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## The WTO Agreement on Government Procurement and the UNCITRAL Model Procurement Law: A View From Outside the Region

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# Articles

## THE WTO AGREEMENT ON GOVERNMENT PROCUREMENT AND THE UNCITRAL MODEL PROCUREMENT LAW: A VIEW FROM OUTSIDE THE REGION

*John Linarelli\**

### ABSTRACT

*Two of the most significant efforts to bring municipal procurement institutions up to international standards are the WTO Agreement on Government Procurement (GPA) and the UNCITRAL Model Law on Procurement of Goods, Construction and Services. Though the Model Law has had limited adoptions, it enjoys global influence as a source of norms and practices for good public procurement. The GPA, also reflective of international standards, seems to be on the rise, as more WTO members elect to become GPA contracting parties. This article explores two aspects of these instruments. First, the article explores how the Model Law promotes efficient public procurement. It explains how the ongoing revisions of the Model Law, in particular in the area of electronic*

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*reverse auctions, continues to promote efficiency in procurement systems. Second, the article explores how the GPA promotes efficiency in its non-market access provisions, but that its market access provisions permit governments to take the fairness of procurement policies into account, through socio-economic programs. Only efficiency is a value at the transnational level, and fairness is a concern only of municipal governments at this time. The GPA thus imperfectly facilitates a mix of efficiency and fairness policies in the procurement systems of the GPA contracting parties. Only GPA contracting parties with significant market leverage, who can open up substantial procurement markets while still maintaining protected socio-economic procurements, can effectively promote both fairness and efficiency in their procurement systems. Of course, what one country might characterize as fairness, another might characterize as rent-seeking protection, and it is well accepted that while trade restrictive policies often seem laudable in theory, they can be difficult to implement and harmful in practice.*

**KEYWORDS:** *public procurement; world trade; law and development; relation of economics to social values; new institutional economics; distributive justice*

## I. INTRODUCTION

Public procurement law and policy exists in a nether world in terms of inquiry about its relationship to international trade and the economic growth of states. Much of the activity in procurement law reform in countries working to improve their procurement systems is undertaken at the level of the practitioner's art. The focus is on action and on the immediate practicalities of procurement reform. It is reminiscent of the substantial legislative activity in the 1980s and 1990s to combat "fraud, waste and abuse" in the United States federal procurement system. How could any U.S. congressman be against fighting fraud, waste and abuse? The result was a "ratchet effect"<sup>1</sup> in production of ever more procurement

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<sup>1</sup> See generally William E. Kovacic, *Regulatory Controls as Barriers to Entry in Government Procurement*, 25 POL'Y SCI. 29 (1992).

laws, so that what we have in the United States is an overregulated procurement system that is still inefficient, and regrettably, prone to corruption.<sup>2</sup> Many of us who work and think about procurement law and policy learned our craft while doing it, either in actual purchasing or in law practice representing government or contractor clients. As a body of experts we thus focus on implementation of procurement reform and liberalization. The aim of this paper is to reflect on the strategic aspects of public procurement law reform and liberalization of public procurement markets at the WTO level. I examine some justifications for procurement reform and liberalization to support a consensus on why reform is important and what it is supposed to do. Public procurement is a means to an end. Even when public procurement reform is seen as part of the project to promote good governance, the higher goal of good governance is a means to an end as well.<sup>3</sup> The end is about improving the lives of the citizens of countries, citizens whose scarce funds are used to finance procurement. It seems uncontroversial to say that public procurement law and institutions must be efficient, but they must be fair as well, and when fairness and efficiency conflict, we must recognize that fairness might come at a social cost. The analysis set forth here requires us to momentarily separate action from inquiry, and to think about procurement reform and liberalization principally from the standpoint of inquiry.

What I am getting at here is a view from outside the region. In the 1960s and 1970s, American lawyers, with the financial assistance of the U.S. government and multilateral institutions, embarked on ambitious programs to assist developing countries with legal reforms. One of the leaders of that movement, Stanford Professor John Henry Merryman, wrote an influential paper, published in 1977, arguing that lawyers spent too much effort doing law reform projects and insufficient effort inquiring about the nature and activity of law in developing countries. Merryman explained:

These characteristics: unfamiliarity with the target culture and society (including its legal system), innocence of theory, artificially privileged access to power, and relative immunity to consequences, have been typical of many law and development proposals and programs for the third world. Put another way, we were probably incompetent to propose or execute third world law and development action, we were encouraged (by our own self-image, by the foreign assistance psychology and by

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<sup>2</sup> Steven L. Schooner, *A Conversation about Malversation: The Post-Millennial U.S. Experience Combating Corruption in Public Procurement* (June 19, 2006) (unpublished draft, on file with the author).

<sup>3</sup> See The World Bank, *Poverty Matters*, <http://www.worldbank.org/html/extdr/gc/governance/governance.htm> (last visited July 5, 2006).

third-world conditions) to do so, and we did not suffer the consequences of having done so. The mainstream law and development movement, dominated by the American legal style, was bound to fail and has failed.<sup>4</sup>

By contemporary standards, Merryman's language may seem off the mark. We no longer speak of the third world. Moreover, his comments seem directed at poorer countries than are represented at this conference, given the rise of the Asian economies. Law and development may not be a proper subject for this conference. But an important lesson emanates from Merryman's words, one which still holds true today. Merryman went on to say that his findings are not as depressing as they may seem, and that he recommend we examine, from the standpoint of inquiry, the legal traditions and social institutions of countries before embarking on reform.<sup>5</sup> In sum, legal scholars should be cautious in recommending reform, and base such recommendations on good information and a thorough understanding of context.

