# Public procurement law as an instrument of trade policy

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For some years now, Brussels has been discussing how to use public procurement law more actively as an instrument of trade policy. The EU has made efforts to end unequal market access for European companies in third countries and to reduce distortions of competition through various measures, such as the rapid signing of bilateral investment agreements. This is due to the fact, that while the EU has largely opened its public procurement markets to companies from third countries, many of these countries do not grant comparable access to EU companies. Moreover, unregulated state subsidies can contribute significantly to unfair competition and play a decisive role in future relations with third countries.

These discussions have been reignited by the current pandemic. The public procurement system suddenly seemed unable to supply public institutions with the required supplies. Recognising this issue has made it clear that certain core needs have to be met self-sufficiently.

## International Procurement Instrument, Higher Regional Court of Brandenburg, White Paper

### International Procurement Instrument (*IPI*)

The search for concrete options for action to strengthen the position of European companies on the global trade market has been occupying the European legislative bodies for some time. To improve conditions under which EU companies can compete for government contracts in third countries and to strengthen the EU's position in negotiations on access of EU goods, services and suppliers to foreign public procurement markets, the European Commission (*Commission*) proposed the so-called IPI in 2012. However, this proposal was heavily criticized by some member states. Taking these criticisms into account, the Commission presented a new proposal in 2016. It was still unsuccessful, as the member states were still unable to agree on a common solution. However, since the parallel negotiations between China and the EU on the conclusion of a far-reaching trade agreement came to a standstill, some member states abandoned their opposing views in 2019. In March 2020, the Commission presented its new industrial strategy for Europe and called for the rapid adoption of the IPI.

The current proposal provides for the Commission to launch an investigation in case of alleged discrimination against EU companies in the procurement market of third countries not covered by the GPA or a free trade agreement. If the Commission finds discrimination against EU goods, services or suppliers, the proposal plans for the Commission to invite the country concerned to enter into consultations. Where the remedial or corrective actions, taken following the consultations, are rescinded, suspended or improperly implemented, the Commission may resume consultations with the third country concerned. The Commission may also decide to impose a price adjustment measure with regard to tenders more than 50% of the total value of which is made of goods and/or services originating in a third country, where the third country adopts or maintains restrictive and/or discriminatory procurement measures or practices.

The European industry is generally in favour of the IPI, but still has some fundamental proposals for change to avoid additional burdens on EU companies (see for example the position of Business Europe). This applies in particular to the legally complicated areas of the regulation, such as the IPI's provisions on the origin of goods, the shaping of foreseen penalties and the agreement on a threshold value. Under the current proposal, for example, the penalties are triggered if more than 50% of the total value of the goods in the tender originates from the targeted third country. This could lead to complex investigations and create new bureaucratic burdens and legal uncertainties for EU companies. During the tendering stage, companies would have to have a full overview of the origin of all goods they will use in the execution of the contract. According to industry representatives, such a rule implies that bidders would have to undergo a costly and time-consuming origin verification during the evaluation of bids and the execution of the project. This not only represents a considerable risk in the event of a misjudgement, but also has a negative impact on European companies with international supply chains. As a solution, the European industry proposes that only the successful bidder should be contractually obliged to purchase no more than 50% of the value of the goods used in the execution of the contract from third countries. In such a case, an ex-post verification could be carried out.

**Decision of the Higher Regional Court of Brandenburg to exclude goods from third countries**

However, current law could also provide a solution to this problem. For many years now, German public procurement law has provided for the possibility to exclude offers, if more than 50 percent of the goods offered come from countries that do not belong to the EEA or with which no agreement on mutual market opening exists (Article 85 of the Utilities Directive 2014/25/EU and the national implementation in Section 55 (1) Sector Ordinance (*SektVO*). The most important third country affected is China. Russia, India and Brazil can also fall under the regulation. For a long time, German contracting authorities did not make use of this provision. This now seems to be changing:

With the decision of the Higher Regional Court of Brandenburg (decision of 2.6.2020 19 Verg 1/20) the exclusion of a company offering goods from third countries was subject

of a (published) court decision for the very first time. According to press reports, the underlying procurement procedure was an invitation to tender issued by the City of Frankfurt (Oder) for the manufacturing and delivery of 45 streetcar vehicles in a competitive procedure with negotiations. After several rounds of negotiations, the contracting authority invited three bidders, among others the Chinese company CRRC and the Czech manufacturer Skoda, to submit their final offers. Subsequently, Skoda was awarded the contract. After an unsuccessful complaint, CRRC filed a review application. The contracting authority excluded CRRC in the course of the review procedure on the basis of Section 55 (1) SektVO. The Review Chamber confirmed CRRC's exclusion, as did the Higher Regional Court upon CRRC's appeal.

