during the tender of two contracts under Phase 1 of the National Roads Improvement and Management Project (NRIMP) in the Philippines. This Report is being made public as part of the Bank's general practice of making INT's operations transparent. However, as INT investigations often prompt related national investigations, this Report has been redacted to avoid detailing information that, if stated publicly, could prejudice any such investigations. INT found evidence indicating that there was collusion in the NRIMP tenders under investigation as well as indicators of corruption. INT's investigation found patterns in the bid prices and bids that indicated collusion among the NRIMP bidders. These patterns included:

- Total bid prices that consistently exceeded the cost estimate by 20% or more;
- Abnormally high and unexplained unit prices, particularly in the bids' Earthworks component, that suggested manipulation of total bid prices;
- Direct mathematical relationships between some bids' prices and the cost estimate;
- Two bidders that submitted bids with component prices that differed by in some cases hundreds of thousands, and in other cases by millions, of US Dollars but total prices that differed by less than a hundred Dollars;
- A majority of bids that repeatedly contained substantial computation errors, many in excess of one million Philippine Pesos, an indicator of last-minute bid manipulation;
- Multiple losing bidders that submitted forged bid securities with their bids; and
- Patterns of inconsistent bidder prequalification results that suggest that some bidders were disqualified for invalid reasons, such as failure to "fit the contract profile."

Consistent with INT's bid analysis, a number of witnesses separately told INT investigators that a well-organized cartel, managed by contractors and government officials, was improperly influencing DPWH contract award decisions and setting inflated bid prices. One witness complained of bidders meeting to rig parts of the bidding process and was able to accurately state, in advance, the results of a round of bidding. In addition, multiple witnesses independently alleged that politicians and government officials were involved in the cartel and, on cartel-affected projects, demanded large percentages of the contract price as kickbacks. Many of these witnesses told INT investigators of previous first-hand experiences of bribe solicitations and payments with this cartel in other projects. These allegations are mentioned because they were made consistently by many witnesses in independent interviews. In November 2007, INT shared these allegations, as well as its information regarding collusion, with the Department of Finance and the Office of the Ombudsman. INT contacted the Office of the Ombudsman about the case several times thereafter. In January 2009, the Bank debarred seven companies and one individual for colluding while bidding for these contracts (an eighth company had been debarred in August 2008).

BACKGROUND

This Report provides the findings, and certain investigation-related allegations, of an Integrity Vice Presidency (INT) investigation into collusion among a group of local and foreign companies, and allegedly involving politicians and government officials, during the tender processes of two contracts under Phase 1 of the National Roads Improvement and Management Program (NRIMP) project in the Philippines. This Report is being made public as part of the Bank's general practice of making INT's operations transparent. However, as INT investigations often prompt related national investigations, this Report has been redacted to avoid detailing information that, if stated publicly, could prejudice any such investigations.

NRIMP, which is administered by the Department of Public Works and Highways¹ (DPWH), seeks to improve sections of the national road network and increase the government's capacity to monitor, maintain, and further develop the Philippines' highways. The Project is being implemented in three phases from 2000 to 2009, at a total estimated cost of US\$2 billion. The Project's first phase, NRIMP-1, sought to establish a well-functioning preventative maintenance program for the national roads system, redesign the system's road management program, and design policy and institutional reforms. The World Bank (Bank) provided the Government of the Philippines with a US\$150 million loan to finance the implementation of NRIMP-1. The Loan became effective on July 7, 2000, and US\$133.3 million of its funds were disbursed by its March 31, 2007 closing.

In April 2003, INT was informed by the Bank team supervising the Project that the procurement process relating to the award of two NRIMP-1 contracts (the NRIMP-1 Contracts) might have been tainted by fraud and corruption.² Those Contracts, with a combined estimated value of approximately Philippine Pesos (PHP) 1.88 billion (US\$33 million), were for the rehabilitation of parts of the Surigao-Davao Coastal Road, the Kabankalan-Basay Road, and the San Enrique-Vallehermoso Road.³ Bank staff had determined that the results of the 2001-2002 bid process showed indications of collusion, most notably the questionable disqualification of some of the potential bidders and abnormally high bid prices. The Bank's task team accordingly declined to issue a letter of no objection to the results of this first round, asked DPWH to re-bid, and referred the matter to INT.⁴ Finding the bid prices still unjustifiably high after the 2004 re-bid, the Bank asked DPWH to carry out a third round of bidding. The Bank ultimately decided not to provide a no-objection letter a third time, for the same reason, in 2006. The contracts were not awarded under the NRIMP project.