This paper proceeds from Merryman's findings. "Law and development" is no longer the right name for the field. It is too narrow and it is misleading. The contemporary focus is on the effect of law on economic growth, which is improved terminology, but still in need of improvement because it fails to focus on fairness and distributive justice concerns. The law and development movement of Merryman's generation was too focused on sociological inquiry and on what should be a repudiated concept of modernization. Law and economics has replaced sociologically based inquiry as the dominant school of thought, but not without the introduction of a new set of problems. Economic analysis of law permits us to ignore important policy questions through a reductionist move of selecting a discipline to use in the analysis that does not provide the analytical tools to recognize and answer the questions. With economics as the dominant paradigm, the focus still is on important issues like, how to produce an adequate institutional infrastructure to facilitate credit and business financing, or how to improve courts and the machinery of justice, or on how to achieve recognition of the informal economy and improve the

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<sup>4</sup> John Henry Merryman, *Comparative Law and Social Change: On the Origins, Style, Decline and Revival of the Law and Development Movement*, 25 AM. J. COMP. L. 457, 481 (1977); see generally Francis G. Snyder, *Book Review: The Failure of "Law and Development" Legal Imperialism: American Lawyers and Foreign Aid in Latin America*, 1982 WIS. L. REV. 373 (1982); Elliot Burg, *Law and Development: A Review of the Literature and a Critique of "Scholars in Self-Estrangement"*, 25 AM. J. COMP. L. 492 (1977); David Trubek & Marc Galanter, *Scholars in Self-Estrangement: Some Reflections on the Crisis in Law and Development Studies in the United States*, 1974 WIS. L. REV. 1062 (1974).

<sup>5</sup> Merryman, *supra* note 4, at 481.

welfare and economic security of participants in the informal sectors.<sup>6</sup> Given that all successful economies are mixed economies,<sup>7</sup> however, one of the weaknesses in looking just to economics for answers is its lack of a theory of justice. The international financial institutions have begun to respond to such concerns.<sup>8</sup> Economic approaches, which rely solely on efficiency concepts, are helpful but incomplete. We also have to inquire about the fairness or justice of a particular law or policy. The fairness or justice inquiry has to be sensitive to the domestic context in which the policy will be implemented. Sometimes the result is friction between the international and domestic. This sort of friction is the locus of concern in many discussions about globalization.

What has all this got to do with public procurement? We want to have the complete set of tools to evaluate public procurement from a strategic policy stance. In section II below, I explain how the transparency characteristics of the UNCITRAL Model Law on Procurement of Goods, Construction and Services<sup>9</sup> promote economic efficiency. In section III, I explain how the WTO Agreement on Government Procurement (GPA),<sup>10</sup> while promoting transparency and efficiency in much the same way as the UNCITRAL Model Law, gives GPA contracting parties the ability to pursue social justice goals, but also how it limits the ability of contracting parties to pursue such goals. Section IV concludes the article.

## II. EFFICIENCY ASPECTS OF THE UNCITRAL MODEL PROCUREMENT LAW

The economic efficiency of procurement rules is in part the result of the way they produce transparency in the procurement process. Transparency, then, relates to the issue of governance. Transparency in public procurement provides governments, taxpayers, and other interested

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<sup>6</sup> See, e.g., Nicholas Georgakopoulos, *Statistics of Legal Infrastructures: A Review of the Law and Finance Literature*, 8 AM. J.L. & ECON. 62 (2006); Juan Carlos Butero, Rafael La Porta, Florencio López-de-Silanes, Andrei Shleifer & Alexander Volokh, *Judicial Reform*, 18 WORLD BANK RES. OBSERVER 61 (2003); HERNANDO DE SOTO, *THE MYSTERY OF CAPITAL: WHY CAPITALISM TRIUMPHS IN THE WEST AND FAILS EVERYWHERE ELSE* (2000); Richard E. Messick, *Judicial Reform and Economic Development: A Survey of the Issues*, 14 WORLD BANK RES. OBSERVER 117 (1999); ROSS LEVINE, *Law, Finance and Economic Growth*, 8 J. FINAN. INTERMEDIATION 8 (1999); Richard A. Posner, *Creating a Legal Framework for Economic Development*, 13 WORLD BANK RES. OBSERVER 1 (1998); Heywood Fleisig, *Secured Transactions: The Power of Collateral*, FINANCE AND DEVELOPMENT 44 (June 1996).

<sup>7</sup> Robert L. Kuttner, *Development, Globalization, and Law*, 26 MICH. J. INT'L L. 19 (2004).

<sup>8</sup> See generally Kerry Rittich, *The Future of Law and Development: Second Generation Reforms and the Incorporation of the Social*, 26 MICH. J. INT'L L. 199 (2004).

<sup>9</sup> The text of the Model Procurement Law can be found at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/procurement\\_infrastructure/1994Model.html](http://www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/1994Model.html) (last visited July 5, 2006).

<sup>10</sup> The text of the GPA can be found at, [http://www.wto.org/English/tratop\\_e/gproc\\_e/gp\\_gpa\\_e.htm](http://www.wto.org/English/tratop_e/gproc_e/gp_gpa_e.htm) (last visited July 5, 2006).

parties with the ability to monitor expenditures of public funds in public procurement. Transparency also provides procurement officials with incentives to conduct procurements in best value terms. In this section, I show how the UNCITRAL Model Procurement Law promotes efficiency and begin to connect the efficiency aspects of the Model Law to good governance, but first a digression about the WTO.

In the 1996 Singapore Ministerial Conference, the WTO members established a Working Group on Transparency in Government Procurement.<sup>11</sup> The aim of the Working Group was to determine whether a new transparency framework agreement could take the place of the GPA. This aim of the transparency framework agreement was to broaden the scope of participation in liberalization of procurement markets. Some trade negotiators and commentators thought that such an agreement could broaden participation beyond the then narrow “club” membership of the GPA, by permitting protectionist practices, so long as those practices were transparent.<sup>12</sup> On August 1, 2004, the WTO General Council adopted a decision in which the transparency negotiations were discontinued.<sup>13</sup> The transparency framework agreement is off the table for the Doha Ministerial Conference. The official WTO position is that the transparency agreement is on hold.<sup>14</sup> Malaysia was one of the countries instrumental in bringing an end to the Working Group and eventual negotiations.<sup>15</sup> It is particularly difficult for Malaysia to join any procurement liberalization agreement unless that agreement permits the kind of substantial preference programs in public procurement that Malaysia has in place for its majority Malay or Bumiputera population.<sup>16</sup>

Though WTO work on the transparency framework agreement is on hold, there is reason for us to be sanguine about the prospects of moves toward transparency in public procurement, coming from the work of UNCITRAL on the Model Procurement Law. The on-hold WTO transparency framework agreement relates to a larger point about public procurement, and that is that nearly all of its rules are at least in part

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<sup>11</sup> World Trade Organization, Singapore Ministerial Declaration, WT/MIN(96)/DEC (Dec. 13, 1996), 36 I.L.M. 218 (1997).

