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EUROPEAN INTERNATIONAL CONTRACTORS

EIC Position

on the

EU Consultation on an initiative on access of third countries to the EU's public procurement market

About EIC

European International Contractors (EIC) has as its members construction industry trade associations from fifteen European countries and represents the interests of the European construction industry in all questions related to its international construction activities. In 2009, the European construction industry was active in all world regions and generated an international construction turnover of more than 75 billion € *outside* of the Europe Union, primarily but not exclusively through the so-called GATS "Mode 3", i.e. a "commercial presence abroad", where the service is provided in a foreign market by a locally-established affiliate or subsidiary of a foreign-owned and -controlled company. We are pleased to take this opportunity to recall that EIC has been from the outset supportive of the so-called "GATS 2000 Negotiations" on the liberalisation of services, launched on February 7th, 2000, and has indicated to the European Commission that the absence of multilateral rules for public procurement is one of the major non-tariff barriers affecting the construction sector.

Introductory Remarks

The European Commission has consulted EU Member States and their Contracting Authorities, European business and its associations as well as the civil society about whether, and to what extent, it should enshrine the rights and obligations deriving from the Government Procurement Agreement (GPA) for EU Member States in a legally binding way into the EU legislation. According to the Commission's analysis, there is presently a gap between the international *obligation* of the EU to open its procurement market in the context of the GPA or Free Trade Agreements (FTAs) commitments and *actual* market access, which goes further.

Bearing in mind the recent example of an award of an EU-funded road works contract by an EU Contracting Authority to a state-owned enterprise from a third country (i.e. not being signatory to the GPA), EIC welcomes the EU Commission's considerations to **apply the degree of existing EU public procurement market commitments resulting from its international obligations** under the GPA and relevant FTAs as the – compulsory – **yardstick for EU Member States and their Contracting Authorities to grant access of third-country goods, services and companies to public tenders in the EU**.

In this context, it should be kept in mind that the European construction industry for many years has been faced with a situation in which **some of the largest construction markets in the world, which still remain outside the ambit of the GPA, are persistently reluctant to open their public procurement market to European or other foreign services providers**. One particularly striking example of such protectionist behaviour is the PR China where foreign construction companies are prohibited by law from participating in all public tenders in the Chinese construction sector, whilst so-called "wholly-foreign owned enterprises" are only allowed to take part in tenders that are *not* financed by Chinese authorities. Hence, participation in the Chinese public procurement market for foreign construction companies is only possible in the form of Sino-Foreign Joint Ventures thus, however, subject to a discriminatory qualification regime that *de facto* puts foreign-invested Joint Ventures at a disadvantage compared to domestic companies. This in turn has resulted, according to the "Study on the Future Opportunities and Challenges of EU-China Trade and Investment Relations" (Study 9 on Construction at page 16), in the market share of foreign construction companies in the PR China shrinking from 6 per cent before the Chinese accession to the WTO to less than 1 per cent today.

Public Procurement and International Law

According to the European Commission, public procurement is today arguably the largest trade sector sheltered from multilateral trade rules. It is not covered by any multilateral WTO discipline and it is, for example, specifically exempted from the WTO obligation to treat foreign and domestic companies equally. Thus the most important international agreement related to public procurement is the **WTO Agreement on Government Procurement (GPA)** which establishes a set of rules governing the procurement activities of its signatories and which also provides for market access opportunities. The GPA is not a multilateral agreement in the sense of Annex 1 of the WTO Agreement but a so-called **"plurilateral" agreement** under its Annex 4 and so far has been signed by only 40 parties (including all 27 EU Member States). As a consequence, the GPA is ***not*** part of the ***WTO's "single undertaking"*** which means that it is not mandatory for all the 153 WTO Members but only for those countries that have ratified the GPA.

In contrast to the WTO Agreement, the **GPA signatories have not reached a consensus either on the stipulation of the Most-Favoured-Nation clause or the principle of equal treatment of all parties**. This means in practice that for parties to the GPA there is no standard or "one-size-fits-all" access to the procurement markets of the contracting partners, but rather there are **different and reciprocal levels of market liberalisation between the GPA parties**. The actual scope of application is set out - in accordance with Article I:1 of the GPA Agreement – in the **Appendix 1** where each party to the GPA has stipulated specific restrictions, which means that the **GPA is** more comparable to a **complex network of bilateral relationships** rather than to an international agreement.

In light of this situation it can be concluded that the **European Commission's proposal to introduce a new legislative instrument** that would transform into the EU's internal legislation the international commitments agreed by the EU as a signatory to the GPA cannot be discredited as a "protectionist" or even "arbitrary" trade defence measure but is a **legitimate adoption of a legal position pertaining to the EU under international law**!

