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Detailed appraisal of the European Commission's Impact Assessment

Rules concerning third countries' reciprocal access to EU public procurement

Commission proposal for a
REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
on access of third-country goods and services to the Union's internal market in public
procurement and procedures supporting negotiations on access of Union goods and
services to the public procurement markets of third countries (COM(2012) 124 final)

ANNEX III

SME related impacts, thresholds and national legislation

**Research paper
by Pedro Telles**

Abstract

Direct benefits for SMEs from the proposed Regulation look limited at best, while indirect impacts appear probable. The 5 Mio EUR proposed for the threshold is similar to pre-existing public procurement thresholds and implies that only a small subset of contracts will be covered by the regulation which may impact its effectiveness. Contracting authorities have no incentive to refer procedures to the Commission. Spain has reciprocity clauses but there is no evidence of their widespread use.

AUTHOR

This study has been written by **Dr. Pedro Telles** of Bangor University at the request of the Impact Assessment Unit of the Directorate for Impact Assessment and European Added Value, within the Directorate General for Internal Policies (DG IPOL) of the General Secretariat of the European Parliament, following a request of the Committee on International Trade (INTA)

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Executive summary

European SMEs tend to bid mostly for public procurement contracts within their home Member State and for small contracts. Participation rates of SMEs in cross-border procurement appear lower than their overall participation on the economy. The Regulation proposed by the European Commission will target contracts over 5 Mio Eur with a view of forcing the opening of public procurement markets in third countries. The direct benefits for European SMEs will be limited if any at all. If indeed public procurement markets are opened in the future, the potential benefits for SMEs will mostly be available through sub-contracting and supply chain opportunities, areas that third countries can easily close down with *de facto* protectionist measures.

Some impacts on SMEs of the proposed Regulation do not appear to have been taken into consideration. Any SME participating directly (tenderers) or indirectly (sub-contractors, supply chain) in the procedure will face transaction and opportunity costs due to the four to eight week timeframes for decisions and any possible legal challenge.

All the solutions proposed by the European Commission could potentially lead to retaliation from third countries and it is impossible to map out their entire scope. Furthermore, irrespective of the solution adopted, it is not certain that retaliation would only happen in the same public procurement markets. It is entirely possible that an aggrieved third country could simply decide to retaliate on other trade areas with direct impact on the European SMEs in that market. This may be the biggest risk for EU companies as it could impact export led companies and even the operations of companies inside Europe.

From the perspective of SMEs, other than maintaining the *status quo*, all options considered by the European Commission imply transaction and opportunity costs. However, had the European Commission adopted option 3A (legislative approach without supervision) instead of 3B it would have at least reduced the timescales involved and the number of decisions that may be subject to judicial review. The European Commission could have also considered the option adopted in some Member States of targeting the origin of the bidders and not the origin of the goods or services and again some transaction and opportunity costs for SMEs could be avoided as long as it did not imply a supervision procedure.

The proposed 5 Mio Eur threshold for the Regulation is similar to some of the current thresholds applicable to European public procurement. By covering only a small number of strategic contracts, it will reduce the transaction costs for contracting authorities and the European Commission but may put at risk the effectiveness of the measure. If the threat is not credible because it is seldom used, how will it force any trading partner to negotiate? On the other hand, by reducing the scope of the application of this measure the risks for retaliation are reduced.

On the Impact Assessment working document the European Commission is forecasting 554 yearly referrals of public procurement procedures. This may prove to be too ambitious, as contracting authorities have no incentive to refer a public procurement procedure to the European Commission. This is due to the fact the costs of doing so are certain, i.e. delays in the procedure, risk and cost associated with a judicial review or a weaker field of candidates, whereas there is no obvious benefit for the contracting authority. Therefore it is quite possible the actual number of notifications will be lower than anticipated.

The exception to the previous reservation will probably be strategic or sensitive contracts where the contracting authority may have an interest in having it awarded to a national supplier. In that case, there is a risk the proposed Regulation will be used simply for protectionist purposes and it is as likely that the target of the referral will be either based on another Member State or on a third country.

Some Member States have developed specific “local mechanisms” that led different kinds of national reciprocity clauses: i) excluding suppliers due to their origin (Austria, Italy and Spain); ii) excluding tenders due to the origin of goods (Belgium); iii) exclusion of access to remedies (United Kingdom).

There is no evidence of widespread actual use of reciprocity clauses in the Member States that have them, nor are they a current topic in academic discussions or subject to abundant case law. This lack of evidence of use or interest appears to be the key lesson to be drawn: without incentives contracting authorities will not exclude foreign bidders.

