Chapter 13

GOVERNMENT PROCUREMENT

1. OVERVIEW OF RULES

Economic Aspects and Significance

Government or public procurement is the purchase, lease or rental of products and services by government entities. The size of the government procurement market and its share of the economy differs from country-to-country, but estimates generally place it between 10 percent and 15 percent of GDP. Therefore, procurement laws that discriminate against foreign suppliers distort the international flow of products and services, which worsens as the economic importance of services and soft industries increases.

National security is one reason offered for policies that favour domestic products in government procurement. However, these policies are also commonly enacted to promote industrial policy, *i.e.*, to protect specific industries. Discrimination between domestic and foreign suppliers in government procurement will, in the short run, help countries achieve their industrial policy objectives, but ultimately creates an arbitrary barrier to fostering a fully competitive environment. For entities procuring goods, restrictive policies will prevent them from buying the best possible goods and services at the lowest possible price and will, therefore, prevent the government budget from achieving maximum utility. For suppliers, procurement restrictions mean that domestic industries are given excessive protection, creating disincentives for the protected industries to improve the ways in which they conduct business or develop new products. Such policies, therefore, weaken suppliers.

Given that the size of the government procurement market is quite large, when procurement protection is linked to policies that protect domestic industry, disciplines on subsidies become meaningless; such protection ultimately causes palpable distortions

to the free-trading system. Policies that accord preference to domestic products in government procurement are without question detrimental to one's own economy, as well as to world trade.

Background of Rules

Governments tend to favour procurement of their own country's goods and services for reasons ranging from national security to the promotion of domestic industry. The negotiators of the GATT were aware of this reality and through Article III: 8(a) exempted government procurement from the requirement of national treatment.

However, as discussed in this chapter, discrimination against foreign products in procurement procedures can exist in a variety of ways, including: (1) expressly prohibiting foreign companies from tendering bids for government procurement contracts; (2) giving preferential treatment to companies that agree to use substantial amounts of domestic merchandise in the execution of government contracts; and (3) imposing conditions and requirements on bidders for the purpose of shutting out foreign companies and promoting domestic industry.

The Kennedy Round of GATT negotiations first recognized that the use of procurement procedures to protect domestic industries constituted a major non-tariff barrier. As the growing volume of government procurement transactions became increasingly important to the world economy, the major contracting parties to the GATT realized a need to establish rules and disciplines. As a result, in 1979, under the Tokyo Round, the Agreement on Government Procurement (hereinafter "the 1979 Agreement") was concluded and required national treatment and most favoured nation status, as well as fair and transparent procurement procedures. The 1979 Agreement subsequently was partially amended in 1987.

Additional negotiations to revise the 1979 Agreement were initiated with a view toward improving the text of the Agreement and to expand its coverage. These negotiations and the WTO Agreement were concluded simultaneously in December 1993. The new Government Procurement Agreement (hereinafter "the 1994 Agreement") was signed in April 1994 at Marrakech and took effect January 1, 1996.

2. LEGAL FRAMEWORK

The 1979 Agreement applied mainly to the central government and only to those entities designated by each party. The designated entities were listed in an Annex to the 1979 Agreement.

Because of these restrictions, the 1979 Agreement did not cover a large percentage

of government procurement contracts and parties to the 1979 Agreement became especially anxious to have the scope expanded to cover service transactions. Because service transactions have become so important to the world economy, their exclusion has led to numerous problems. Parties to the 1979 Agreement also became interested in expanding the range of entities subject to the 1979 Agreement. To resolve these and other related issues, negotiations on government procurement were held in conjunction with the Uruguay Round. On December 15, 1993, negotiators reached a new Agreement that covered the procurement of services and the procurement by sub-central government entities and government-related entities.