<sup>12</sup> John Linarelli, *The WTO Transparency Agenda: Law, Economics and International Relations Theory*, in *PUBLIC PROCUREMENT: THE CONTINUING REVOLUTION* 235, 241-42 (Sue Arrowsmith & Martin Trybus eds., Kluwer Law International 2003).

<sup>13</sup> Robert D. Anderson, *Developments on Public Procurement in the WTO* (June 19, 2006) (unpublished manuscript, on file with the author).

<sup>14</sup> *Id.*

<sup>15</sup> See generally Christopher McCrudden & Stuart G. Gross, *WTO Government Procurement Rules and the Local Dynamics of Procurement Policies: A Malaysian Case Study*, 17 *EUR. J. INT'L L.* 151 (2006).

<sup>16</sup> *Id.* at 153.

justifiable on the basis of transparency, regardless of the legal regime in which the rules happen to be located.

In this section, I provide a way of thinking about the transparency aspects of procurement, mainly using the tools of new institutional economics. Public procurement law is rich in legal rules susceptible to economic analysis.<sup>17</sup> The potentially richest source of economic methods available for analyzing the structure of legal rules on public procurement is what economists variously describe as contract theory, principal agent theory, or the economics of information. The economic toolkit provides what Laffont and Tirole call “contractible variables” – variables facilitating the ability of interested parties to monitor procurement practices and market access.<sup>18</sup> Transparency gives interested parties the ability to know about poor practices in public procurement, as well as trade barriers in public procurement markets. Transparency relates to both good procurement practices – in achieving value for money – and to market access – to understanding how open or closed procurement markets actually are.

The standard explanation goes as follows.<sup>19</sup> A basic question procurement officials face during the planning stages of a procurement is what method of procurement should be adopted. Related to this question is what should be the evaluation criteria by which offers should be judged. In the legal systems of many countries, and in the UNCITRAL Model Procurement Law, a range of options exist to deal with these two issues. These options are usually constrained by certain conditions that must be met in order to justify reliance on a particular method of procurement or method of evaluation. As for methods of procurement, governments can use a very formal approach, such as sealed bidding, a very informal approach, such as unstructured negotiations with few rules to bind procurement officials, or an intermediate approach, such as a request for proposals method of procurement, which permits negotiations but usually within a highly structured and legalistic format. If sealed bidding is used, firms submit sealed bids, the government opens the bids for public view on a predetermined and published date and time, and the government makes award to the qualified bidder who submits the lowest price or cost and whose bid does not materially deviate from the government's solicitation of

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<sup>17</sup> See generally Daniel R Fischel & Alan O Sykes, *Governmental Liability for Breach of Contract*, 1 AM. L. & ECON. REV. 343 (1999).

<sup>18</sup> See generally JEAN-JACQUES LAFFONT & JEAN TIROLE, *A THEORY OF INCENTIVES IN PROCUREMENT AND REGULATION* (1993).

<sup>19</sup> The above discussion is based on Linarelli, *The WTO Transparency Agenda*, *supra* note 12, at 256-65. For detailed discussion of the procurement principles, see generally SUE ARROWSMITH, JOHN LINARELLI & DON WALLACE, JR., *REGULATING PUBLIC PROCUREMENT: NATIONAL AND INTERNATIONAL PERSPECTIVES* (Kluwer Law International 2000).



bids.<sup>20</sup> In some jurisdictions, negotiations between government and bidders are banned in the sealed bid procedure, which usually means that the government cannot go to the lowest bidder and ask for a lower price.<sup>21</sup> To be contrasted with sealed bidding is a request for proposals method of procurement, where no bid opening occurs, but instead a closing date for submission of confidential proposals, which are then evaluated in secret by the government, although they are still required to be evaluated in accordance with evaluation criteria published in a request for proposals issued by the procuring entity. In a request for proposals procedure, the government may negotiate with proposing firms, and will typically apply significant discretion in evaluating technical merit and in trading off technical merit against cost in determining which proposing firm is offering “best value.” We can contrast the sealed bidding and request for proposals methods of procurement with a wholly unstructured negotiated approach mirroring what might happen in some private sector contexts, in which the purchasing agent has maximum discretion, and in which there are few constraints on the structure of the offer and acceptance process leading to contract award.

An important question for governments, taxpayers or other interested parties in a procurement context – what in economics are called “principals” – is whether procurement officials – the “agents” – have conducted procurements efficiently.<sup>22</sup> This is a difficult question to answer because the principals have less information than the agents about how procurements are actually conducted. Principals want to monitor agents to determine whether the agents are making efficient procurement awards, but they lack adequate information to determine whether procurements are actually conducted efficiently. Governments have developed proxy variables to assess efficiency, much like variables that were developed by the insurance industry to evaluate risk. It is costly for insurance companies to determine whether an insured is actually careful, so they do not base insurance terms on the actual care exercised by the insured. Rather, insurance companies use proxies that focus on results and statistics, such as numbers of accidents or claims, smoker versus non-smoker, young male versus other drivers, and other such information which can facilitate

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<sup>20</sup> In some jurisdictions, sealed bidding can only be used along with an evaluation criterion requiring award on the basis of lowest price or cost. ARROWSMITH, LINARELLI & WALLACE, *supra* note 19, at 674-79.

<sup>21</sup> *Id.* at 488-503.