The Review Chamber established that contracting authorities are provided with an extensive scope of discretion when exercising Section 55 (1) SektVO. Accordingly, contracting authorities may not only exclude a bidder from a procurement procedure as soon as the circumstances justifying their exclusion becomes known. They may also decide to do so at a later point in time, even as late as during the review procedure. The Higher Regional Court followed the Review Chamber in this because, among other things, considerable language barriers had arisen during the negotiations. It only added that the contracting authority must expressly reserve its possibility of exclusion pursuant to Section 55 (1) SektVO.

**White Paper: More extensive control of subsidized companies**

A further issue in this context is how to deal with subsidies from third countries to companies that participate in a procurement procedure in the EU. The EU directives on public procurement law, such as Art. 69 of the Public Procurement Directive 2014/24/EU, grant a wide margin of discretion in reviewing third country subsidies to the member states. In addition, the European Commission published the "Guidance on the participation of third country bidders and goods in the EU procurement market" in 2019. With this, the Commission wanted to establish a uniform understanding of the existing European legal framework regarding the participation of third country companies in EU procurement procedures. However, in the opinion of many member states and the Commission, none of these measures is a suitable means of comprehensively combating distortions of competition resulting from third-country subsidies.

Therefore, the Commission announced comprehensive control mechanisms for companies that are subsidized by third countries in the currently discussed White Paper on subsidies from third countries, The term "third countries" is intended to refer to those states that have not joined the GPA or with which no other bilateral agreement exists. With regard to procurement law, the White Paper suggests that economic operators participating in public procurement procedures, would have to notify to the contracting authority when submitting their bid whether they, including any of their consortium members, or subcontractors and suppliers have received foreign financial contribution from a third country in the last three years or whether they expect such foreign financial

contributions during the execution of the contract. Threshold values - not yet estimated in detail - are to apply. Among other things, the notification should also contain the main sources of overall financing of the tender. Subsequently, national authorities in cooperation with the Commission are to check in a two-step procedure whether the foreign subsidy leads to a distortion of the procurement procedure. During the investigation, the contracting authority is barred from awarding the contract to the investigated economic operator. The identification of a market-distorting third country subsidy can lead to the exclusion of the economic operator concerned from the ongoing procurement procedure, but also to the economic operator being debarred from taking part in future procedures.

Two further instruments are intended to complement the procurement law suggestions made in the White Paper. Firstly, the introduction of a general instrument for market observation is suggested, which would allow for the Commission or for national authorities to proceed against companies supported through third country subsidies. Similar to the anti-trust controls placed upon market-dominating companies, corrective measures should be available to encounter distortions of competition. Possible corrective measures suggested in the White Paper are, amongst other things, the reimbursement of subsidies received, the withdrawal from European markets, or market behavioural requirements. Finally, the White Paper suggests an examination of the acquisition of EU-companies through buyers subsidized by third countries. If specific threshold values were to be exceeded in the examination, the transaction would have to be registered with the Commission, and would only be allowed to be carried out upon the Commission's approval. This suggested examination is supposed to complement merger control measures, as well as measure minority interests.

**Conclusion**

The discussion about the IPI picked up momentum again last year. However, despite the considerable need for discussion, it can be assumed that the member states will reach a common consensus in the coming months.

Section 55 SektVO also follows the trade policy principle of reciprocity and acts as a control instrument for dealing with bidders from third countries with which no agreements on mutual market access exist. The Higher Regional Court of Brandenburg has confirmed an exclusion on this basis for the first time. It remains to be seen whether this regulation will be used more often for this purpose in the future.

It is still unclear, how the concrete conversion of the White Paper to handling third national subsidies will look like. The deadline for stakeholders to submit their views is 23 September 2020. The Commission is already preparing to submit concrete legislative proposals in the course of next year.

BLOMSTEIN will monitor and inform about further developments. If you have any questions regarding the potential impact of changes in public procurement law on your company or industry, Dr Pascal Friton and Dr Laura Louca are always available to answer them. Furthermore, should any questions regarding the anti-trust instruments suggested in the White Paper arise, please contact Dr Max Klasse.