



## Government Procurement in Economic Partnership Agreements and FTAs

### Introduction

The ability of governments to procure from firms of its own choice can be an important development tool and can also be an instrument for macroeconomic management. Providing preferences to local producers of goods and suppliers of services and set-asides may be part of an industrial policy or an instrument to attain social objectives and can have immense implications for

national development, local business and job creation.

This Policy Brief analyses the scope of international trade rules governing government procurement in the European Union's Economic Partnership Agreements (EPAs) and Free Trade Agreements (FTAs) with developing countries, the key provisions of EPAs regarding this topic and its potential implications for development.

### Executive Summary

The ability of governments to procure from firms of its own choice can have immense implications for national development, local business and job creation and can be an important development tool. Government procurement remains one of the few areas of state involvement not covered by any multilateral agreement. It is, however, an area which is increasingly being negotiated and discussed in Free Trade Agreements (FTAs).

The development challenges that will result from liberalising public procurement in these FTAs /EPAs for developing countries include: (a) the prohibition of the use of preferences for national suppliers as a policy instrument, (b) high costs of compliance with transparency rules and insufficient support to overcome institutional and supply capacity constraints and (c) the asymmetric capacities of the EU compared to its developing country partners, with the result being that only the EU benefits from these disciplines. In the process, developing countries would have lost the opportunity to use regional procurement markets to develop industrial and services supply capacities in their sub-regions.

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### I. Importance of Government procurement for developing countries

Government Procurement refers to the purchasing activities of government controlled activities. It comprises the expenditures of government on goods and services (including projects such as building of schools, roads, dams and industrial complexes, excluding personnel costs). In some developing countries, government procurement could account for 15 to 30 percent of the GNP<sup>1</sup>.

The ability of governments to procure from firms of its own choice and to provide preferences to local producers of goods and suppliers of services may be part of policy instruments to attain social objectives, to pursue an industrial policy or an instrument for macroeconomic management. Thus, government procurement can have immense implications for national development, local business and job creation and can be an important development tool.

Joseph Stiglitz, former chief economist at the World Bank, referred to it in the following manner: "Government procurement policies have important economic and social roles in developing countries which could be curtailed if governments were mandated to observe national treatment principles. The level of expenditure and the attempt to direct the expenditure at local producers is a major macro economic instrument, especially during recessionary periods, to counter economic downturn. Additionally, procurement policy might be used to boost domestic industries or encourage development in specific sectors of national interest. Social objectives could also be advanced by preferences for specific groups or communities, especially those that are underrepresented in economic standing"<sup>2</sup>.

### II. International trade rules regarding government procurement

At the level of the World Trade Organization (WTO) disciplines related to Government Procurement apply to a limited number of members. The plurilateral Agreement on Government Procurement (GPA) is currently applicable to 13 WTO members (counting the European Union as one). Most developing countries are not parties to this agreement. Some OECD countries such as Australia and New Zealand are also not parties to this Agreement.

The GPA includes disciplines aimed at guaranteeing that access to procurement is available to foreign products, services and suppliers in a non-discriminatory manner. It places considerable emphasis on procedures for providing transparency of laws and regulations. It applies not only to purchases by national and local government entities but also to entities at the sub-federal level and to contracts above specified threshold values.

After the WTO's Ministerial Conference in Singapore (1996), the possible launch of negotiations for a multilateral agreement on government procurement at WTO was discussed. During this debate, the EU emphasized the need and benefits of provisions aimed at ensuring transparency on public procurement. For the EU, transparency meant "ensuring that information on procurement policies, rules practices and opportunities were made available to all interested parties, particularly potential suppliers and services providers"<sup>3</sup>.

To many, the EU objective in pursuing transparency was to gently minimise resistance towards more offensive market access measures in the future<sup>4</sup>. The US, too, had a similar agenda. The then acting US Trade Representative (Charlene Barchefsky) declared, in 1996: "The study on procurement was intended to be the first step toward an agreement on transparency practices in government. This initiative will, as we continue to push it, help create an environment where business can expect a fair share in competing contracts with foreign governments"<sup>5</sup>.

Including transparency in government procurement in the WTO's Doha Round was rejected by the majority of developing countries at the WTO's 2003 Ministerial in Cancun. Most developing countries opposed the idea of such a multilateral framework on the following grounds:

- Lack of institutional, regulatory and administrative capacity to respond to the requirements by a potential agreement and to conduct procurement as per some of the proposed provisions. Several developing countries strongly supported that implementation of any potential agreement should only take place after assistance to capacity building is in place.
- Potential conflict with internal legislations and procurement methods.

- Potential loss of sovereignty in case dispute settlement instruments provided the possibility of appealing decisions made by domestic review systems.

Thus, currently no multilateral rules have been agreed at the WTO with respect to (a) the treatment of foreign providers of goods and services to public entities and (b) procedures relating to public tendering of contracts.