METHODOLOGY

In 2004, INT commenced an investigation into the first two rounds of bidding and ultimately investigated the third round of bidding as well. INT's investigation, which lasted over three years and spanned six countries, consisted of a review of relevant NRIMP documents; a quantitative analysis of the bids submitted in the three rounds of bidding to identify any patterns indicative of collusion or other evidence of illicit cartel activity; and more than 60 interviews with representatives of bidders, government officials, representatives of financial institutions, and construction industry representatives.

¹ The DPWH is a cabinet-level department of the government of the Philippines that is responsible for the planning, design, construction, and maintenance of elements of the national infrastructure, most notably including roads, bridges, and flood control systems.

² In the third round of bidding, Contract 2 was split into two packages, designated herein as Packages 2(A) and 2(B).

³ US Dollar figures are provided for ease of reference only and are approximations as, over time, the initial contract valuations have been reassessed and currency exchange rates have fluctuated. The initial cost estimate for the two contracts was PHP 1.88 billion.

⁴ INT also received allegations that the NRIMP-1 Contracts were subject to kickbacks to politicians and government officials from contractors.

FINDINGS

INT's investigation found evidence indicating that the contractors bidding for the NRIMP-1 Contracts colluded during all three rounds of bidding.

1. INT found substantial evidence indicating that a cartel, consisting of international and local companies, operated on Philippines road projects.

Numerous witnesses independently informed INT investigators that a well-organized cartel, managed by contractors with support from government officials, improperly influenced DPWH contract awards and set inflated bid prices on projects funded by the Bank and others. Witnesses stated that, under the cartel's system, bid prices were dictated by the cartel leadership; uncooperative bidders were forced out of the process before bids were submitted; winners were prearranged; and losing bidders, which in some cases participated to avoid displeasing influential members of the cartel, were compensated for their participation.

Witnesses told INT investigators that, a)s a result of the collusive activity that took place during the bidding for the NRIMP-1 Contracts, bid prices were inflated by 20% to 30% above the DPWH's own cost estimate—called the Approved Budget for the Contract (ABC)⁵—in order to facilitate the demanded bribe payments. This was consistent with the bidding results, as detailed in the following charts that rank bids by the percentage that their bid prices exceeded the ABC.⁶

Contract 1 – 1st round
Winning Bid 26.2%
Losing Bid 1 27.8%
Losing Bid 2 31.0%
Losing Bid 3 32.0%
Losing Bid 4 33.0%
Losing Bid 5 34.0%
Losing Bid 6 34.7%

Contract 2 – 1st round
Winning Bid 25.5%
Losing Bid 1 26.6%
Losing Bid 2 28.7%
Losing Bid 3 35.4%
Losing Bid 4 52.0%

Contract 1 – 2nd round
Winning Bid 27.1%
Losing Bid 1 45.3%
Losing Bid 2 46.4%
Losing Bid 3 78.1%

Contract 2 – 2nd round
Winning Bid 24.8%
Losing Bid 1 38.2%
Losing Bid 2 39.1%
Losing Bid 3 43.1%
Losing Bid 4 51.5%
Losing Bid 5 58.4%

⁵ The ABC refers to the budget for the contract duly approved by the Head of the Procuring Entity.

⁶ The contractor that submitting the winning bid, as well as the positions of various losing bidders, changed between the various rounds of bidding.