As was the case with the 1979 Agreement, participation in the 1994 Agreement is voluntary. As of January 1, 2007, only 13 countries and regions are parties to the Agreement: Canada, Hong Kong (China), the EU[1], the Republic of Korea, Israel, Japan, Liechtenstein, Netherlands (with respect to Aruba), Norway, Singapore, Switzerland, the United States, and Iceland. Bulgaria, Jordan, the Kyrgyz Republic, Panama and Chinese Taipei are negotiating their accession to the Agreement.

We look forward to the broad participation of developed countries in the future and anticipate that many countries, including developing countries, will participate in the Agreement.

Elimination of Non-application

The extent to which the 1994 Agreement applies to procurement by entities of each party to the Agreement is specified in Appendix I to the Agreement, which is divided into five Annexes. Figure 13-1 contains a summary of the concessions offered by the “Quad” countries and Korea. A complete agreement, however, has not been reached on procurement by sub-central government entities and government-related entities. For example, the United States initially stated in its Annex that the 1994 Agreement would not apply to its sub-central and government-related entities unless it received commensurate offers from Japan, the European Union and Canada. The European Union expressed similar reciprocal reservations.

The United States and the European Union continued negotiations, reaching an agreement to expand their offers on April 13, 1994. This agreement eliminated mutual non-application between them to some extent, and called for the necessary amendments to be made to their Appendices. Japan and the United States initially decided that the 1994 Agreement would not apply to sub-central government entities or government-related entities. However, the two countries reached an agreement to eliminate most of the mutual non-application between them, and their Appendices were revised accordingly in February 1996. The United States and Norway agreed to eliminate

[1] The agreement should also apply to Romania and Bulgaria, which became EU members in January 2007. Procedures are currently in motion to make this addition to the EU Agreement ANNEX.

mutual non-application in specific areas in July 1996 and the United States and Switzerland agreed to do so in May 1997. While negotiations are reducing the partial non-applicability provisions among the major countries, partial non-application of the Agreement still remains. This partial non-application remains an exception to the principle of non-discrimination prescribed in the Agreement. Japan hopes to see a full agreement applicable to procurement by sub-central and government-related entities soon.

Figure 13-1

Outline of Concessions by the "Quad" Countries and Korea under the 1994 Government Procurement Agreement

[Entities]

	Central government entities	Sub-central government entities	Government-related entities
Japan	All central government entities (including legislative and judiciary entities)	47 prefectures and 12 designated cities	73 special corporations and 66 independent administrative institutions
US	All central government entities	37 states	TVA, 5 power marketing administrations of the Department of Energy and the St. Lawrence Seaway Development Corporation (11 entities total)
EU	All central government entities (including the Council of the European Union and the European Commission)	All sub-central government entities (including municipal-level entities)	Entities in the water, electricity, urban transport, port and airport sectors
Canada	All central government entities (including some judiciary entities but excluding legislative entities)	No offer	9 Crown Corporations
Rep. of Korea	Almost all central government entities	15 Sub-central governments including Seoul Special City	19 entities including Korea Development Bank

Notes:[1] Under the agreement between the United States and Japan, each country eliminated most of the partial non-application provisions pertaining to sub-central and government-related entities in February 1996.

[2] Canada did not offer to cover its sub-central government entities and sub-central government- related entities. Therefore, partial non-application between Canada and three countries (the European Union, the United States, and Japan) continues to exist.

[Threshold values] (Unit: SDR 10,000)

		Japan	US	EU	Canada	Korea
Products	Central government entities	13	13	13	13	13
	Sub-central government entities	20	35.5	20	35.5	20
	Government-related entities	13	18.2 (40)	40	35.5	45
Services (excluding construction services and architectural, engineering and other technical services)	Central government entities	13	13	13	13	13
	Sub-central government entities	20	35.5	20	35.5	20
	Government-related entities	13	18.2 (40)	40	35.5	45
Construction services	Central government entities	450	500	500	500	500
	Sub-central government entities	1500	500	500	500	1500
	Government-related entities	1500 (450)	500	500	500	1500
Architectural, engineering and other technical services	Central government entities	45	13	13	13	13
	Sub-central government entities	150	35.5	20	35.5	20
	Government-related entities	45	18.2 (40)	40	35.5	45

Notes: [1] Under an April 1994 agreement between the United States and the EU, the United States decreased the threshold for government-related entities except in the area of construction services from 400,000 SDR to 182,000 SDR. (However, the threshold for the Port Authority of New York and New Jersey, the Port of Baltimore and the New York Power Authority remains at 400,000 SDR.)