No evidence has been found that the United Kingdom has a reciprocity clause other than an apparent restriction imposed in the access to remedies by suppliers based in third countries. Furthermore, in 2012 the UK Government has spoken against the proposed Regulation in no uncertain terms citing the risk of escalating protectionism.

1. Impact on SMEs

I - SMEs and public procurement

Participation by SMEs in public procurement has been seen for some time as an important goal within the internal market (European Commission, 2010 and European Commission, 2007) but so far have not entirely realised their potential. Between 2006 and 2008 SMEs captured over 60% of contracts but only 33% of the value for contracts above the EU thresholds. The share of value secured by SMEs is between 14% and 21% lower than their weight in the European economy, particularly for micro and small enterprises.

The current figures highlighted above are similar to the ones found for the period between 2002 and 2005 (European Commission, 2007). This indicates two important points for this report:

- i) The capacity for SMEs to win public contracts above the thresholds within the EU is plateauing;
- ii) SMEs tend to win the contracts with smaller value above EU thresholds.

When taken together, these findings point out towards a rule of thumb regarding the participation of SMEs in public procurement: the larger the contract, the less likely a SME will be able to capture it. It is important to take this into consideration when talking about SME participation in public procurement, particularly for contracts above 5 Mio EUR, which is the threshold proposed by the Commission in the proposal being analysed.

The EU thresholds currently have an established range from 130,000 EUR (certain services and goods) to 5 Mio EUR (works), thus meaning that only the contracts over those thresholds are harmonised under EU law. Contracts beneath these thresholds are not harmonised and, with some caveats such as the cross-border interest test, it is up to each Member State to regulate them.

By looking at the numbers, it is apparent that the bulk of EU rules do not apply to the contracts of the size most SMEs would be interested in competing for. The higher the value of the contract the higher the transaction and opportunity costs for a SME. When taken together, these two put a small company at a disadvantage in comparison with bigger tenderers. Furthermore, larger contracts tend to be tendered through restricted procedure or competitive dialogue which are biased against new or smaller firms due to the need to pick a pre-determined number of candidates based on their prior experience or financial capacity.

In addition, the current thresholds and other exclusions leave out 81.4% of the total procurement spend of the bulk of EU regulation. That is, the current procurement rules and as a consequence the GPA, only cover a small percentage of the total procurement spend.

In some Member States, such as the United Kingdom, participation of SMEs in public procurement has led to the realisation that the only way to increase their spend capture would be by increasing the advertising of lower value contracts and making them more transparent. This was requested by SMEs (Welsh Government, 2009) and implemented by the UK Government in 2011 through the creation of the portal ContractsFinder and the obligation of contracts over circa 12 000 EUR tendered by certain contracting authorities to be widely advertised. Between 2009/10 and 2011/12 the percentage of total direct procurement spend with SMEs grew from 6.5% to 13.7%, with an aspiration of reaching 25% by 2015 (Cabinet Office, 2012).

Taking into consideration the data provided above it appears that within national markets SMEs prefer and are more successful in smaller rather than larger contracts. Furthermore, regulatory and policy changes can foster their participation in procurement markets. This should be taken into account when looking into the impact of the proposed procurement opening policy, particularly as it will affect only contracts over 5 Mio Eur.

Regarding the participation of SMEs in cross-border procurement in Europe the data is less clear but a number of baselines from available research (European Commission, 2010a) may be drawn upon. The first one is that overall cross-border procurement in Europe is the exception and not the rule: only 1.5% of the total number of contracts covered by EU regulations are won by firms based in a different Member State. These contracts represent 3.4% of the procurement spend, once again indicating that they tend to be of a larger size and therefore of less interest to SMEs. Taking into account the conclusion of the previous point, it is probable that SMEs are under-represented in that percentage. If European SMEs appear not to be taking part nor winning public contracts in other Member States how can we expect them to win business in third countries?

Furthermore, the barriers to SMEs participation in foreign public procurement markets across Europe are well known: difficulty to establishing subsidiaries, adapting to different legal regimes and the need to do business in a foreign language. These are recognised by the Commission in the Impact Assessment document accompanying the proposed Regulation. They can be distilled into the higher transaction and opportunity costs of bidding for public procurement contracts abroad, which serve as a deterrent for SME participation. As only larger contracts are covered by EU regulations and as such widely advertised, it is again arguable that the current regulation of public procurement in Europe does not have a large effect on SMEs in terms of cross-border procurement.

