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(II)

CONTENTS

	Page
GATT articles.....	1
Foreign procurement practices.....	1
Selected foreign procurement practices.....	2
European Economic Community.....	2
European Free Trade Association (EFTA).....	3
Japan.....	3
Canada.....	4
Federal supply procurement in the United States.....	4
OECD work on international procurement code.....	5
U.S. objectives in OECD.....	6

Discriminatory Government Procurement Practices

GATT Articles

Government purchases of goods made for its own use and not for commercial resale fall largely outside the GATT trade rules. Countries that were unwilling to accept international obligations on the conduct of their procurement frustrated earlier efforts to formulate trade rules on government procurement paralleling those in the GATT which apply to private trading. In discussions which preceded the entry into force of the GATT, other countries rejected a United States proposal which would have extended the national treatment requirement (Article III) and the Most-Favored-Nation Principle (Article I) to government purchasing.

GATT provisions have limited applicability to government procurement. Article III expressly excludes the application of the national treatment rule to government purchasing and explicitly provides that it does not prevent subsidies to domestic producers, "including the purchase by the government of domestic products at higher prices than those for imported products." The only specific GATT obligation on government purchasing is found in Article XVII dealing with state trading. While excluding the application of the state trading provisions to this activity, the article requires a contracting party to accord "fair and equitable treatment" to the trade of other contracting parties with respect to imports of products "for immediate or ultimate consumption in government use." This provision is generally regarded as a near substitute for the most-favored-nation (MFN) clause.

Foreign Procurement Practices

Despite differences due to institutional and other local conditions, the procurement systems which have evolved under these conditions share in common a buy-national bias. National governments give effect to this propensity mainly through the flexible administration of procurement guidelines, particularly at the bidding and award stages in the procurement process.

Chances for participating in the bidding are circumscribed when advance publicity on prospective purchases is lacking or inadequate or when purchasing entities choose to ignore foreign suppliers in selectively seeking out suppliers of particular products. Criteria for the award of contracts can also be applied in a manner which effectively precludes contract awards to suppliers of foreign goods. The usual commercial considerations are sometimes set aside to buy only domestic products.

These actions are taken, for example, to relieve cyclical unemployment, promote regional economic development, protect domestic industry and establish a domestic industry in a high technology sector. These justifications are additional to those based on safeguarding national security or protecting public health and morals, which are widely recognized exceptions. Governments also resort to using administrative guidance, either formal or informal, to "persuade" purchasing entities to buy only domestic products whenever possible.

Avenues open for the redress of grievances growing out of contract award decisions are limited. The underlying reason for this can be attributed mainly to the absence of agreed international rules on government procurement. There is nothing to prevent an aggrieved party from raising a government procurement issue in the context of the GATT, but the very limited provision in the General Agreement covering trade involving government purchases would severely hamper reaching a firm judgment on the GATT legality of the action. As a consequence, there is virtually no GATT case history in the government purchasing area. Charges of discrimination are also difficult to prove when governments discriminate against foreign supplies through the procurement procedure. In some cases, published government procurement regulations do not exist. The difficulty is compounded when governments are reluctant to reveal information after the fact on considerations ruling in the contract award, the prices quoted in bids, and firms participating in the bidding, a deficiency which is particularly felt when foreign goods are offered in competition with domestic products. The large discretionary element which rests with the national government in procurement activities perhaps also explains the reluctance of some foreign suppliers to press complaints with other governments for fear of jeopardizing chances for future sales.

Selected Foreign Procurement Practices

European Economic Community

Within the European Community member countries follow their own procurement policies and regulations. However, a draft EC Council-Directive has been prepared by the Commission on "the coordination of adjudicating procedures for the award of public supply contracts" which is currently under review for possible adoption by the end of 1973. The EC member governments are thus under some constraint to move toward a fairer and more open system of procurement among themselves, but how far it will proceed in this direction is uncertain. Of course, to the extent the member country governments accord national treatment to suppliers in the other EC member countries, outside suppliers—including those in the United States—may face broader discrimination and possibly reduced sales to the EC government procurement market.