<sup>22</sup> There can be a number of principals in the public procurement context. The principal can be taxpayers or ministers. In procurements financed by a development bank such as the World Bank, the principals can be the bank shareholders, the bank's directors, the bank itself or even the taxpayers in the shareholder countries.

separating equilibria in the insurance market.<sup>23</sup> Similar conditions hold in public procurement. It is costly for principals in the procurement context to determine whether procurement agents are actually efficient, so they do not actually evaluate efficiency in procurement. They instead use proxies. For example, sealed bidding is easier to monitor than the request for proposals or negotiated methods of procurement. In a sealed bid context, the question whether a procurement is conducted efficiently is answered simply by asking whether the agent has followed the mandatory rules set out in the law. If she has, then the procurement is efficient. This analysis seems to explain a number of legal rules used in public procurement systems. It explains why the World Bank and the regional development banks maintain a strong preference for sealed bidding and ban negotiations in bank-financed procurement. The development banks do not have the resources to conduct comprehensive audits, evaluations or investigations of the many procurements they finance, so they accept that if the sealed bid procedure is used properly, then by definition, bank funds are being spent properly. What I have explained thus far, I have named the “information rationale” for transparency in public procurement.<sup>24</sup>

In addition to providing for less costly monitoring of procurement agents, formal methods of procurement, such as sealed bidding, provide procurement agents, who, unlike their private sector counterparts, are not constrained (or are constrained less) by market forces, with less discretion. The economist Armen Alchian has explained this “incentive rationale” for procurement rules.<sup>25</sup> Alchian's incentive rationale is the traditional rationale for procurement law. The incentive rationale focuses on the need for tried and tested procurement methods in lieu of reliance on procurement officials making their own decisions. The incentive rationale is the weaker rationale because it fails to account for the fact that in the right circumstances, government officials have reputational, career and programmatic incentives to be efficient. Both the incentive rationale and the above information rationale, and particularly the informational rationale, support formalism and legalism in public procurement, when it is necessary to preclude or at least mitigate moral hazard in procurement. Moral hazard is the problem of unobservable or hidden action that may occur during the procurement process, when the behavior of an agent conducting the procurement is insufficiently observable.

A significant policy base for the rules in the UNCITRAL Model Procurement Law is the promotion of transparency in public procurement.

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<sup>23</sup> See, e.g., Steven Shavell, *On Moral Hazard and Insurance*, 93 Q.J. ECON. 541 (1979).

<sup>24</sup> Linarelli, *supra* note 12, at 258-59.

<sup>25</sup> Armen Alchian, *Electrical Equipment Collusion: Why and How*, in *ECONOMIC FORCES AT WORK* 259-69 (Armen Alchian ed., 1977).

The Model Law is loaded with procedures to facilitate monitoring of government officials. If we examine UNCITRAL's work in drafting and revising the Model Law, we see that the information and incentive rationales for transparency in procurement regimes are at work. Let us take a look at the latest round of discussions of the working group, which occurred in at the United Nations in New York on April 24-28, 2006. One of the more substantive areas of discussion in that session was on the inclusion of provisions in the Model Law to deal with electronic reverse auctions or ERAs for short. The Note by the Secretariat, upon which discussions were based, explained, among other things that "the main issue for consideration is whether the ERA should include non-price criteria that are qualitative and not quantifiable."<sup>26</sup> The Secretariat explained that two models existed for electronic reverse auctions. In the first model, labeled Model 1, "all aspects of the bids that are to be evaluated in selecting the winning supplier are to be submitted through the auction. These criteria are the price alone, or the price and price-equivalents that can be expressed as a percentage of price or in figures."<sup>27</sup> In the second model, labeled Model 2, there is a

pre-auction assessment of all elements of the initial bid or of those elements not to be submitted to the auction, following which suppliers are ranked, and their rankings communicated to them. All evaluation criteria are then factored in a mathematical formula, which would then re-rank the bidders on the submission of each bid during the auction itself.<sup>28</sup>

So, Model 1 resembles the typical sealed bid procedure, in which only price and price-related factors are evaluated, and what is evaluated are the "bids" submitted through the electronic auctioning process. Model 2, on the other hand, involves "more complex procedures that allow criteria other than price to be subject to auction," in which "a formula is to be used to quantify the non-price or non-price-equivalent elements to be presented."<sup>29</sup> Though the Secretariat found it "implicit in the use of a formula that the non-price or price-equivalent elements are expressed as a figure, percentage, or otherwise numerically" the Secretariat suggested that the Working Group "consider whether it is realistic to make an assumption that

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<sup>26</sup> Note by the Secretariat, Possible Revisions to the UNCITRAL Model Law on Procurement of Goods, Construction and Services – Drafting Materials for the Use of Electronic Reverse Auctions in Public Procurement and Addressing Abnormally Low Tenders, A/CN.9/WG.I/WP.43 (Feb. 15, 2006). This and other UNCITRAL documents can be found at, [http://www.uncitral.org/uncitral/en/uncitral\\_texts/procurement\\_infrastructure/1994Model.html](http://www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/1994Model.html) (last visited July 7, 2006).

<sup>27</sup> *Id.* ¶ 28.

<sup>28</sup> *Id.* ¶ 29.

<sup>29</sup> *Id.* ¶ 31.

non-price or non-price equivalent criteria can be so expressed in a clear and transparent manner.”<sup>30</sup> The Model 2 approach is one adopted by the new European Union Directives. As the UN Secretariat has explained:

The new European Union Directives make provision for such non-price criteria to be subject to auction, but the Secretariat has been able to locate very limited examples of such auctions conducted in practice so as to examine their effectiveness. In those encountered, non-quantifiable criteria were assessed using a points system. For example, the technical and commercial aspects of the tender in one case were assessed out of a score of 6000, and each such point was converted using an “exchange rate” of 2500 to equate price reductions with the additional value provided by the non-price assessment points (the latter included such matters as management of subcontractor and the ability to deal with unusual incidental aspects of the contract, such as archaeological constraints). In another case, the value of risk transferred back to the procuring entity from minor tender noncompliances and caveats was weighted in cash terms (so doing is relatively straightforward if the risk can be insured, but in other cases may be difficult).<sup>31</sup>