The proposed Regulation does not address any of the issues previously identified and as such it is likely that its immediate impact on the participation of SMEs in public procurement at national, cross-border or international level will be limited even if the objective of opening other procurement markets is successful. In other words, if there are any immediate beneficiaries from the proposed Regulation, it will not be European SMEs. Regarding the negative impacts however, the answer is different as they can affect SMEs in many different ways (see next section).

II – To what extent has the impact for SMEs been evaluated?

The Impact Assessment working document looks briefly into the potential impact of the proposed Regulation for SMEs. Its focus is mostly on the difficulties facing SMEs in public procurement (Impact assessment p.18) and the opportunities arising from negotiations downstream for the opening of new public procurement markets (Impact assessment p.28) if negotiations with third countries are successful (SME internationalisation). Looking at the arguments provided, it seems plausible that some European SMEs will benefit in specific sectors and countries if this regulation indeed leads to the opening of new markets. The examples put forward of Portuguese SMEs in Brazil or Polish SMEs in Russia appear reasonable as at least in the first case the language and legal regimes are similar enough to justify the argument. However, no clear evidence of such benefits is provided in the Impact Assessment.

In addition, those are *indirect* benefits that *could* be accrued by SMEs. Looking at the limited success of cross-border procurement wins by SMEs within Europe it is apparent that subsequent issues such as the language and legal requirements of the third countries would have to be solved before European SMEs could reap the benefits of the opening of new markets. These are uncertain long-term benefits.

If the Regulation was indeed successful in the opening of new public procurement markets, perhaps that the biggest potential benefit for SMEs might be through the supply chain of those larger contracts in third countries. This is an area that the Impact Assessment working document does not shed light on unfortunately. One could argue against this potential benefit in that it is one thing to open the procurement market (i.e. the process that results in the choice of the contractor) and another the full blown opening of sub-contracting or supply chain possibilities underneath. It is not farfetched to imagine a situation whereby a third country could open a certain procurement market but would keep trade barriers in place to ensure that local supply chains would benefit from downstream work opportunities. This would not be covered by procurement related agreements and does not seem to have been taken into equation in the case made for the proposed Regulation.

As mentioned in the Impact Assessment working document it is possible that third countries will retaliate on the procurement access offered to European suppliers before starting any negotiations to strengthen their negotiating position. As such, European SMEs already involved in public procurement may lose the access they currently enjoy, either through direct participation or sub-contracting and supply chain opportunities on larger contracts. As mentioned before, participation of SMEs outside their home country is limited even within Europe but it is not unreal to foresee that in specific sectors there may be SMEs directly affected by any retaliation measure.

The Impact Assessment working document does not refer to two important general impacts that affect SMEs as well: i) inward impact, i.e. the impact that SMEs would face within Europe if the Regulation goes ahead; ii) the risk of retaliation outside public procurement.

1.1 Inward impacts

- i) Increased timescales on public procurement procedures subject to the notification procedure

In accordance with article 6(3) of the proposed Regulation, contracting authorities will have to notify the Commission of an intention to exclude a supplier. The Commission will have to produce a decision within two or four months of receiving the notification. In consequence, a procedure affected by a notification can be delayed for a period of up to four months. Any SME involved in the procedure either as a tenderer (unlikely due to the high threshold value, unless if part of a consortium), sub-contractor or part of the supply chain of any of the tenderers involved will suffer the same delays. It should be mentioned again that transaction and opportunity costs in public procurement are felt more strongly by SMEs and any delays to the conclusion of a procurement process will affect them more than larger companies. As the procedure will be stopped for a certain period of time, all tenderers, sub-contractors and supply chains will be affected and not only the ones involved in the tender will be subject to potential exclusion. Therefore, the suggestion of an opportunity cost of 3% for 6-8 weeks of delay on the tenderers affected (Impact Assessment working document footnote 104) seems reasonable for larger companies but understates the downstream costs on sub-contractors and supply chains. These are the areas where the potential cost impacts for SMEs may be higher.

- ii) Further delays due to legal challenges

In addition to the above, the creation of a new key decision within a procurement procedure will also open the possibility for legal challenges to be brought by any of the tenderers. For example, the tenderer facing exclusion may certainly appeal the decision taken by the Commission and will have access to the full remedy system available within the European public procurement legal framework. It will be entitled to apply for an interim suspension of the decision or the judicial review which would further delay the procedure.

Furthermore, it will provide the other tenderers with two opportunities to bring legal proceedings as well. Firstly, if the Commission decision is negative the remaining tenderers may decide to apply for judicial review of the decision. Secondly, if the contracting authority decides not to refer a tender to the Commission for exclusion, any of the remaining tenderers may also bring judicial review against such decision.