[2] With respect to procurement below the threshold values specified in the 1994 Agreement, Japan voluntarily requires non-discrimination and transparency for procurement of goods and services worth 100,000 SDR or more by central government entities and government-related entities.

[3] Japan decided that the threshold for Independent Administrative Institutions for construction services was 4,500,000 SDR and that Note 3 to ANNEX 3 would not apply to the above-mentioned Institutions.

[4] SDR 10,000 converts to approx. 13,000 US dollars.

[5] "Architectural engineering and other technical services" refer to services related to "Construction services", engineering services and other technical services.

Reinforcement by the 1994 Agreement

The negotiations on government procurement provided a good starting point for further progress. Importantly, the negotiations expanded the coverage of the 1979 Agreement. In addition, the negotiations produced a much-improved 1994 Agreement, most notably by breaking it down into 24 articles instead of the nine articles contained in the 1979 Agreement and adopting stronger disciplines. As is the case with the 1979 Agreement, the 1994 Agreement defines the principles of national treatment and non-discrimination and requires fair and transparent procurement procedures. The 1994 Agreement reinforces and improves the 1979 Agreement in the following aspects:

(a) Expansion of Coverage

The Agreement expands coverage to include procurement of services and procurement by sub-central government entities and government-related entities. As coverage of the Agreement expanded, necessary changes were also made to the text. In the Appendix to the Agreement, each member specifies services and entities subject to the Agreement.

(b) Challenge Procedures

Under the Agreement, parties must hear the complaints of suppliers that suspect government procurement procedures are violating the Agreement; a court or an impartial and independent institution must review complaints submitted. If a violation is found, correction of the breach of the Agreement, compensation for damages, and other remedial measures shall be provided, according to the Agreement. Japan has created an Office of Government Procurement Review within the Prime Minister's Office to handle complaints concerning government procurement. The Chief Cabinet Secretary chairs the new agency. After establishing detailed procedures for the handling of complaints, Japan formed a Government Procurement Review Board consisting of experts in the field to serve as the complaint resolution body. (For example, in December 2005, U.S. Overseas Bechtel Incorporated filed a complaint involving construction of company apartments by the East Japan Railway Company. The complaint committee investigated the case following the aforementioned procedures and rejected the complaint in January 2006. The committee stated: "The relevant procurement organization (JR-East) has already become a completely private company and should be excluded from this Agreement. However, it should be considered as subject to this Agreement, as long as it is included in the Agreement ANNEX". The Committee also deemed it appropriate that JR-East had required engineers with experience and performance of similar construction as a condition for bidding, when

considering the peculiarities of the construction.) Sub-central entities also have their own procurement review procedures.

(c) Dispute Settlement Procedures

The Agreement requires that disputes be settled in accordance with the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU). There are, however, several departures from normal DSU procedures. First, given the time-sensitive nature of government procurement tenders, the Agreement requires that an effort be made to shorten the panel review period as much as possible. Second, the Agreement does not allow cross retaliation under any circumstances. (Normal DSU procedures allow for cross retaliation if one can show that retaliation in the same area would not be effective.)

(d) Reduced Obligations for Sub-Central and Government-Related Entities

The Agreement allows sub-central and government-related entities to use simplified procedures in a request for tender and to maintain lower statistical reporting obligations than central-government entities. This has the effect of reducing the burden on sub-central and government-related entities to which coverage has been newly extended.