However, rules governing government procurement are increasingly being included in Free Trade Agreements (FTAs). These rules generally require developing countries to open their government procurement markets to foreign firms.

<b>Scope of rules generally included in Economic Integration Agreements</b>	
<b>Obligations</b>	<b>Scope of rules</b>
<ol style="list-style-type: none"> <li>1. Non discriminatory treatment</li> <li>2. Valuation of contracts</li> <li>3. Technical specifications</li> <li>4. Procurement methods</li> <li>5. Qualification of suppliers</li> <li>6. Invitations to participate</li> <li>7. Time limits</li> <li>8. Tender documentation</li> <li>9. Award of contracts</li> <li>10. Provision of information</li> <li>11. Challenge procedures</li> </ol>	<ol style="list-style-type: none"> <li>1. Fair and open procurement procedures, transparency, accountability and due process</li> <li>2. Key principles to determine the value of contracts</li> <li>3. To avoid unnecessary obstacles to trade</li> <li>4. To specify methods and procedures that can be used</li> <li>5. Essential criteria to ensure fulfilment of contract</li> <li>6. Requirement for publication of tender notice</li> <li>7. Minimum period of time for allowing suppliers to prepare and submit tenders</li> <li>8. Requirements related to the time for allowing suppliers to prepare and submit tenders</li> <li>9. Rules regarding award criteria and information of results to suppliers</li> <li>10. Requirement to publish laws, regulations, decisions, rulings and other procedures relating to government procurement</li> <li>11. Requirement to allow recourse to an impartial body to review complaints</li> </ol>

Source: WTO. Government Procurement-related provisions in Economic Integration Agreements. Documents S/WPGR/W/49, 31 Aug 2004

Agreements also generally include differentiated commitments on the basis of thresholds values. These thresholds often differ between types of entity and also vary between goods, construction services and other services. Thresholds are generally higher for construction services than other services<sup>6</sup>.

### III. Motivation and Rationale of the EU for Disciplines on Government Procurement in FTAs

Government procurement was identified as a priority area in the European Commission's "Global Europe Strategy"<sup>7</sup>. This strategy aims at maintaining the competitiveness of Europe in the global market by securing new and profitable markets for EU companies through FTAs.

In FTAs, the EU generally includes (a) enhanced provisions on market access in goods and services and (b) binding provisions on regulatory transparency in areas relevant for trade and investment, including government procurement.

For example, in the case of FTA negotiations between the EU and India, and EU and ASEAN, provisions on public procurement include:

- Progressive liberalization of procurement markets at the national, regional and, where appropriate, local levels.
- Binding rules on adequate transparency that support so-called "effective" procurement systems.
- Procedures to challenge contracts that have been awarded, and cooperation in the field of electronic procurement.
- That to the extent appropriate, the procurement chapter should be consistent with the GPA.

The opening up of public procurement abroad is believed to hold "enormous untapped potential" for the EU. This is because, according to the EU, some practices identified in partner

countries impede the participation of EU suppliers and exclude them from important exporting opportunities. Hence, disciplines on the government procurement regulatory environment in third countries have become important for the EU.

To cite an example, the EU's market access database<sup>8</sup> states that in relation to India, "discrimination" in this country's procurement practices and particularly targets the energy and port maintenance contracts for favouring local companies.

Sectorally, European interests are in the areas of construction works, services relating to architecture, law, accounting and construction business, medical and pharmaceutical devices and services and office and computing equipment. These sectors account for 50 per cent of government procurement in the EU.

The draft mandates for the EU Association Agreements with the Andean Community and Central American nations and India confirm the importance of government procurement. In the former, the EU is targeting water, energy, transport and the information and communication sectors<sup>9</sup>. For Central America, the priorities are water, energy and transport.

### IV. Key Provisions of EPAs Regarding Government Procurement

At the end of 2007, some ACP countries initialled Interim EPAs with the European Union and one comprehensive EPA was signed with CARIFORUM. Amongst other topics, the latter contains detailed provisions regarding public procurement. Although the Interim EPAs do not include commitments on government procurement, the ACP countries are likely to come under pressure in the negotiations towards comprehensive EPAs to make commitments in this area in the future.

The main provisions on Government Procurement contained in the EPA negotiated between CARIFORUM and the EU include:

- National treatment (art. 167), i.e. the obligation not to discriminate against EU companies that have a commercial presence in a CARIFORUM state. That is, countries cannot give preferences to local suppliers and exclude locally established foreign suppliers or affiliates.
- Progressive liberalization based on positive listings of purchasing entities. This list contains central government organs and is applicable to procurement over certain thresholds (contained in Annex 6). In addition, art 167A.4 states that a decision by the Joint CARIFORUM-EC Council may specify other types of procurement covered by national treatment.
- Transparency provisions. The EPA text requires publication of all laws, regulations, decisions, as well as all administrative and judicial rulings related to procurement. This obligation includes, for instance, publication in officially electronic media, within a reasonable period of time and creation of an online facility to further the effective dissemination of tendering opportunities. The EPA text provides for a transition period limited to 5 years to complete implementation, in the case of less developed countries.
- Technical specifications. The EPA text requires the use of agreed international standards. In practice, this means that some form of discretion will still remain, because purchasers must decide whether existing international or national standards are adequate.
- No Special and Differential Treatment (SDT) provisions. There is no explicit exemption from national treatment commitments on development grounds. The EPA text therefore appears to be less generous than the GPA.
- Few and weak provisions on technical cooperation. Article 182 provides for exchanges of experiences, the establishment of appropriate systems to ensure compliance and the creation of an online facility at the regional level.
- Exceptions. Security-related purchasing is excluded from future liberalization.