The risk for legal challenges will depend on the culture of each country and the specific circumstances of the tender. For example, legal challenges in public procurement are quite common in countries such as Portugal, Spain or Greece but uncommon in other Member States such as the United Kingdom or Denmark due to cost or the cultural issues.

1.2 Retaliation by third countries outside public procurement

Third countries affected by the proposed regulation may also decide to retaliate outside the field of public procurement in a more general trade dispute. There is no reason to assume that any retaliation will be done on a like for like basis. In the view of the author this poses a major risk that is underrepresented in the Impact Assessment working paper.

If a third country wants to maximise the effect of their retaliation, it may be that the most beneficial way for it to do so will be to target a completely different market. The obvious targets would be sectors where European suppliers (including exporting SMEs) are already operating and could stand to lose the access they currently enjoy. For example, in a scenario based on the construction sector where the steel being procured for the construction of a bridge is coming from a third country without a GPA agreement, if the Commission decides to exclude the tenderer the third country might retaliate by banning imports from European suppliers in the car industry or stop selling rare earth minerals to European buyers. Any SME operating directly or indirectly on these sectors could potentially be affected, including SMEs depending on inputs coming from third countries. In other words, not only the external market would be at risk but also the ability of European companies to keep operating at all in case their own supply chain is affected.

The legality of such retaliation may be disputed under WTO regulations but it would not be impossible for this to happen and it would take a number of years to go through the appropriate WTO mechanisms to solve the issue.

III - Are there some options more beneficial for SMEs than others?

The European Commission presented a number of different options before adopting solution 3B, that is, a legislative approach with supervision by the European Commission. All options involved trade offs and the case presented can be understood with the caveat that no hard data was provided but only the subjective impressions that led to the decision taken.

It is hard, if not impossible, to identify all the risks and possible consequences of any of the options provided due to the unlimited dependencies and the fact that the actual consequences will depend on the reactions from affected third countries. It is assumed that the overall impact will be dealt with in more detail in another of the areas of the questionnaire provided.

Although it is not advisable to focus the decision making process on the impact on a single group of stakeholders or beneficiaries, it is still relevant to look at what might be the consequences of the different options originally proposed on SMEs.

From the perspective of SMEs, the option adopted can lead to the aforementioned direct and indirect impacts and costs. However, it would appear that all other options have similar drawbacks. As the objective is to inflict some financial pain on third countries, any of the solutions to achieve this aim can lead to retaliation either on the original

market of the dispute or on a completely different market. It is quite possible that any option, to be effective, will impose transactions costs directly and bears the risk the effect of retaliation will be borne by unforeseen victims, including European SMEs.

It can be said however that any option (legislative or not) that did not include supervision by the European Commission would reduce but not eliminate potential negative impacts on European SMEs. For example, solution 3A, a legislative approach without supervision by the European Commission would trade the delay imposed by the two to four month decision timeframe with the possibility of more contracting authorities unilaterally deciding to exclude suppliers falling into the conditions imposed by the Regulation, particularly if said suppliers were foreign, i.e. based on other Member States or from third countries.

In addition to solution 3A, another option that might reduce the transaction costs for SMEs would be to adopt an approach similar to the one taken currently in Austria, Italy or Spain (please see last question) where the exclusion depends on the place of incorporation of the company. If this was a simply mandatory condition as currently imposed in some Member States without interference by the Commission, only foreign bidders would be excluded and at least some of the transaction costs could have been avoided.

Key findings

- European SMEs tend to bid for contracts much lower than the proposed threshold of 5 Mio Eur by the Regulation and they do not take part directly in most contracts covered by it. Any SMEs participating in supply chain or sub-contracting roles in tenders subject to the notification procedure would still be affected.
- Cross-border SME procurement participation is limited and Regulation does not address any of the already identified cross-border barriers, as such it is unlikely to have a direct positive impact for SMEs.
- Direct benefits for SMEs from the proposed Regulation other than supply chain opportunities on larger contracts tendered in third countries seem limited and even those are uncertain.
- Inward impact of Regulation has not been thoroughly explored in the Impact Assessment working document and potential impacts not originally forecast can be anticipated.
- Risk of retaliation outside public procurement by third countries has not been taken into consideration. This poses the biggest risk for EU businesses including SMEs
- All solutions proposed by the European Commission could lead to retaliation and other impacts on SMEs, but it is impossible to measure them with precision.
- From a perspective of the transaction costs for SMEs, option 3A (legislative approach without supervision by the Commission) or a system like the one currently in place in Austria, Italy or Spain that targets the origin of the supplier itself would potentially affect less European SMEs. That does not mean that these would be overall better tools to achieve the stated aim of forcing third countries to negotiate access to public procurement.