(e) Privatization of Entities

Procedures have been established for withdrawing privatized entities from the Appendix of the Agreement. The entity is automatically withdrawn from the Appendix if the Committee on Government Procurement is notified of the withdrawal and no objection has been made. Should there be an objection, it will be settled under the procedures described in section (c) above. We note that a *quid pro quo* is not necessarily required for a modification to the Appendix. In other words, the party is not obligated to offer a new entity of similar size in exchange for the one withdrawn.

However, since “privatization” is not clearly defined in the Agreement, some problematic cases have arisen in which factually privatized entities could not be withdrawn from the coverage of the Agreement due to the objections by some countries. (For example, all stock of the East Japan Railway Company (JR East Japan) and West Japan Railway Company (JR West Japan) held by the Japanese Government was sold off to private entities. However, the European Union has not withdrawn its objections against the exclusion applicable to both companies under the Government Procurement Agreement.) Thus, the definition of privatization and the EU withdrawing its objections is being discussed in current negotiations focusing on a review of the Agreement.

(f) Offsets

The practice of offsets in government procurement (requiring local content, technology transfers, investments or counter trades in exchange for award of contracts) is, in principle, prohibited under the 1994 Agreement. The 1979 Agreement did not necessarily prohibit these practices.

Expansion of the Coverage of the Agreement

Article III:8(a) of the GATT (national treatment) exempts government procurement in principle.[2] The 1994 Agreement, despite its expanded coverage, still does not cover all government procurement practices; some reciprocal exemptions exist, and the coverage of the agreement is not necessarily clear due to the fact that, with respect to the EU, detailed individual names of agencies subject to agreements are not recorded in the Annex. Therefore, there are some areas in which neither the GATT nor the 1994 Agreement will apply. Specifically, these areas address procurements below the thresholds set out in the 1994 Agreement and procurements by sub-central and government-related entities not bound by the Agreement.

3. RECENT DEVELOPMENTS

(a) The Ongoing Work to Amend of the 1994 Agreement

Article XXIV:7(b) of the 1994 Agreement mandated that new negotiations begin within three years from the date of entry into force of the Agreement. In accordance with these provisions, the Committee on Government Procurement began negotiations during 1997 to: (1) improve and simplify the Agreement (introducing information technology where appropriate); (2) eliminate discriminatory measures and practices that distort open procurement; and (3) expand the coverage of the Agreement.

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[2] Article XVII:2 of the GATT provides, however, that with respect to "imports of products for immediate or ultimate consumption in governmental use," which are not subject to the Government Procurement Agreement, each Member shall accord to the trade of the other Members "fair and equitable treatment," even though it may not accord non-discrimination treatment. This Article can be interpreted to obligate each contracting party to accord "fair and equitable treatment" with respect to government procurement.

This GATT provision was established based on US suggestions. The phrase "fair and equitable treatment" was adopted because it is not possible to apply non-discrimination treatment to government procurement with the same precision that is possible in the case of other regulatory measures. Nevertheless, in the future, Japan would like to see more areas covered by the Government Procurement Agreement.

Work is proceeding on these three issues simultaneously. For the first goal (improvement and simplification) a draft work plan was created in June 1998 that sought to complete negotiations by the third WTO Ministerial Meeting that was held in Seattle in December 1999. The Committee continuously considered this plan, but was unable to agree on the details. Following this, in February 2002, although the Government Procurement Committee agreed on an action plan to conclude negotiations by January 1, 2005, an agreement was not reached by the deadline. The continued discussions in 2006 have increased the possibility of concluding negotiations for revisions during 2007. As for points (ii) and (iii), above, these issues are currently being discussed together and in July 2004, members agreed on a modality (a negotiation framework) to conclude the discussions by January 2006. Under this modality, each member was supposed to make a request regarding the expansion of coverage of the Agreement to other members by the end of November 2004, make an initial offer to expand their nation's coverage by May 1, 2005, and then start bilateral negotiations based on the request-offer procedure. Since December 2004, nine countries (Japan, the United States, the EU, Canada, Norway, Hong Kong, Singapore, South Korea and Switzerland) have submitted an initial request, but submission of offers has been delayed. Initial offers were submitted by the EU in November 2005, by the United States and Canada in December 2005, and by Japan and South Korea in January 2006. Bilateral negotiations started in February 2006.