In the third round of bidding, all of the losing bid prices still exceeded the ABC by 20% or more:

<i>Contract 1 – 3rd round</i>	<i>Contract 2(A) – 3rd round</i>	<i>Contract 2(B) – 3rd round</i>
Winning Bid 15.6%	Winning Bid 13.4%	Winning Bid 16.9%
Losing Bid 1 20.0%	Losing Bid 1 29.6%	Losing Bid 1 36.0%
Losing Bid 2 22.2%	Losing Bid 2 35.5%	Losing Bid 2 36.0%
Losing Bid 3 22.2%	Losing Bid 3 35.7%	Losing Bid 3 37.0%
Losing Bid 4 22.4%	Losing Bid 4 38.5%	Losing Bid 4 39.0%
	Losing Bid 5 40.0%	Losing Bid 5 39.6%
		Losing Bid 6 42.3%

Further, various witnesses told INT investigators that the ABC itself appeared inflated. These witnesses stated that the existence of the collusive activity is an “open secret” and that it is referred to as the “SOP,” or Standard Operating Procedure. Remarkably, an anonymous informant correctly told INT investigators in advance what the results of the final round of bidding would be.

2. INT’s analysis of the bids for the NRIMP-1 Contracts revealed significant indicators of collusion.

INT’s quantitative analysis of the three rounds of bidding identified two significant indicators of collusion that corroborated the witnesses’ statements that a cartel was involved in the NRIMP-1 Contract tenders. First, bids in all rounds showed abnormally high and unexplained unit costs. For example, the Earthworks component of each bid represented a large percentage of the bid’s total cost. Earthworks is comprised largely of manual labor to prepare the land for the road, e.g., clearing and grubbing, removal of structures and obstructions, excavation, embankment, etc.. Such non-specialized labor should not vary significantly in price between bidders. However, INT’s analysis revealed significant price variation among the NRIMP-1 Contract bids’ Earthworks components, indicating that the bidders were using the price of Earthworks to manipulate their total bid prices to meet pre-arranged amounts:

- In the first round of bidding on Contract 1, the bid prices for Earthworks ranged from 8.5% to over 100% above the Earthworks ABC.
- In the second round of bidding for Contract 1, the bid prices for Earthworks ranged from over 70% to nearly 175% above the Earthworks ABC. Notably, although the DPWH lowered the second round’s Earthworks ABC by nearly PHP 7 million, the lowest bid’s Earthworks price rose by over PHP 60 million.
- In the second round of bidding for Contract 2, the overall lowest bidder’s Earthworks price exceeded the Earthworks ABC by almost 43%, and the other bids’ Earthworks prices exceeded the ABC by between 90% and nearly 175%. Comparing bidders’ pricing between different bids also suggested price manipulation: for example, the same bidder that offered the lowest Earthworks price in the second round of bidding for Contract 1 simultaneously offered nearly the highest Earthworks price (over 170% above the Earthworks ABC) in the second round of bidding for Contract 2.
- In the third round of bidding for Contract 2, Package 2(A), the lowest Earthworks bid price exceeded the Earthworks ABC by over 20%, and the highest Earthworks bid prices exceeded that ABC by between 110% and 125%.

- In the third round of bidding for Contract 2, Package 2(B), the lowest Earthworks bid price was 6.5% lower than the Earthworks ABC. However, the other bids' Earthworks prices exceeded that ABC by 31%, 38%, 43%, 60%, 90%, and 105%, respectively.

Second, patterns between bids indicated price coordination between bidders that corroborate witnesses' statements that the bidders colluded. Examples of such patterns include the following:

- Symmetrical relationship between bids and the ABC. In the first round of bidding for Contract 1, four bidders' subtotals exceeded the ABC in exact 1% increments: 31.0% over the ABC; 32.0% over the ABC; 33.0% over the ABC; and 34.0% over the ABC.
- Two bidders submitted bids with widely disparate component prices but extremely similar total prices.

In the third round of bidding for Contract 1, the two bidders' Earthworks prices differed by PHP 77 million (US\$1.43 million), but their total prices differed by less than PHP 1,700 (US\$31). Similarly, in the third round of bidding for Contract 2, Package 2(A), the two bidders' Earthworks prices differed by PHP 56 million (US\$1 million), but their total prices differed by less than PHP 300,000 (US\$5,600). Moreover, in the third round of bidding for Contract 2, Package 2(B), the two bidders' Earthworks components differed by PHP 34 million (US\$630,000) and their Surface Course components differed by PHP 98 million (US\$1.81 million), but their total prices (after the correction of calculation errors) differed by only PHP 3,519 (US\$65).

In a competitive bidding process it is highly unlikely that prices would exhibit these types of patterns.