Though the second, more complex and less transparent approach is the subject of the new European Union Directives and hence may be the subject of European practice now and in the future, a number of the delegates seemed uncomfortable with the level of discretion Model 2 affords to procurement officials. The result of the discussions to-date is a more conservative, less discretionary and more transparent approach. The Secretariat reported the sentiments of the delegates as follows:

It was pointed out that in drafting any provisions on electronic reverse auctions (ERAs) in the Model Law and the Guide, conditions in and interests of countries that would primarily benefit from the Model Law should be kept in mind. It was pointed out that the Model Law had promoted so far traditional open tendering as a “gold standard”, whose fundamental principles included prohibition of negotiations and a single opportunity for a supplier to submit its best tender, which were contradicted by the inherent features of ERAs. Acknowledging and regulating ERAs in the Model Law could mean deviation

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<sup>30</sup> *Id.*

<sup>31</sup> *Id.* ¶ 32.

from these fundamental principles and dilution of the “gold standard” of open tendering.<sup>32</sup>

So, the option is to produce an electronic reverse auction procedure that is more transparent. A more transparent procedure appears to mean one that resembles sealed bidding more closely. The Working Group took into account, among other things, the position of the multilateral development banks on the question. The development banks tend to prefer more formal procedures in the nature of sealed bidding.<sup>33</sup> The Secretariat expressed the collective view that the risks inherent in electronic reverse auctions should be mitigated through regulation.<sup>34</sup> So, the Working Group considered a number of procedural safeguards designed to maximize transparency in the electronic reverse auction process. “Anonymity of bidders and clear specifications established and made known to suppliers at the outset of procurement were named as such important considerations.”<sup>35</sup> As well, “[e]xperience with ERAs in at least one jurisdiction, it was said, indicated that they might be a costly tool for procurement of demands for only one procuring entity as third-party contractors were hired. Therefore, consolidated purchases were encouraged.”<sup>36</sup> Price is to be the only evaluation criteria to be used, making the electronic reverse auction very much like a sealed bid procedure:

The initial preference was that the provisions should be drafted in such a way as to allow the price to be the only award criteria when ERAs were used. Allowing criteria other than price would open the possibilities of abuse as a subjective element could be introduced into the process when trying to quantify these criteria.<sup>37</sup>

In addition, the delegates expressed the view “that establishing the lowest price below which tender would not be accepted could be an important safeguard for a proper management of ERAs and against abnormally low tenders.”<sup>38</sup>

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<sup>32</sup> Report of Working Group I (Procurement) on the Work of its Ninth Session, ¶ 87, A/CN.9/595 (May 8, 2006).

<sup>33</sup> *Id.* ¶ 88.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.* ¶ 89.

<sup>36</sup> *Id.* ¶ 90.

<sup>37</sup> *Id.* ¶ 91.

<sup>38</sup> *Id.*

Some delegates were of the view that only “standard goods and commodities” should be the subject of electronic reverse auctions.<sup>39</sup> The Secretariat has explained the various views as follows:

The point was made that even standard services (for example, cleaning services) could have qualitative elements and therefore procurement through ERAs could compromise quality. On the other hand, it was stated that it would not be desirable to limit ERAs to any particular type of procurement as at this stage it would be difficult to predict how the tool would evolve. As experience in some countries suggested, services were capable of being procured through ERAs even when quality mattered with a two phase approach, the first phase involving the assessment of quality aspects.<sup>40</sup>

Throughout the discussion, the countervailing arguments for and against Models 1 and 2 procedures were discussed. Some delegates were not entirely convinced that transparency required only a Model 1 approach. As the Secretariat has explained, “[a] number of objections were raised to providing exclusively for Model 1 ERAs as they presupposed a fully automated process, which especially at a transitional stage in development, could not be achieved without the risk of excluding a substantial number of suppliers.”<sup>41</sup>

The delegates agreed that electronic reverse auctions should be a “stand-alone procurement method, to avoid prejudicing their evolution,” but also acknowledged that they could be an “optional phase” in some procurement methods.<sup>42</sup> The current proposed text for a new method of procurement known as electronic reverse auctions, seen as a “compromise solution, drafted in a sufficiently broad and flexible manner to allow evolution of ERAs within a number of parameters,”<sup>43</sup> is the following:

**Article [36 bis]. Conditions for use of electronic reverse auctions**

A procuring entity may engage in procurement by means of an electronic reverse auction in accordance with article [s 47 bis and ter] in the following circumstances:

(a) Where it is feasible for the procuring entity to formulate detailed and precise specifications for the goods, construction and services;

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<sup>39</sup> *Id.* ¶ 92.

<sup>40</sup> *Id.*

<sup>41</sup> *Id.* ¶ 93.

<sup>42</sup> *Id.* ¶ 94.

<sup>43</sup> *Id.* ¶ 96.

- (b) Where there is a competitive market of suppliers or contractors that are anticipated to be qualified to participate in the electronic reverse auction such that effective competition is ensured;
- (c) Where it concerns (i) commonly used goods, the characteristics of which are generally available on the market; or (ii) commonly used services or constructions, the characteristics of which are generally available on the market and provided that the services or constructions are of a simple nature; and
- (d) the price is the only criterion to be used in determining the successful bid; or
- (e) [option for the legislator:] the price and other criteria that can be expressed in figures or transformed into monetary units and can be evaluated automatically are to be used in determining the successful bid.<sup>44</sup>

It is clear from this tentative provision and its discussion, that the new procedure promotes the information and incentive rationales that justify transparency in public procurement.