(b) Laying the Groundwork for an Agreement on Transparency in Government Procurement

The 1994 Agreement requires high levels of discipline and imposes procedural burdens on participating governments that keep developing countries from joining. While signatories to the 1994 Agreement see expanding their numbers as an important goal, they are also aware that a significant expansion is not realistic over the short term. Nonetheless, it is still desirable, in light of the importance of government procurement to the world economy, that as broad a number of WTO Members as possible adopt appropriate disciplines for government procurement. Among these disciplines, transparency is of vital importance since it assures procurement opportunities by applying such fundamental principles as national treatment. To that effect, a new agreement, which is limited to assuring transparency and does not contain the detailed provisions of the 1994 Agreement, may enjoy wide participation from developing countries.

Therefore, while advocating expansion of the 1994 Agreement as a long-term goal, Members proposed in October 1996 that a new agreement on transparency should be drafted that might be acceptable to all WTO Members, including developing countries. During the Singapore Ministerial, a working group to explore how such an agreement might be drafted was established. In 1997, the working group began to discuss transparency elements and has worked towards formulating a new agreement. An initial target for completing discussions was the third Ministerial Conference held in Seattle in December 1999. However, no agreement on the details was reached and the Working Group has continued discussions.

Developing countries have traditionally been very cautious about establishing new procurement disciplines, but some have begun to realize the need for an agreement of this type. Accordingly, the November 2001 Ministerial Declaration issued at the Fourth Ministerial Conference in Doha included an agreement by Members to consider negotiating modalities for a multilateral agreement on transparency in government procurement, keeping in mind the need for enhanced capacity building in developing countries. However, members failed to agree on negotiating modalities by the Fifth Ministerial Conference in Cancun in September 2003. At the General Council meeting in July 2004, Members agreed on negotiating modalities to continue the discussions but not on a negotiating agenda. The working group on transparency in government procurement has not met since 2003.

4. MAJOR CASES

Procurements which fall outside the scope of covered entities, as set forth in each country's Agreement on Government Procurement, can obviously not be considered to violate the Agreement. The United States and other countries, for example, engage in practices, which, while not in violation of the Agreement on Government Procurement, generally contravene the spirit and intent of the Agreement. These practices are examined below.

THE UNITED STATES

1) Myanmar Sanctions Law (The Massachusetts Act of June 25, 1996 Regulating State Contracts with Companies Doing Business with or in Burma (Myanmar)(DS88(95))

In June 1996, the Commonwealth of Massachusetts passed a law prohibiting the ability to contract with companies doing business in Burma (Myanmar). The law excludes from state agency procurement: (1) companies that have a principal place of business in Myanmar or who otherwise conduct business in Myanmar, including any majority-owned subsidiaries of such companies; (2) companies providing financial services to the Government of Myanmar; (3) companies promoting the importation or sale of gems, timber, oil, gas or other related products from Myanmar (trading in all is largely controlled by the Government of Myanmar); and (4) companies providing any goods or services to the Government of Myanmar. Under the law, the state government created a "restricted purchase list" of companies that meet these criteria. Companies on the list are, in principle, barred from bidding on state contracts, or when allowed to bid, less favorable terms are imposed on them than companies not on the list. There were

350 companies on the list, 50 of which were Japanese.