The evolving EC industrial policy and the role assigned to government procurement is also likely to have a major impact on future EC procurement policy. Some elements within the EC regard restrictions on procurements of certain products from foreign sources as a means of fostering the development within the EC of industries in the advanced technology sector. The advisability of this course is still being debated. Should the EC adopt the approach of promoting high-technology industries through protectionist government procurement policies, however, U.S. exports of high-value products making up an important part of our trade with industrialized countries could fall off. The treatment which other countries, especially the United States, give to imports under government procurement from the EC will almost certainly have some influence on EC's future procurement policy.

European Free Trade Association (EFTA)

EFTA countries have adopted a common set of procurement rules for observance by "public undertakings" in intra-EFTA trade of products eligible for "area tariff treatment". Public undertakings include central, regional and local government authorities as well as State monopolies, nationalized industries and semi-public enterprises. The twofold objectives of the procurement rules, developed pursuant to the requirements of Article XIV of the EFTA Convention, are to eliminate for the benefit of other EFTA countries protection for domestic producers and discrimination by nationality of suppliers. Guidelines on tendering methods provide that: (a) public tenders shall be adequately publicized and sufficient time for tendering shall be allowed; (b) selective tenders shall allow equal opportunities for domestic and other EFTA suppliers to compete; and (c) the single tender shall be used only when competitive tenders would be clearly impracticable or unreasonable. Elimination of preferences which frustrate the aim of the agreement is required. Use of the general consultation and complaints procedure of the EFTA Convention is prescribed for settling disputes which arise from infractions of the procurement rules. Member countries are free to maintain their existing procurement procedures and practices provided inconsistencies with the EFTA procurement rules are removed. No EFTA procurement rules have been elaborated for trade with third countries. These procurement rules remain in effect even though two former EFTA members—the United Kingdom and Denmark—have in the meantime joined the EC.

Japan

The Japanese Government buys its supply requirements under general provisions contained in certain laws and regulations introduced during 1946-47.

Procurements are made generally under either the selective automatic tender procedure, where bids are solicited selectively from

certain suppliers and the contract is awarded to the lowest bid, or on the basis of private negotiations involving no competition. Though there is no legislative requirement to buy domestic over foreign goods, a strong tendency exists for buying domestic products.

Canada

The Department of Supply and Services has taken over in large measure the supply procurement activities of all departments of the Federal Government and many Crown Corporations since April 1, 1969, except for certain products essential for the conduct of military operations. The following statement by the Canadian Minister of Supply succinctly describes Canadian policy regarding the purchase of foreign goods:

“. . . to the full extent to which they are procurable, consistent with proper economy and the expeditious carrying out of the contract, Canadian labor, parts and materials shall be used. Therefore, the department buys from Canadian firms if practicable and only turns to other sources of supply when procurement from the Canadian sources is deemed to be uneconomical or impractical.

“In addition, it is the government’s policy that a modest premium will be paid for a product with higher Canadian content. This premium is calculated at up to 10% of the difference of foreign content.

“In high value equipment such as aircraft, ships, special vehicles, etc. due to agreements for defense production sharing with the U.S. and other NATO countries many components contain an element of foreign content, but on an overall procurement basis, by far the largest proportion is Canadian.”

Federal Supply Procurement in the United States

In the U.S. Federal Government purchases of foreign goods are very small relative to total supply procurements. Domestic firms selling to the Federal Government are to a degree insulated from import competition, a condition due largely to the buy national policy of the Buy American Act and Executive Order 10582, its implementing order. Procurements of foreign goods for use in the United States are basically limited to those justified on grounds of nonavailability in sufficient quantity and quality, unreasonable cost of domestic products, or inconsistency with the public interest.

In applying the unreasonable cost criterion, U.S. products are accorded a preference margin when evaluating prices in competitive offers of foreign and domestic products. The Defense Department, which accounts for over 80 percent of total Federal procurement, currently adds a 50 percent price differential, considered as a benchmark, to the price quoted in the lowest responsive bid offering foreign goods for purpose of making price comparisons. The use of the 50 percent preference margin which the Defense Department applies to its

procurements for use in the United States under the "national interest" exception is justified as a temporary measure to alleviate the impact on the U.S. balance of payments of Defense Department spending for goods.