2. Justification of thresholds

I - Has the 5 Mio EURO threshold been assessed?

There is some logic behind choosing a single threshold instead of multiple ones for the application of the proposed Regulation. Having multiple thresholds, as it occurs within European public procurement, where there are different thresholds for different types of contracts and contracting authorities would increase the complexity and the compliance costs with the new Regulation. It could be argued however that if the objective was indeed for the Regulation to be applied in practice it would have been preferable to simply adopt the current multiple thresholds in force, as they cover many more contracts.

The 5 Mio Eur threshold appears to be aligned with existing relevant thresholds in public procurement. For the award of works contracts covered by the Directives 2004/18 and 2004/17 the threshold is also 5 Mio Euro. In addition, the GPA thresholds for works tendered by contracting authorities covered by Annex 1 (central purchasing bodies) or Annex 3 (state owned enterprises and utilities) is 5 Mio SDR, which amounts to around 4 Mio Eur. Therefore, by adopting a 5 Mio Eur threshold it is guaranteed that only contracts that are subject to the general EU procurement rules will be subject to this Regulation as well.

The value of 5 Mio Eur indicates that the proposed Regulation is not to be used very often in practice, as recognised by the European Commission on the suggested yearly notification numbers. This raises a question surrounding the effectiveness of this measure. To be effective, a threat needs to be used. Without a real threat of use it may simply be irrelevant as a tool to force third countries to negotiate the opening of their procurement markets directly. Even so, it may be a useful “bargaining chip” in more encompassing trade negotiations, something that is not put forward directly by the European Commission. For example, by having this Regulation in place it is possible to force a discussion on public procurement in general trade negotiations and be offered as a concession even if it has not been used many times against suppliers from a specific third country.

It is unclear whether this specific threshold has been assessed but it would appear it has been chosen as a compromise: it is high enough that will only apply to a limited subset of strategic contracts and with a value similar to already existing EU public procurement thresholds, thus limiting the compliance costs both to contracting authorities and to the European Commission.

II - Have the reasons in terms of cost and benefits been assessed for setting up this threshold?

Choosing a threshold value for the proposed Regulation implies a degree of trade offs between competing interests as argued above. On the one hand, there is the ultimate objective of using it as a bargaining chip for future negotiations and for that to happen

the Regulation needs to be effective or at least *appear* to be effective and being applied in practice. Otherwise it will be a proverbial “paper tiger”. On the other hand, the consequences and implications for participants in public procurement (contracting authorities, suppliers and the European Commission to a certain extent) need to be taken into account.

The European Commission estimates that there will be 554 notifications a year for the exclusion of tenders. The potential implications in terms of administrative burden are well established in the Impact Assessment working document assuming the number of notifications comes near the estimates (please see next question). If the Regulation was applicable to lower value contracts the number of notifications would necessarily be higher, increasing the transaction costs both for the contracting authority, the European Commission and suppliers taking part directly or indirectly (sub-contractors or supply chain) in the procedure. By having a lower threshold the number of notices could increase exponentially as a much higher percentage of contracts would potentially be covered. In other words it would not be focused on strategic procurement exercises but would lead to an increased number of referrals, perhaps with an increase in the efficiency (leverage) of the Regulation in future trade negotiations. A larger number of referrals would also imply that more third countries would be affected and increase the risk of retaliations.

The opposite is also reasonable. A higher threshold value would lead to a situation with only the proverbial “tip of the iceberg” of only a limited number of cases being potentially covered. As such, if only a limited number of notices were pushed every year the Regulation would not create any leverage over our trading partners.

It is not clear from the Impact Assessment working document or the Regulation in itself if the specific threshold of 5 Mio Eur was chosen as a value that would keep the negative impacts (transaction and opportunity costs) low while maximising the efficiency of the Regulation or if it was chosen as a benchmark value similar to threshold values already existing in public procurement.

III - Is the estimation of the number of notification cases correct?

The European Commission estimates that the Regulation will yield around 550 notifications yearly across all Member States. Forecasting how people will respond to future regulation is not an exact science and the case presented by the European Commission does not detail the assumptions that lead to the proposed number. However, some points are worth noting, particularly the issue surrounding incentives. The key question to pose on this issue is what is the incentive for someone to make the decision of referring a procurement procedure to the European Commission?