The Commonwealth of Massachusetts is included among the 37 state governments listed by the United States under the 1994 Agreement on Government Procurement. The law is likely in violation of Article VIII, which mandates the qualification of suppliers, and Article XIII:4, which contain bidding standards. In addition, the state government discriminates between companies depending on whether they are on the list, which may also be inconsistent with Article III:1 of the 1994 Agreement, which mandates both national treatment and non-discrimination.

Japan repeatedly expressed its concerns about the apparent inconsistency of this state law with the Agreement on Government Procurement, and in March 1997 requested further information under the terms of the Agreement. Japan repeatedly asked the United States to expedite its answers on Agreement-consistency and its provision of further information, but the government of the United States failed to respond in good faith on this matter. The EU shared many similar concerns with Japan on this issue. The EU and Japan requested consultations with the United States in June and July 1997, and during 1997 three consultations were jointly conducted.

Subsequently, Japan decided — in light of the situation in the United States, the schedule of the Massachusetts state legislature, and the apparently positive attitude of the country — to observe the US actions. No progress was made, however, leading Japan and the EU to jointly request the establishment of a WTO panel in September 1998. This panel was established in October, but subsequent litigation within the United States (described below) declared the law unconstitutional and void, so Japan and the EU took procedures to suspend the panel in February 1999. On February 11, 2000, the authority of the panel lapsed because Article 12.12 of the Dispute Settlement Understanding (DSU) voids panels that have been suspended for more than twelve months.

Apart from the WTO panel, a private US organization, the National Foreign Trade Committee (NFTC), filed a suit in federal court on April 1, 1998, claiming that the state law conflicted with the US Constitution. In November 1998, the federal district court decided that the law was indeed unconstitutional and declared it null and void. The Commonwealth of Massachusetts appealed the decision and filed a motion for stay pending appeal, but in June 1999 the federal appeals court upheld the decision of the district court. Massachusetts appealed to the US Supreme Court, but the Supreme Court in June 2000 affirmed the lower courts' findings that the Massachusetts law was unconstitutional.

One problem is that many US states and local governments have imposed or are considering sanctions similar to those enacted by Massachusetts. Most of these sanctions take the form of restricting government procurement from companies that have business dealings with the sanctioned countries. We are pleased that the US Supreme Court found the law unconstitutional because the ruling will eliminate the barriers for private companies from trade-related legislation passed by individual states. The Supreme Court bases its ruling on the principle that foreign relations is an area

specifically reserved to the federal authority and state laws that impinge upon this authority are unconstitutional. The ruling will act as a restraint on future state-level legislation.

In some cases, however, the state or local government will not be bound by the obligations of the Agreement on Government Procurement because it was not included in the "offered" institutions, although many of the measures themselves are likely to constitute violations. We should pay close attention to whether these measures will be eliminated or amended in the United States.

In the meantime, the US Federal Government established a law in July 2003 that bans imports from Myanmar and freezes their assets in the United States until Myanmar's military regime improves human rights policies and adapts democratic policies. This calls for close observation in the future.

2) National Security Exceptions

Article XXIII of the 1994 Agreement states that any party may take such measures as warranted by national security concerns. This Article permits any party to use national security as a reason to refuse foreign tenders. The same provision was contained in Article VIII of the 1979 Agreement. The 1994 Agreement does not contain any clear standards as to the kind of cases in which national security exceptions may apply.

It is common for the United States to use national security as a reason for excluding contracts from open, competitive tendering procedures. Domestic law states that US security may not be compromised by disclosing an agency's needs to persons who do not have access to classified information. It also states that products must be procured from domestic enterprises so as to preserve the US industrial mobilization base and to ensure that the United States does not have to rely on foreign products in times of emergency.

(a) Federal Acquisition Regulations (FAR)

FAR provides general rules on US government procurement. It provides for full and open competition in the acquisition process. (The Buy American Act is still applicable, though.) FAR, however, allows exceptions from those procedures for contracts: (1) when it is necessary to award the contract to a particular source or sources and keep a facility, producer, manufacturer or other supplier available for furnishing certain supplies or services in case of a national emergency or to achieve industrial mobilization; or (2) when the disclosure of the agency's needs would compromise national security (unless the agency is permitted to limit the number of sources from which it solicits bids or proposals).