There were some dissenting views in the UNCITRAL session, preferring more flexibility in the new procedure. “An observation was that the proposed text favoured price considerations at the expense of quality and that the approach should be reconsidered.”<sup>45</sup> The response was that “that situation was inherent in ERAs and thus in procurement where quality was more important than or equal to price, other procurement methods might be more suitable.”<sup>46</sup> One possible solution to the problem of ensuring that electronic reverse auctions be as transparent as practicable is to explain their use and their risks in the Guide to Enactment.<sup>47</sup>

The point I am trying to make in this discussion is that the UNCITRAL Model Procurement Law takes a conservative approach to procurement, focusing on the traditional procurement disciplines, which promote transparency and hence economic efficiency. Given that the intended constituency of the Model Procurement Law is countries in need of procurement law reform – principally developing countries and countries in transition from socialism – the conservative approach is appropriate because what needs to be developed in the procurement systems of these countries is widely held competencies – good procurement practices, based

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<sup>44</sup> *Id.* ¶ 95.

<sup>45</sup> *Id.* ¶ 97.

<sup>46</sup> *Id.*

<sup>47</sup> *Id.* ¶¶ 99-104.

on time-tested procurement disciplines. Ultimately, to take the reasoning to its logical conclusion, it is not just about drafting and promulgating legislation on the books, but about developing capacities to conduct procurement based on the disciplines found in the Model Law.

The formalism and legalism prevalent in the UNCITRAL Model Law is not without tradeoffs.<sup>48</sup> There may be cases in which legal rules imposing formality in public procurement, and the resulting loss of discretion in the hands of procurement officials, may mean that a procuring entity is forced to achieve transparency at the expense of good business practice. Anyone experienced in procurement practices can cite the examples. But as a general matter, all things being equal, we want procurements to be more rather than less transparent.

Two models of procurement governance have emerged from the efforts of the last decade or so to develop and improve public procurement systems. These models relate directly to the above institutional analysis. Some of these efforts come from the need to distinguish public from private contracting in countries transitioning to market oriented economies. In some cases their purpose is to bring procurement systems up to international standards in response to attention from the World Bank and other international institutions. In the past I have divided these models into two, the developed country model and the developing or transitioning country model, though this terminology may not be sufficiently general.<sup>49</sup> The terminology can be generalized to classify according to the level of sophistication of the procurement regulatory regime in a country, regardless of the income level of the country. The two models can be described as a “mature” procurement systems model, which I designate as model 1, and an “emerging” procurement systems model, which I designate as model 2. In model 1 systems, governments have a significant degree of power to provide incentives for contractor compliance with procurement rules and contract terms. In model 1 systems, a high degree of professionalization of the procurement workforce exists, and adequate remuneration for procurement officials through an established civil service system. The professionalization of the workforce is due in substantial part to years of costly investment in the human capital of civil service employees. Model 1 systems include substantial criminal and quasi-criminal investigative institutions complementing significant procurement regulatory institutions. In countries with model 1 systems, substantial levels of monitors exist in the form of internal enforcement bodies whose functions are to deter fraud, waste and abuse. In addition to such internal enforcement institutions, some countries have privatized enforcement in bid challenge or bid protest

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<sup>48</sup> The above discussion is based on Linarelli, *supra* note 12, at 259-60.

<sup>49</sup> The above discussion is based on *id.* at 264-65.



systems that permit interested parties (typically disappointed offerors) to protest procurement actions that they claim violate procurement law. In model 1 systems, procurement by open procedures or by sealed bidding is not the norm. Effective enforcement institutions and a well-trained and well-compensated bureaucracy make less transparency a worthwhile trade-off for enhanced discretion and flexibility.

The procurement systems in the countries meeting model 1 characteristics contrast markedly with procurement systems meeting model 2 characteristics. Many of the features of procurement law and practice in model 1 systems tend either to not exist in model 2 systems, or tend to exist at only the early stages. A commonly held view is that countries with model 2 systems are not yet in a position to use, at least extensively, informal procurement procedures. The implementation of a model 1 system would require the fundamental reform of judiciaries, legislatures and bureaucracies, something that cannot be forthcoming immediately in some countries, especially in developing countries and countries with transition economies. Enforcement institutions do not exist or are deficient in model 2 systems. Model 2 systems rely relatively more on the transparency of procurement procedures to facilitate monitoring of procuring entities and contractors. Open competitive bidding, which provides more transparency than methods of procurement based on requests for proposals or negotiation, tends to be the norm. A commonly held view is that bidding promotes a number of procurement disciplines that are fundamental to good procurement practice and that should be mastered before taking on procurement through requests for proposals or negotiation.

The above analysis is not intended to suggest that procurement officials in countries with mature procurement regulatory systems are noble and public interest minded and that their counterparts in countries with emerging procurement regulatory systems are venal and corrupt. As we well know, corruption in the procurement systems of developed countries can be widespread.<sup>50</sup> Moreover, it is not a matter of culture but of context and incentives. The point is that principal-agent monitoring relies on established legal and bureaucratic institutions that do a good job at aligning the incentives of procurement agents with those of their principals.

### III. TEMPERING EFFICIENCY WITH FAIRNESS: GPA MARKET ACCESS

In an article I wrote in 2001, I called the GPA a “failure of cooperation” because of its limited “club” membership.<sup>51</sup> At the time, there

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<sup>50</sup> Schooner, *supra* note 2.

<sup>51</sup> Linarelli, *supra* note 12, at 235. The focus of my criticism was on the limited number of WTO members who are GPA contracting parties. An alternative measure suggested to me, the value of procurements liberalized, would have produced a more optimistic assessment of the GPA. *Id.* at

was some optimism about the development of the transparency framework agreement, though that project has since been discontinued.<sup>52</sup> I would like to retract my “failure” conclusion. With the pressure of the United States and other WTO members, it seems the GPA is to have broader participation in the future. At the current time, nine WTO members are negotiating for accession to the GPA. They are: Albania, Bulgaria, Georgia, Jordan, the Kyrgyz Republic, Moldova, Oman, Panama, and Chinese Taipei. Moreover, the Protocols of Accession of a further six WTO members say something about eventual accession to the GPA. These WTO members are: Armenia, China, Croatia, the Former Yugoslav Republic of Macedonia, Mongolia and Saudi Arabia. China recently confirmed that it will formally begin the accession process by submitting an accession offer under GPA Appendix I by the end of 2007.<sup>53</sup>

Some of these WTO members have relied on the UNCITRAL Model Law to reform their procurement systems.<sup>54</sup> Both the GPA and the UNCITRAL Model Law promote transparency. The transparency characteristics of the UNCITRAL Model Law promote trade liberalization because they facilitate monitoring of commitments of the GPA contracting parties by each other. The same principal-agent reasoning discussed above in the domestic context applies in the international context. To the extent that the GPA text contains similar principles – and it does – these principles facilitate monitoring by GPA contracting parties. The GPA implements the information rationale discussed above. The GPA sets forth detailed “positive” rules with which GPA contracting parties are required to comply.<sup>55</sup> The aim of the GPA is to harmonize domestic procurement rules, for public procurements to which the GPA applies. For procurements to which the GPA applies, GPA contracting parties are obligated to conform their domestic procurement rules to GPA requirements. Positive rules are to be distinguished from negative rules, which require countries to comply with WTO obligations, but leave it to the members to decide how

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235 n.1.