People react to incentives. For the contracting authority the regulation implies a certainty: extra transaction costs due to the compliance costs and the round trip of the notification

to the European Commission. In addition, it will have to factor in the risk that the decision may be challenged in court, further delaying the procurement procedure. What, then, is the incentive for a procurer to a) disclose on the tender documents the faculty of excluding a tender; b) spend time assessing all the documentation and certificates on all bids received to see if any should be referred; c) wait six to eight weeks for a reply from the European Commission; d) face the risk of having the process derailed with a judicial review; e) be left with a weaker field of candidates, thus potentially leaving it with a poorer choice? The upside for a procurer is negligible while the downside, particularly in terms of reputation risk for both the authority and the individual person leading the procurement procedure is quite tangible.

There is only one situation where all the drawbacks of the regulation may be put aside and that is if there is pressure within the contracting authority, namely political pressure, to exclude a bid from a foreigner supplier. By foreigner it is meant both a bid coming from outside the EU (the proposed target of a Regulation) and also a bid coming from a company based in another Member State. There is a clear danger that this Regulation may be used as a protectionist tool against all foreign bids and not only the ones from third countries as intended. As it stands, the 50% test imposed by Regulation is focused on the goods or services being supplied by the bidder and not the bidder nationality. As such, any European bidder using inputs coming from third countries is at risk of this Regulation. This risk can be minimised by amending the Regulation to make it clear that it is applicable to suppliers based on third countries only. However, this minimisation strategy introduces new risks, namely that third country suppliers will use European companies as “straw men” when bidding or will create special vehicles either in Europe or in countries not affected by the Regulation (i.e., GPA countries for example) to side step it (please see next question).

The higher the value and the visibility of the contract the bigger the incentive to use any tool available, even if illegally, to ensure the contract is won by a national firm. This is not a farfetched scenario. For example, in a situation where a national supplier and one based on another Member State present bids that would fall under the conditions imposed by the regulation for potential exclusion, it is entirely possible that the contracting authority will refer only the foreign bid to the Commission. The counter-argument would be that this would violate the principle of equal treatment (it does) but how would anyone know that if only the contracting authority has access to both bids? Unless the foreign bidder has a good knowledge of the competition he may not be in a position to argue that both bids should have been referred. This risk is not addressed by the European Commission on the Impact Assessment working document.

Key findings

- The 5 Mio Eur threshold is similar to some of the current thresholds for the application of EU public procurement rules. It will cover a limited number of contracts which may reduce its effect as a credible threat to force third countries to open their procurement markets.
- The proposed threshold seems to be a compromise between having a threat in place and the transaction costs imposed on contracting authorities and the European Commission by being applicable to a small number of strategic contracts.
- A lower threshold would increase the transaction costs for all involved (contracting authorities, direct and indirect suppliers and the European Commission) but at the same time make a more credible threat to third countries. As a consequence, however, retaliation would be more likely.
- The estimated number of 554 notification cases per year seems ambitious. The lack of incentives for contracting authorities to refer a procedure to the European Commission do not appear to have been tackled. Referring a procedure incurs on costs and downsides that are certain without any visible benefit for the contracting authority.
- There is a danger that this Regulation will be used for protectionist purposes, not only against bidders based in third countries but also bidders based in other Member States, particularly on larger contracts. At a cost, this risk can be minimised by amending the proposed Regulation as to apply the 50% test only to suppliers based in third countries. On the other hand, this would open the door to third country bidders using European companies as “straw men” or complex company structures to sidestep this solution.

3. National legislation restricting access to public procurement

I – Is there any more detailed information available on the existing national and regional legislation restricting access to public procurement?

The Impact Assessment working document put forward by the European Commission states that some Member States have created national regimes for the exclusion of tenders coming from tenderers based outside the European Union. The approaches taken by these pieces of legislation vary from country to country but may provide some interesting insights to potential use of the reciprocity clauses with the caveat of the widespread lack of data or reliable information on their use. This limitation has already been pointed out on the Impact Assessment working document. It should be noted that, in general, third country access is not perceived to be a leading public procurement issue discussed either in national academic circles or subject to significant national case law.

It is possible to organise the ways Member States have imposed reciprocity clauses in three different approaches: i) excluding suppliers due to their origin; ii) excluding tenders due to the origin of goods; iii) exclusion of access to remedies.