(b) Department of Defence FAR Supplement (DFARS)

DFARS is a supplement to FAR that may exclude foreign companies from defence contracting. Under DFARS, no Department of Defence contract under a national security program may be awarded to a company owned by an entity controlled by a foreign government if access to proscribed information is required for that company to perform the contract.

(c) Clinger-Cohen Act (The Information Technology Management Reform Act of 1996)

This law took effect February 2, 1996, and abolished the Brooks Automatic Data Processing Act. The aim of this law is to promote the efficient federal procurement of goods and services in the area of computer and telecommunications equipment and support. Authority for all procurement in this sector is granted to the Office of Management and Budget and other federal agencies; the Act does not apply to national security-related procurement by the Department of Defence or Central Intelligence Agency. The contracting officer of each agency makes the decision on whether security exceptions apply. It is difficult to ascertain whether those decisions are consistent with the Agreement.

The possibility remains that security exceptions could be employed arbitrarily to unfairly limit foreign companies' access to the US government procurement market. It would be appropriate to clarify the principles under which national security exceptions are granted and to ensure their uniform application.

In addition, management and operation of research and development facilities under the Department of Energy, NASA and the Department of Defense are often entrusted to private companies and universities under "Management and Operating Contracts" (M&O Contracts). Because many of these facilities began as nuclear weapons development centers, they are considered security exceptions. Their M&O contracts, thus, do not follow the full and open competition procedures required under Federal Acquisition Regulations (FAR).

The main fields of technology addressed by these facilities are now being converted to commercial technology or dual-use (military and commercial) technology. Even though there are some examples of agencies using competitive procedures, the United States shows no signs of uniformly placing their M&O Contracts under competitive procedures except in a few limited cases. The United States has excluded M&O Contracts from the list of covered services in the 1994 Agreement. We consider this to be an attempt to use national security as an excuse to limit competition and thereby improve the competitiveness of the US industry. The expansion of "national security" to include "national economic security" goes against the spirit of the 1994 Agreement and its basic principle of non-discrimination.

EUROPEAN UNION

EU Utilities Directive

In January 1993, as part of its market integration, the European Union issued an EU-wide directive on the procurement procedures of entities operating in the water, energy, transportation and telecommunications sectors. The directive contains two discriminatory provisions designed to ensure that third parties would not enjoy a "free-ride" after EU integration. The two discriminatory provisions are:

- A local content provision that permits the rejection of bids for supply contracts where the proportion of foreign products to be used exceeds 50 percent of the total value of products; and
- A provision that grants preferential treatment to domestic suppliers by stipulating that prices of tenders shall be considered equivalent if the price of domestic products is not more than three percent higher than that of imported products.

These provisions are intended to apply to countries that do not offer the same openness in government procurement procedures as the European Union provides in the same sector.

In response, the United States designated the European Union under Title VII of the Trade Act of 1974, as amended by the Omnibus Trade and Competitiveness Act of 1988, as "a country which maintains procurement practices discriminatory toward the United States." This provision of US law provides for sanctions against countries that discriminate against US firms in their public procurement practices. Subsequent consultations between the two parties failed to resolve the issue. January 1, 1993 was the member countries' deadline for implementing the EU directive (for developing related domestic laws). On February 1, the United States announced its intent to invoke sanctions beginning on March 22, 1993. The United States delayed imposing sanctions to allow for further bilateral negotiations. On April 21, following limited progress in the consultations, an agreement was reached under which the United States removed heavy electrical equipment from the scope of the sanctions.