Liberalisation negotiations in the construction sector

Given that European international contractors generated in the year 2009 a total of 140 billion € in construction turnover outside their home markets, **EIC generally supports the principle of open construction and procurement markets**. The European construction industry is currently active on all five continents via its subsidiaries and affiliates, and, as noted before, **EIC has been supporting the international liberalisation negotiations in the construction services sector since the start of the Doha Round in November 2001**.

At the same time, and much to our regret, we have to observe that the **GATS and GPA negotiations in the construction sector** have not progressed over the last decade and have failed to produce **any presentable result**:

1. No visible steps towards liberalisation in construction services have been taken in the context of the **GATS negotiations**, nor was there any cross-sectoral or "horizontal" progress with respect to GATS mode 3 ["commercial presence abroad"], which is particularly relevant for the international activities of the European construction industry;
2. Since the **GPA Agreement** came into effect on 1 January 1996, none of the major emerging markets, which today have construction markets of very significant volumes, has become a party to the agreement;
3. Not even the minimum target of **achieving greater transparency in public procurement** has been reached, as the WTO Ministerial Conference decided on 1 August 2004 in Cancún to no longer pursue the respective negotiations for a multilateral agreement;
4. The most recent example of a general disinterest in the liberalisation of public procurement markets is the **PR China's revised offer to become a party to the GPA,** submitted on 9th July 2010. In addition to the well-known deficits with respect to threshold values and transitional periods as well as those relating to the lack of participation of provinces, municipalities and state-owned infrastructure enterprises, we must also, from the part of the construction sector, criticise that the Chinese offer **excludes in Annex 5 the entire civil engineering sector** from market liberalisation. Other market segments which are **excluded are foundation works, water well drilling as well as construction works for educational and health buildings**. Such a "cherry-picking" attitude can hardly be considered as serious.

EU Consultation on third-country participation in EU public procurement

In the light of this, from a European perspective, **disappointing development in the global negotiations of liberalisation for construction services**, EIC approves the European Commission's consideration to **seize a legitimate international legal position and to introduce a new EU legal instrument** that would permit access of third-country companies to the EU public procurement market only to the extent that there is a mutual and symmetrical possibility to access the respective third-country public procurement market.

Looking at the various options for action presented by the EU Commission in the consultation, **EIC supports** for the following three reasons the **proposed Option 3(A)**, i.e. an **EU legislative initiative with mandatory character for national Contracting Authorities**:

1. The EU itself has already specified in its "General Notes and Derogations from the provisions of GPA Article III of Appendix I of the EC" a number of caveats for liberalisation and has declared its intention to open its procurement market to other GPA signatories only insofar as those are providing reciprocal market access. The **GPA was implemented in internal EU law with the Directive 97/52/EC** of the European Parliament and Council dated 13 October 1997. In Recital 1 the EC Directive stipulates that *"...the purpose of* [the GPA]... *is to establish a multilateral framework of* ***balanced rights and obligations with respect to government procurement*** *with a view to achieving liberalization and expansion of world trade"*. Recital 3 further states that *"... the contracting authorities... which apply the same provisions as regards contractors, suppliers and providers of services of third countries* ***signatory to the Agreement are therefore in conformity with the Agreement****"*. The Directive thus implies that the exclusion of third-country companies that are not party to the GPA is lawful under EU law.

2. According to **Article 218 of the Lisbon Treaty**, the **EU Member States have authorised the European Commission to negotiate on behalf of the EU** in relation to agreements with third countries or international organisations. On the basis of this exclusive negotiating mandate, the EU Commission for several years has been calling for the PR China to become a signatory to the GPA (and for a FTA with India that includes an ambitious chapter on public procurement). It is **paradoxical** that under EU law **individual EU Member States are *not* legally bound to forego all measures that could weaken or even undermine the negotiating position of the EU Commission**, i.e. that neither the objectives nor the results of the GPA negotiations have the legal power to prevent individual EU Member States from opening their public procurement market beyond the agreed level of reciprocity. Such **legal incoherence in the internal EU law severely weakens the negotiating position of the European Commission in its international trade negotiations** thus raising the fundamental question of the value of this mechanism if the EU Commission's positions are not upheld by EU Member States. EIC would dare to argue that **there is an unintended loophole in the EU law** to the extent that **Article 3a paragraph 3 of the EU Treaty of Lisbon** stipulates that *"pursuant to the principle of sincere cooperation, the Union and the Member States shall, in full mutual respect, assist each other in carrying out tasks which flow from the Treaties... The Member States shall facilitate the achievement of the Union's tasks and refrain from any measure which could jeopardise the attainment of the Union's objectives".* **The described legal deficit can only be reduced by Option 3(A).**

3. A recent case in Poland illustrates that **individual Contracting Authorities in EU Member States can be receptive to "abnormally low offers" from third-country service providers** which probably benefit from state subsidies or consider an aggressive bid as the potential entry gate to the European procurement market.