3. Bids for the NRIMP-1 Contracts contained numerous, significant calculation errors.

Of the 37 bids accepted for review in the three rounds of bidding for Contracts 1 and 2, only 16 were free of substantial computational errors. Of the 21 arithmetical corrections required, eleven were larger than PHP 1 million. This pattern of errors corroborates witnesses' statements, detailed below, that the cartel leaders dictated bidders' final bid prices the day before the bids were due to be submitted. Such a practice would prompt last-minute bid price revisions likely to result in mathematical errors.

4. INT found evidence that at least two bidders submitted forged bid securities with their bids.

While forged bid securities are instances of fraudulent activity that may be independent of any cartel, their use can be an indicator of collusion. Preordained losing bidders have little or no direct financial stake in the outcome of their bids, and obtaining a bid security imposes a large cost on a bidder, so in a cartel designated losing bidders often forge their bid securities to reduce the cost of submitting a bid that they know that they will lose. INT investigators inquired with the banks that purportedly issued various bidders' bid securities and found that at least two losing bidders submitted forged bid securities with their bids for the NRIMP-1 Contracts. Indeed, one of the foreign contractors that purportedly had bid for the NRIMP-1 Contracts told INT investigators it had not submitted a bid at all; rather, another company had submitted bids using its name.

ALLEGATIONS OF CORRUPTION

In addition to the evidence of collusion detailed above, over 15 witnesses independently complained of systemic corruption undermining competition in Philippines road projects. Witnesses told INT investigators that politicians, local businessmen, and DPWH officials usually were involved in the cartel's operations. Some witnesses told INT investigators that a politician representing the area in which the project is to be carried out normally selected the winning contractor. Witnesses said that then, usually the day before the bid submission deadline, the cartel members met at a local hotel and the designated losing bidders were told the pre-arranged prices that they were to bid. Witnesses explained that these prices were significantly inflated to exceed the already-inflated price of the designated winner. Witnesses added that, prior to their submission, the losers' bids would be checked by the government officials who acted as the cartel's "mediators", to ensure that the bids adhered to the cartel-ordered pricing scheme.

Witnesses stated that the participating politicians and government officials demand large percentages of the contract price as kickbacks, and that doing work at a profit is virtually impossible for honest contractors. Some witnesses told INT investigators of meetings that they have had with politicians and public officials during which bribes were discussed, and of instances in which they or their companies made, or otherwise knew of, payments to public officials and politicians. Some companies told INT investigators that, because of the cartel, they would no longer bid on public works projects or had left the Philippines altogether. Some companies also spoke of how dangerous it was to act contrary to the cartel's wishes and told INT investigators that they feared for their safety because of the impunity of the corrupt officials that they faced. Consistent with these statements, INT investigators found a pattern of inconsistent bidder prequalification results, suggesting that the prequalification process may have been abused. Companies were disqualified for reasons that were invalid on the face of their submissions, for example, for vague reasons such as failure to "fit the contract profile."

POST-INVESTIGATION ACTIVITY

Beginning in 2006, while its investigation was ongoing, INT began discussions with the Philippines Office of the Ombudsman about NRIMP after consultations with the Department of Finance. At the close of INT's investigation in November 2007, the Bank formally referred INT's investigative findings, and investigation-related allegations, to the Department of Finance, which is the Bank's official counterpart in the Philippines under the Bank's Articles of Agreement, and the Ombudsman's Office, which was designated by the Department of Finance as the appropriate national investigative authority. As evidence indicated that some companies based in other countries were involved in the cartel, INT is sharing its investigative findings, and investigation-related allegations, with the Ministries of Finance and national investigative authorities of those companies' home countries. In May 2008, the World Bank issued Notices of Sanctions Proceedings to companies that evidence indicated had engaged in sanctionable practices when bidding for the NRIMP-1 Contracts. Each company had 90 days to submit a response in its defense and contest the allegations against it, as well as to request a hearing before the Bank's Sanctions Board. In November 2008, the Sanctions Board held a hearing on the case. Following a review of the evidence that took into account all of the companies' submissions, on January 14, 2009, the World Bank announced the debarment of seven companies and one individual for engaging in collusive practices under NRIMP. This followed the August 2008 debarment of an additional firm that did not contest the Bank's imposition of sanctions upon it.