1. Excluding suppliers due to their origin (Austria, Italy and Spain)

Under this approach to reciprocity, Member States provide contracting authorities with the possibility of excluding companies based on their place of incorporation. As such, a Chinese company can be barred from taking part on a procurement procedure just due to the fact of being incorporated in that country. In some Member States such as Austria (and perhaps Spain), contracting authorities have the discretion to exclude or not companies based on third countries. In Italy, however, the law leaves no scope whatsoever for the contracting authority to make a decision to accept the participation of a company incorporated in a country not party to the GPA or specific trade agreements.

In comparison with the approach taken by the proposed Regulation, the exclusion of companies due to their origin has benefits and drawbacks. On the benefits side it provides more certainty to the contracting authority than assessing the origin of goods. It reduces uncertainty in the process as a simple transcript of the companies registrar will suffice for the decision to be made. In addition, this approach cannot be used as a protectionist tool against bidders based on other Member States, unless they are part of a consortium that includes members from a third country. On the other hand, as argued in the previous question, this is a system that can easily be defeated simply through the creation of a vehicle on any Member State or country party to the GPA or a trade deal covering public procurement. For example, the Chinese company could just incorporate a subsidiary in Germany or Canada to tender for contracts in Austria, Italy or Spain. In alternative, in contracts where technical or financial requirements are substantial it could enter an agreement with an European partner to use it as a front on the bidding or an existing subsidiary. Either way, these provisions are easily defeatable.

Although at least in Italy the contracting authority is obliged to exclude suppliers incorporated in third countries not covered by the GPA or trade agreements, there is limited evidence of the use in practice of this provision. For example, it appears that only one foreign company has taken this matter to the Italian courts so far (the company lost the appeal).

The actual use of these exclusions is even more limited where the contracting authorities have the discretion to exclude companies or not, for example in Austria and arguably in Spain. In Austria, anecdotal evidence has pointed to the limited use of this tool although it appears to be on the rise (albeit from a small base). There are not, however, reliable statistics available to provide a more certain answer. In Spain, both the national and a regional (Navarra) legislation allow for the exclusion of suppliers and there are no known cases of this provision being applied in practice. That does not mean it has not been used but there is a lack of doctrinal discussion or case law on this topic. Furthermore, even the various procurement advisory bodies in the country have not been asked to provide any guidance either.

This lack of evidence in various EU Member States with simple reciprocity clauses based on the origin of the supplier which cover most of their procurement (goods, services and works with values well under the 5 Mio Eur threshold of the proposed Regulation) seems to support the argument made on the previous question: without incentives, few contracting authorities will resort to exclude foreign bidders on the basis of reciprocal access to procurement markets.

2. Excluding tenders due to origin of goods (Belgium)

Other Member States such as Belgium have introduced legislation barring bidders from taking part on a public procurement procedure where a certain percentage of the goods provided is coming from the countries not party to the GPA or specific trade agreements. In other words, they have extended the current rules applicable to the utilities sector to all public procurement. In comparison with the proposed Regulation it is worth noting some differences.

The first difference is that there is no report process to an external authority. The contracting authority takes the decision and it can be challenged in the courts, but is not vetoed or approved by any other body as the Commission is proposing to do. This makes the process simpler and faster as it avoids the delay involved with a second decision maker.

Secondly, these rules are applicable to any goods supply or mixed contract covered by the legislation. As such they will cover a larger number of contracts by being applicable to contracts with a value well below the 5 Mio Eur threshold set in the proposed Regulation.

As mentioned in the Impact Assessment working document, the situation in practice in Belgium is unclear as the 2006 public procurement law was expected to come into force only in next July. In any case, the provision was already present in the previous 1993 law but no evidence of its widespread use was possible to be found.

3. Exclusion of remedies access (United Kingdom)

Although not technically an issue of access to public procurement markets by third country suppliers, the Impact Assessment working document refers to the United Kingdom, where the current public procurement remedies legislation appear to exclude the access to the remedies system to suppliers based outside the EU or a GPA signatory party. The Impact Assessment refers to the existence of case law in the UK which however was not possible to be found or analysed. The working document also correctly mentions that in any case the use of remedies in the UK is quite limited in general. However, particularly in Northern Ireland, the use has been increasing over the last few years albeit from a very small base.

On a literal reading of section 47B of the Public Contracts Regulation 2006 (as amended by the Public Contracts (Amendment) Regulation 2009) it appears to limit the access to the remedies system to suppliers based on GPA signatory parties. There are some reasonable grounds of uncertainty and the actual implications of these rules can be disputed.