<sup>52</sup> See *supra* notes 13-16 and accompanying text.

<sup>53</sup> See Anderson, *supra* note 13.

<sup>54</sup> The following countries have adopted legislation based on or inspired by the UNCITRAL Model Procurement Law: Albania, Azerbaijan, Croatia, Estonia, Gambia (2001), Kazakhstan, Kenya, Kyrgyzstan, Malawi (2003), Mauritius, Mongolia, Poland, Republic of Moldova, Romania, Slovakia, Tanzania, Uganda, and Uzbekistan. UNCITRAL, Status of 1994 UNCITRAL Model Law on Procurement of Goods, Construction, and Services, [http://www.uncitral.org/uncitral/en/uncitral\\_texts/procurement\\_infrastructure/1994Model\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/1994Model_status.html) (last visited July 7, 2006).

<sup>55</sup> Linarelli, *supra* note 12, at 236-37; William A. Dymond & Michael M. Hart, *Post Modern Trade Policy Reflections on the Challenges to Multilateral Trade Negotiations after Seattle*, J. WORLD TRADE 21, 29 (2000); Susan Brown, *The Developing Countries and Transparency in Government Procurement Strategic Issues*, paper prepared for UNCTAD (Aug. 11, 1999).

compliance will be achieved.<sup>56</sup> In this sense, the GPA was ahead of its time. This sort of positive rule making did not occur in earnest in the multilateral trading system until the Uruguay Round; its most prominent example is the Agreement on Trade Related Aspects of Intellectual Property Rights.<sup>57</sup> The positive rules in the GPA text may form part of the reason why the GPA participation base has been so limited.

The text of the GPA itself – the part detailing requirements on how procurements are to be conducted – can be conceptualized as the non-market access provisions of the GPA.<sup>58</sup> The market access provisions are the all-important annexes, which the GPA contracting parties negotiate. While the non-market access provisions could be said to promote transparency, the market access provisions could be said to promote fairness. This may seem an odd conclusion, but here is the explanation.

The GPA market access provisions promote fairness to the extent that they give GPA contracting parties the ability to promote social justice and to intermediate the effects of globalization on public contracting markets, and to the extent that some level of protection forms part of a legitimate political consensus within the constitutional systems of GPA contracting parties who choose to follow such a route. For example, if a GPA contracting party maintains a policy of repair to remedy past actual or societal discrimination against certain groups, then it can withhold market access for some procurements designated for these groups, by not putting those procurements on the table for coverage by the GPA. The United States does something like this for its substantial minority and small business programs.<sup>59</sup> Two stories have been told about so-called preferences in public procurement.<sup>60</sup> Both stories contain a number of truths, though the stories themselves are oppositional to some extent, one describing a case of justice and the other a case of economic waste.

First, I provide the “good” story about preferences. Preferences promote social justice for disadvantaged groups. In some countries, they are intended to mitigate historic injustice, situations in which past policies made favored groups better off while making disfavored groups worse off.

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<sup>56</sup> Linarelli, *supra* note 12, at 236-37, for a discussion of these issues.

<sup>57</sup> See Frederick M. Abbott, *TRIPS in Seattle: The Not-So-Surprising Failure and the Future of the TRIPS Agenda*, 18 *BERKELEY J. INT'L L.* 165, 166-67 (2000).

<sup>58</sup> I am grateful to Robert Anderson for the market access and non-market access terminology.

<sup>59</sup> The U.S. Supreme Court has imposed constitutional limitations on such “set asides.” See, e.g., *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200 (1995). (The claim made by the petitioner, Adarand Constructors, Inc., which was not a certified small business under the Small Business Administration program, was that the race-based presumptions used in subcontractors compensation clauses violate the Fifth Amendment.)

<sup>60</sup> The typical preferences are for domestic contractors owned by certain disadvantaged groups, based on ethnicity or gender, or preferences based on the domestic content of the goods and services provided by the contractor.

This is the policy of repair approach mentioned above. Some scholars have named such an approach a trade stakeholder model.<sup>61</sup> Such a model values broad participation by domestic constituencies in trade policy, at both the domestic and international levels. It is a model of deliberative democracy in which social justice is taken into account as a variable separate from economic efficiency. In the good story, domestic interest groups are important and are cast in a positive light. In the good story, interest groups in an open and transparent policymaking process promote diversity and the achievement of a broad overlapping consensus for public policy.

In the good story, as a matter of fairness, WTO members should retain the ability to develop programs to promote participation in public procurement by members of all segments of their societies, including programs such as domestic preferences, set asides, and procurement assistance for small and minority owned firms. Procurement is recognized as having important social policy implications. The good story accepts that the social consensus reached within the domestic constitutional systems of the WTO members may produce states of affairs in which certain social justice goals trump trade goals.

In contrast to the tightness of the GPA non-market provisions around efficiency concepts, the market access provisions give the GPA contracting parties “outs” by converting the GPA into an umbrella arrangement for a series of negotiated arrangements liberalizing only those markets the WTO members could liberalize without running afoul of fairness principles. The non-market access provisions are subservient to the market access provisions; they apply only to procurements liberalized in the annexes.