Other Federal agencies generally use either a 6 or 12 percent preference margin in favor of U.S. products, the higher rate applying, under certain conditions, when products are offered by small business firms or concerns located in a labor surplus area. Procurement of goods for use abroad is outside the Buy American Act; all Federal agencies, however, use a 50 percent preference margin in such circumstances for balance-of-payments reasons. Other provisions of the Buy American Act are used to restrict or even prohibit Federal procurements of foreign goods. Considerations of national security ordinarily rule against the purchase of foreign products of a military or paramilitary character.

The Defense Department restricts the purchase of certain products to those of domestic manufacture to maintain a U.S. defense mobilization base. In addition to miniature and instrument ball bearings, Defense Department requirements for jewel bearings and precision components for mechanical timing devices are for this reason procured domestically to the maximum extent possible.

Special provisions are made in domestic legislation to assure that a fair proportion of total purchases for Government use are placed with small business concerns. For suitable purchase transactions Federal agencies, either unilaterally or by joint action with the Small Business Administration, may stipulate that procurements should be made exclusively from small business concerns.

Still other statutory requirements restrict or prohibit the purchase of certain foreign products. For example, the Defense Department Appropriation Act includes a provision, the so-called Berry Amendment, prohibiting the use of appropriated funds for the procurement, with certain exceptions, of any article of food, clothing, cotton, wool or spun silk yarn for cartridge cloth not grown or produced in the United States. A similar restriction applies to buses other than those of U.S. manufacture for use by the Armed Forces and to certain foreign components for the conversion or construction of naval vessels in U.S. shipyards. The purchase of any naval vessel constructed in foreign shipyards is prohibited. For all ship construction on which a Federal subsidy is paid, domestic shipbuilders, subcontractors, materialmen and suppliers are required under the Merchant Marine Act to use, insofar as practicable, only articles, materials and supplies produced or manufactured in the United States.

OECD Work on International Procurement Code

Government procurement policies and practices of the industrialized countries were first reviewed during a country-by-country examination

within the Trade Committee of the OECD in the early 1960's. The OECD's work arose largely from complaints against the Department of Defense's decision in 1962 to apply a 50 percent margin of preference for domestic suppliers in evaluating bids where foreign suppliers were in competition. This examination became the forerunner of current efforts in that forum to develop a set of international guidelines on government procurement. Discussions have been underway for several years looking toward the development of an international code on government procurement which would reduce discrimination against foreign supplies and suppliers, including the phasing out of existing preference margins used to favor domestic over foreign supplies. Apart from conditions set out for the use of general exceptions and special derogations from the provisions of a possible code, the principal provisions deal with purchasing procedures, including advance publicity on planned purchases, conditions applying to the use of various tendering methods, technical characteristics of products, qualification of suppliers, evaluation of bids and award of contracts, and information on contracts awarded. In addition, provisions would be made for notification of significant changes in procurement rules, periodic review of the operation of the code and consultation procedures for resolving government procurement problems. In this effort, which aims at a degree of international harmonization in procurement policy and practice, progress has been slowed by the natural inclination of participating countries to be cautious in accepting departures from customary national practices, particularly where certain policies or procedures are incorporated in national legislation. Major differences remain on some key provisions which must be included in any proposed code.

U.S. Objectives in OECD

Major aims of U.S. participation in the OECD work on procurement guidelines are to safeguard the important stake U.S. suppliers have in sales to foreign governments and improve conditions of access to public sector markets abroad. To this end, the United States has provided the main impetus for this effort, emphasizing particularly the need for published procurement regulations, tightly-drawn rules to discourage discrimination against foreign supplies and suppliers, and minimal exceptions or derogations from the proposed rules. The steady growth over the years of central government expenditures for supplies and services underscores the importance of moving ahead on this work. Of perhaps greater importance, the failure to reach agreement could create the conditions conducive to the development of restrictive provisions applicable to third country interests as a counterpart to measures designed to promote intra-regional trade and to the increased use of government procurement as a policy instrument to achieve national

or regional objectives. An agreement reached on procurement guidelines would represent an important breakthrough in dealing with a major nontariff barrier, and might enhance prospects for negotiating the removal of other nontariff barriers. Major obstacles to agreement nevertheless remain, not the least of which is the insistence of others that the United States eliminate preference margins for domestic goods.

The enactment of additional restrictions by the United States or any other government at this time would make it more difficult to obtain an international consensus with regard to government procurement.