Despite the fact that the award of the road contract to a Chinese state-owned construction company has raised legal and political questions from the outset, the **EU Commission** currently has **no legal authorisation to investigate such matters**. To remedy this deficit, the EU Commission should be granted a right of supervision and intervention on the basis of Option 3(A), in the event a national Contracting Authority wants to award a contract to a third-country company.

Potential objections against the EIC Position

EIC is well aware that a number of industries and national industry umbrella federations have taken a rather critical view on enhanced symmetry in public procurement, and generally disapprove the principle of reciprocity. **We are surprised to the extent that in some cases this view has been taken even by sectors which are not (or not essentially) affected by public procurement issues themselves.** Whilst we duly respect all positions taken in relation to the EU Commission's consultation, EIC considers the arguments put forward in this context against anchoring the reciprocity rule in public procurement in the internal EU legislation as not convincing for the following four reasons:

1. **The European construction sector is verifiably more affected by European and international public procurement laws and regulations than any other industry**. Contracting Authorities inside and outside the EU remain the key contracting entities for a very large part of the European construction industry. Based on the notices published in the European public procurement journal **"Tenders Electronic Daily"**, the average distribution of contracts awarded across the EU by value is on average 40% construction works, 35% services (including construction) and 25% goods. In the largest EU economy, Germany, it is estimated that whilst total capital expenditure by national Contracting Authorities amounted to some 42 billion € in 2010, **nearly 75 per cent was spent on construction projects**. This rate of expenditure may well be repeated in other countries. Conversely, EIC takes the view that industry sectors primarily maintaining relations with private or commercial customers ("B2B") are less affected by public procurement regimes.

2. **The construction industry is particularly dependent on fair play in the public procurement market** as EU Contracting Authorities are often obliged by law to award the contract to the **"lowest bidder"**. Consequently, a competition with publicly subsidised third-country companies would end up in a disastrous race to the bottom, putting at risk both the social and environmental accomplishments of the European Union as well as millions of jobs in the European construction industry.

3. Unfortunately, **EU law does not provide for any trade-related defence instrument which would tackle trade distortions in the services sector**. This is due to the fact that the WTO Agreements on Anti-Dumping and on Subsidies and Countervailing Measures only apply to goods but not to services. To make matters worse, EU competition law itself does not provide any protection against a distortion of competition by state-owned companies from third countries, as the **ban on distortive public subsidies set out in Article 107 et seq. of the EU Treaty only applies to EU companies** but not to those from third countries. Again, this is a paradox and

here, too, EIC considers current EU law to be incoherent and directly disadvantageous to the European construction industry.

4. Last but not least, reiterating the fact that the GPA is ***not*** part of the WTO's "single undertaking", we wonder if and how the introduction of a **reciprocity rule strictly confined to public procurement could provoke sanctions or similar measures under the WTO Agreement (GATT, GATS, TRIPS)**. EIC would assume that **sanctions or retaliation measures are not admissible with regard to other WTO disciplines**, in particular not from countries that are not even a GPA signatory.

Conclusion

The EU Commission's public consultation on the access of third countries to the EU's public procurement markets represents a "golden opportunity" for the European Union and its Member States to establish a uniform, standardised and legally binding regulation on the very sensitive subject matter of access of third-country goods, services and companies to the EU procurement markets.

EIC fully concurs with the introduction of a new legislative instrument as considered by the EU Commission (Option 3) and recommends that it be structured in such a way that EU Member States are only allowed to permit the participation of third-country companies if European companies are granted symmetrical access in the relevant market segment to the procurement market of the home country of the potential tenderer or supplier. In this context, it is necessary that the third country in question is either a GPA signatory or a trade partner of the EU which has signed a FTA comprising a substantial chapter on public procurement.

In order to prevent further deviations between the above legal principle and the acts of individual Contracting Authorities, **EIC would support the proposed approach 3(A) with one important amendment**: **EU Contracting Authorities should be required to notify *ex ante* to the European Commission any decision to allow the participation of third-country goods, services or companies** not covered by the EU's international commitments and should be required to set out its reason for doing so. Whilst **approach 3(A)** would ensure **a uniform application of the principle of reciprocity across the European Union**, the alternative **approach 3(B) would inevitably lead to confusion and disaccord** inside of the European Union, as the decision to apply the principle of reciprocity would be left to the discretion of individual Contract Authorities which, evidently, would construe such discretionary powers in accordance with the national rather than with the European interest.

Thus EIC calls on policy and business leaders in the European Union to, firstly, acknowledge the immense importance of the issue of third-country access to the European public procurement market and, secondly, to support the EU Commission acquiring a powerful mandate in that matter which is crucial for the identity and strength of the Europe Union in a globalised economy.

Berlin, 1st August 2011