So far, the good story has been cast in ideal terms. In reality, the GPA market access provisions permit the implementation of social justice policies imperfectly and incompletely. The GPA market access provisions allow GPA contracting parties to keep domestic preferences, provided they can liberalize sufficient numbers and values of other procurements. The United States does this; it opens up substantial procurement markets yet also keeps substantial procurement markets closed, in order to maintain its substantial preference programs. But here lies the potential problem. The extent of a GPA contracting party’s autonomy to pursue its own domestic social justice goals is a function of its ability to offer up on the GPA negotiating table substantial other procurements unaffected by preference programs. Thus, in the GPA context, only contracting parties with substantial import markets in public procurement have substantial policy autonomy. The bottom line is that a GPA contracting party needs market power to implement its own social justice goals in its own municipal legal

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<sup>61</sup> See, e.g., G. Richard Schell, *Trade Legalism and International Relations Theory: An Analysis of the World Trade Organization*, 44 DUKE L.J. 829, 910 (1995).

system. The first story thus has a mixed ending, though this is not controversial, since theories of justice do not easily extend beyond the nation state even in ideal terms.<sup>62</sup>

The second or “bad” story about preferences is that they are wasteful and in some cases unjust. Perhaps the bad story simply brings a measure of realism to the good story. The bad story is that some governments have used public procurement as an enclave in which politics predominates over market-based considerations, to protect favored industries or even to dispense patronage to political friends. In the worst case, corruption diverts scarce public resources to socially wasteful contracts. The result is the typical litany of public policy ills, “corruption, inefficiency, political capture, rent seeking, protectionism, inflated costs, and the development of cartels.”<sup>63</sup> Interest groups are cast in a negative light, as rent seekers. Even without corruption, there is evidence to suggest that preference and other programs that limit competition in procurement are inefficient, poorly suited to the policies they are designed to implement, fail to help the constituencies they are ostensibly intended to help and can do more harm than good.<sup>64</sup> A major concern in the bad story is that protectionism will be institutionalized by what is not liberalized in the GPA market access provisions.<sup>65</sup> In the bad story, the GPA market access provisions have the potential to create a protected enclave of interest groups that make the GPA very difficult to change in a significant way, and thus procurement markets become very difficult to liberalize.

Which story is true? Perhaps the truth lies somewhere in between these two stories. Which version of the story one accepts depends on one’s training and perspective. One can take a nonreductionist view and argue that elements of truth can be found in both stories. The good story accepts both direct and collateral policies as legitimately pursued in public

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<sup>62</sup> There is a substantial literature on the application of theories of justice beyond the domestic level. For a recent discussion, see generally MARTHA C. NUSSBAUM, *FRONTIERS OF JUSTICE: DISABILITY, NATIONALITY AND SPECIES MEMBERSHIP* (2006). Some of the influential writings in this area are CURRENT DEBATES IN GLOBAL JUSTICE (Gillian Brock & Darrel Moellendorf eds., 2005); ALLEN BUCHANAN, *JUSTICE, LEGITIMACY AND SELF DETERMINATION: MORAL FOUNDATIONS FOR INTERNATIONAL LAW* (2004); GLOBAL JUSTICE AND TRANSNATIONAL POLITICS (Pablo DeGrieff & Ciaran P. Cronin eds., 2002); GLOBAL JUSTICE (Thomas W. Pogge ed., 2001); CHARLES R. BIETZ, *POLITICAL THEORY AND INTERNATIONAL RELATIONS* (1999). Some of the literatures do not address the questions of institutions. To the extent it lacks institutional connections; it has a way to go in its direct application in legal contexts.

<sup>63</sup> McCrudden & Gross, *supra* note 15, at 153-54.

<sup>64</sup> See generally Bernard M. Hoekman, *Using International Institutions to Improve Public Procurement*, 13 *WORLD BANK RES. OBSERVER* 249 (1998); JOHN LINARELLI ET AL., *SMALL AND MEDIUM SIZED ENTERPRISES AND EXPORT-LED GROWTH: ARE THERE ROLES FOR PUBLIC PROCUREMENT PROGRAMMES?* (International Trade Centre UNCTAD/WTO 1999).

<sup>65</sup> Linarelli, *supra* note 12, at 262-63.

procurement.<sup>66</sup> Direct policies have to do with buying goods, construction and services on the most efficient basis practicable. The focus is solely on value for money. Collateral policies have to do with pursuing social policies outside of value for money, realizing that some social policies come at a social cost, so long as a political consensus exists on such policies and their costs to society. Of course, what is one WTO Member's social justice is another's protectionism. WTO Members have no obligations to accept one another's social justice policies.

#### IV. CONCLUSION

Merryman was right. We need to keep doing more inquiry about public procurement law and policy. More inquiry might lead to greater understanding and appreciation of the importance of public procurement in both domestic and international legal contexts. As I have tried to explain above, a number of substantial policy issues relate to the operation of public procurement at both the domestic and international levels. These policy issues relate not only to good governance and to the efficiency of markets, but also to fairness and social justice in civil societies.

Based on the above account, two areas seem especially fruitful for further study. First, as for domestic law reform in countries in need of improving their procurement systems, it would seem that the focus should be on capacity development and not just on the production of law and regulation. The law on the books offers little by itself; it is the law in action – the competencies of procurement officials in actually conducting procurement – that matter most. I think that much of UNCITRAL's focus on developing transparent principles relates to the need for competencies in basic procurement disciplines. The rules enacted are designed to direct procurement officials toward core procurement competencies. Second, efforts to broaden participation in the GPA have the potential to expose the rock face of globalization. Without further inquiry, it is unknown at this time, but it would seem that at least as an area for further inquiry that the GPA market access negotiations, in the right cases, has the potential to tell us in stark relief how the domestic policy autonomy of smaller states is effected by international obligations. What we find out remains to be seen, but these are interesting times, as the GPA broadens its participation base.

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<sup>66</sup> For a discussion of these two kinds of policies, *see generally* ARROWSMITH, LINARELLI & WALLACE, *supra* note 19, at 237-322.

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