The Impact Assessment working document appears to take a literal reading of the UK law as excluding any non-EU or GPA based supplier access to the remedies regime. However, this literal reading disregards two important points. Firstly, it would violate the principle of equal treatment as some bidders accepted to the tender would have access to means of redress whereas others would be excluded just due to their country of origin. It would be one thing for the law to allow the exclusion of tenderers from the start based on their origin, as it is possible on some Member States, another to treat it differently after he has been accepted to the tender.

Secondly, the literal reading implies also excluding suppliers from countries with trade agreements with the EU or the UK but that are not party to the GPA, such as Chile and Mexico.

In addition to the above reservations, the Cabinet Office has produced a public procurement policy note in April 2012 (Cabinet Office, 2012a) criticising the proposed Regulation as following a “tit for tat” approach that would lead to protectionism and would not be conducive to the objective of opening the public procurement markets. This appears to imply a very strong political view not only against the current Regulation proposal but also against the protectionist spirit it seems to embody. As such, it would not be surprising if the remedies rules would be amended as to make them clearly applicable to all tenderers in case they have really been applied as a discriminatory measure against bidders from third countries.

II – Which mechanisms have been put in place and can any lessons be drawn from this legislation?

From the previous section it is apparent that three different mechanisms have been used to restrict market access or the access to remedies by suppliers based in third countries: i) excluding suppliers due to their origin; ii) excluding tenders due to origin of goods; iii) exclusion of remedies access.

There is no clear evidence that at least in Austria, Italy and Spain there has been an extensive use of reciprocity clauses. In Austria and Italy there is evidence of occasional use only but without any clear data or information that could be of use to draw lessons from such use. There is also no evidence that many complaints have come forward through the judicial review systems of these three countries.

A specific lesson from the apparent lack of use of reciprocity clauses can be derived though. As argued in the question regarding the threshold value, even when contracting authorities are left with a fairly broad discretion to exclude a bidder it is not certain that they will do so if incentives are not there. It is likely that contracting authorities in the Member States analysed simply see no benefit to excluding tenderers taking part in public procurement procedures.

In addition to the above, regarding Spain, as this is a country where access to judicial review in public procurement is relatively easy for aggrieved bidders, there is actually an incentive for contracting authorities not to exclude tenderers in general (and specifically on reciprocity grounds). This ease of access to the remedies system leads to risk averse strategies that minimise the risk of challenges during the process. Not excluding candidates is a way to reduce the risks of challenges. In what concerns reciprocity clauses, the ease of access to remedies and the duration of judicial procedures may actually function as a deterrent against their use.

Another lesson can be derived from the way Member States have introduced reciprocity clauses in their national legislation. There appears to be a preference for targeting suppliers themselves and not the origin of the goods being supplied. This is different from the proposed Regulation where the deciding factor for exclusion is the origin of the goods. This may be a relevant point for analysis as it avoids the problem identified earlier with the proposed Regulation. By targeting the origin of inputs and not the supplier itself, the proposed Regulation may be used for protectionist purposes against suppliers based on other Member States. This risk does not occur with the current national reciprocity clauses as only suppliers from third countries not covered by the GPA or trade agreements are affected. However, as argued before, the national reciprocity clauses can easily be side stepped by simply using a subsidiary based on any Member State. For very large companies with subsidiaries it should be easy to just use an existing one based somewhere in Europe. Even for medium sized companies it may be reasonably easy to just create a vehicle in a Member State just for the purposes of tendering within the EU Member States with a reciprocity clause that targets the origin of the supplier.

Key findings

- The local mechanisms developed by EU Member States lead to three different kinds of reciprocity clauses: i) excluding suppliers due to their origin (Austria, Italy and Spain); ii) excluding tenders due to the origin of goods (Belgium); iii) exclusion of access to remedies (United Kingdom).
- There is no evidence of widespread use of reciprocity clauses in Member States such as Austria, Italy or Spain. In the first two cases the use seems limited and in the third non-existent.
- The lack of evidence of the use of reciprocity clauses appears to be the key lesson to be drawn from this legislation: without incentives contracting authorities will not be excluding foreign bidders.
- No evidence that the United Kingdom has a reciprocity clause other than apparent restriction imposed in the access to remedies by suppliers based in third countries. Furthermore, the Government has spoken against the proposed Regulation in no uncertain terms.
- National reciprocity clauses (Austria, Italy and Spain) appear to target the origin of the supplier and not the origin of the goods being supplied as it is the case with the proposed Regulation. This approach avoids the risk of being used for protectionist purposes against bidders based on other Member States but can easily be avoided by the creation of subsidiaries or similar strategies.

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