## V. Implications for development

The stated aim of EU-ACP trade relations is to “foster the smooth and gradual integration of the ACP states into the world economy, promoting their sustainable development and contributing to poverty eradication”<sup>10</sup>. However, the structure and content of EPA negotiations have raised concerns about the impact of these agreements on ACP countries and their efforts towards poverty eradication, economic growth and regional integration.

Potential development implications of including provisions on procurement in the EPAs include (a) the prohibition of the use of preferences for national suppliers as a policy instrument and (b) costs associated with compliance with transparency rules and (c) deepening dependency in the European market, to the detriment of regional markets.

One of the reasons why ACP states have not signed the GPA is the desire to retain preferences in procurement as an industrial or development instrument. In this sense, commitments on national treatment envisaged under the CARIFORUM EPA text are contrary to this, as they entail the loss of the right to provide preferences to local suppliers.

Another reason for not signing the GPA is that ACP states believed compliance costs are excessive. According to Professor Stephen Woolcock, government procurement transparency provisions contained in the EPAs are likely to entail high compliance costs as many ACP states have not completed domestic reforms based on the UNCITRAL model<sup>13</sup>.

Several studies that surveyed policy reforms in developing countries’ government procurement<sup>14</sup> have concluded that the lack of trained professionals and lack of regional regulatory capacity are major challenges in the area of government procurement. It is therefore not surprising that the need for adequate support and assistance to implement transparency rules

related to government procurement was highlighted repeatedly during discussions held in the now defunct WTO committee on Transparency in Government (WTO, 2003).

EPAs are supposed to promote regional integration in the ACP regions and the EPA text on procurement supposedly encourages the creation of regional procurement markets by requiring the adoption of common rules on procurement within regions. However, given the supply constraints of ACP industries and suppliers, once liberalized, it is more likely that ACP procurement markets will be flooded by EU suppliers, hence destroying prospects for closer intra-regional cooperation.

Similarly, ACP suppliers have limited capacities to compete in government procurement markets of the EU. Hence, opening up government procurement at this stage will bring real exporting benefits only to the developed partner under the EPA.

## VI. Conclusion

The ability of governments to procure from firms of its own choice can have immense implications for national development, local business and job creation and can be an important development tool.

Currently, no multilateral rules have been agreed at the WTO with respect to (a) the treatment of foreign providers of goods and services with respect to public procurement and (b) procedures relating to the public tendering of contracts. However, the liberalization of government procurement markets is increasingly being negotiated and discussed in FTAs.

The desire to retain preferences in procurement as an industrial or development instrument is at the core of understanding the opposition of developing countries to a multilateral framework on Government Procurement. The main reasons why developing countries refused to agree to a multilateral framework on trans-

parency in government procurement in 2003 were: (a) the lack of institutional, regulatory and administrative capacity and (b) potential conflict with internal legislations and procurement methods and (c) potential loss of sovereignty in relation with dispute settlement instruments.

From a European perspective, disciplines pertaining to the regulatory environment on government procurement in third countries have become an important goal to pursue in FTAs, in accordance with the "Global Europe Strategy". The objective is to tap into the enormous potential of access to procurement markets in emerging developing countries, creating a "friendly" environment for business to compete in the award of contracts. European sectoral interests include: construction works, services relating to architecture, law, accounting and construction business, medical and pharmaceutical devices and services and office and computing equipment.

Key provisions on government procurement in the CARIFORUM EPA include commitments with respect to national treatment, progressive liberalization of ACP countries' procurement markets, comprehensive transparency obligations, technical specifications, the absence of Special and Differential Treatment (SDT) provisions and few and weak articles on technical cooperation.

The development challenges of these provisions for developing countries include:

- (a) The inability to favour local producers over foreign ones. Giving the market to local companies can be an important instrument for industrialization, employment, macroeconomic stability, and affirmative action.
- (b) The high costs associated with compliance with transparency rules and inadequate support provided within the EPA/FTA framework to overcome the lack of institutional and regulatory capacities.
- (c) The asymmetric capacities of both partners so that liberalization benefits only the EU. Any possible strengthening of regional supply capacities by suppliers benefiting from regional procurement markets would also have been lost.

## End Notes

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