Because the agreement was limited, on May 23, 1993, the United States imposed sanctions against the European Union worth approximately $20 million a year. The European Union retaliated on June 8, when it approved sanctions against the United States worth approximately $15 million. Despite an additional agreement reached on April 13, 1994, the United States maintained the sanctions because of the absence of an agreement on telecommunications procurement. Under the Title VII review conducted in April 1995, the United States decided to continue the sanctions and to extend them to the three new EU member states: Austria, Finland, and Sweden. The European Union

also decided to continue counter sanctions against the United States in June 1995. Subsequently, the EU made a proposal to the United States to mutually abolish existing sanctions by excluding the telecommunications sector from the application of a new directive on government procurement. In January 2002, the EU adopted rules to abolish sanctions against the United States Title VII provision. The sanctions, however, remain in effect because they will be abolished only after the rules are formally adopted by the EU in concert with the abolition of the US sanctions.

Since the four sectors in question were not subject to the provisions of the 1979 Agreement, the fact that the European Union issued this directive does not mean that it failed to comply with the 1979 Agreement. It did, however, include three of the sectors in question as part of the 1994 Agreement (the telecommunications sector was still excluded). Therefore, the European Union determined that the Directive in question no longer applies to tenders comprising certain products originating in Korea, Japan, Switzerland and the United States. For each of these countries, the European Union excluded certain products in certain sectors from the Directive, pursuant to its Annex to the 1994 Agreement. The European Union, however, still applies the Directive to Japanese suppliers with respect to the procurement by entities in electricity and urban transport sectors, which are not within the scope of the 1994 Agreement. The system is discriminatory in nature and Japan urges the European Union to dismantle it voluntarily.

CANADA

Provincial "Buy Canadian" Legislation

Canada's provincial governments have "Buy Canadian" and "Buy Local" policies similar to those of the United States. Preferential treatment is accorded to Canadian products in a variety of ways, requiring *inter alia* the purchase of Canadian or provincial products that are three percent to 15 percent more expensive than comparable foreign products.

On June 1, 1995, the federal government arranged an "Agreement on Internal Trade" between all ten of the country's provinces under which provincial governments were prohibited from discriminating against goods and providers from other provinces in their procurement. While this prevents provincial governments from enacting preferential pricing policies or discriminatory technical specifications for goods and suppliers from other provinces, it does not apply to goods and suppliers from other countries. This allows provinces to maintain their discriminatory treatment if they wish. Provinces are also allowed to exempt specific services and procuring institutions from the agreement. Improvements were seen in July 1999 with a new agreement obligating institutions that were formerly exempt from the agreement — local government institutions, education committees and other organizations using public funds to procure academic research, insurance or services — to adhere to non-discriminatory, transparent

and fair procedures in their procurement processes. However, Canada still maintains some exceptions. For example, institutions can give preferential treatment to domestic suppliers if the price difference is less than 10 percent, and can limit bidding to Canadian suppliers if Canadian markets are found to be sufficiently competitive and Canadian products are found to be sufficiently high in quality.

Industry Canada announced in December 2004 that the Federal Government and all territorial governments had agreed to include Crown Corporations (established in each provincial and territorial government) as covered entities under the 1994 Agreement. Registered companies in Canada are now entitled to participate in tenders launched by Crown Corporations in Federal, provincial and territorial governments. Provincial governments opened the doors to bidding in January 2005, and the Federal Government in April 2005. This means that foreign companies with subsidiaries registered in Canada may participate in procurements by Crown Corporations.

Canada initially expressed its intention to make domestic adjustments that would cover all provincial governments and to present a final offer covering sub-central government entities and sub-central government-related entities within 18 months of the signing of the 1994 Agreement in Marrakesh. However, Canada was unable to obtain a commitment from provincial governments, and the Agreement took effect without an offer from Canada on its sub-central government entities and sub-central government-related entities. From the perspective of further liberalization of government procurement, we would like to see a broad offer on sub-central government entities and sub-central government-related entities in the near future. We would also like to see the system discussed above remedied as quickly as possible.