
Government Procurement

Buy-national procurement rules or other restrictions exist at the federal and subfederal levels in both Pakistan and the United States, and Pakistan is not yet a signatory to the World Trade Organization (WTO) Government Procurement Agreement (GPA). A US-Pakistan FTA would enable less fettered competition for government purchases and thus could deliver considerable benefits to both countries.

This chapter considers the ramifications of a US-Pakistan FTA for government procurement requirements. The first two sections review the regulatory environment and recent developments in the United States and in Pakistan. The third section outlines our recommendations for liberalizing government procurement in the context of a prospective US-Pakistan FTA.

The United States

Regulatory Environment

The United States signed the WTO GPA in 1996 along with 28 other nations. Thus US procurement rules, at the federal level and in most states, are generally applied in keeping with GPA obligations. The agreement, however, does not cover all US federal or state government procurement but only scheduled entities, and even then only for goods and services above certain threshold values. Coverage under the agreement is further restricted by exceptions listed in general notes to the schedules.

At the federal level, US public procurement takes place through various departments supervised by the Office of Management and Budget

(OMB) and two acquisition regulatory councils, the Defense Acquisition Regulations Council and the Civilian Agency Acquisition Council (WTO 2004a). The Federal Acquisition Regulation (FAR) establishes umbrella regulation for all federal entities, but permits them to follow their own internal guidelines (WTO 2004a).¹ Under the FAR, federal entities are obligated to publish their procurement requirements on a Web site known as FedBizOpps when the procurement exceeds \$25,000. The proposed contract must be published at least 15 days before bids begin; thereafter, prospective bidders must be given at least 30 days to place their bids (WTO 2004a).²

At the subfederal level, state and local governments regulate procurement contracts, which are subject to threshold values and other provisions specific to each state. While some states grant preferences to local suppliers and impose local-content requirements, 37 states have adopted the GPA provisions³ and are thus obligated to publish tender invitations on the FedBizOpps Web site for GPA-covered sectors.

The Buy American Act

The Buy American Act (BAA) of 1933 (as amended) is the core document governing US procurement of goods at the federal level. The act establishes discriminatory measures, also known as Buy American restrictions, for government-funded purchases, including supply and construction contracts (European Commission 2004). These restrictive measures can take several forms—prohibiting government entities from purchasing foreign goods and services, requiring a certain amount of local content, and preferring domestic suppliers when evaluating bid prices.

The United States maintains a number of Buy American procurement restrictions that are not covered by the GPA, the North American Free Trade Agreement (NAFTA), the WTO Agreement on Trade in Civil Aircraft, or bilateral procurement agreements with Australia, Chile, Israel, and Singapore (WTO 2004a). BAA requirements apply to goods, not services, and require federal entities to procure only US-mined or US-produced unprocessed goods as well as manufactured articles with at least 50 percent local content (European Commission 2004).

1. The FAR was amended in 2001 to change aspects of electronic procurement and preferential access for small businesses, improve transparency of procedures, and alter bidding processes and thresholds. Part 25 of the FAR deals with policies and procedures to acquire foreign supplies, services, and construction materials (WTO 2004a).

2. Exceptions are made for purchases of perishable supplies when the delayed publication could be damaging (WTO 2004a).

3. The 37 states are listed in Annex 2 of the US GPA schedule (WTO 2002b).

Executive Order 10582 of 1954 goes beyond the scope of the BAA by carving out special status for procurement contracts with small businesses and firms in areas with labor surpluses. The order also allows government entities to reject bids by foreign firms for national interest or security reasons (European Commission 2004).

The Berry Amendment

Like the BAA, the Berry amendment of 1941 provides strict guidelines that require the Department of Defense to prefer US producers when making procurement decisions. It is more stringent than the BAA, however, as it requires 100 percent domestic origin (as opposed to 50 percent under the BAA) and is not limited to contracts in the United States. Some interest groups have lobbied for the extension of the Berry amendment to other US government agencies (such as the Department of Homeland Security), but its provisions currently govern procurement only by the Department of Defense.⁴

As a US ally in the war against terrorism, Pakistan might request, during FTA negotiations, a limited role in Defense Department procurement of textile and clothing. In 2002, the US armed forces purchases of textiles and clothing were estimated at \$2 billion, of which only \$4 million were supplied directly by foreign firms (US Department of Commerce 2003).⁵

The Balance of Payments Program

The Balance of Payments Program is a nonstatutory program that potentially restricts the purchases of supplies by government entities and contracts for the construction, alteration, or repair of any public building outside the United States, such as a US embassy (WTO 2004a). Since 2001, this program no longer applies to civilian agency acquisitions, but it still applies to the Department of Defense for purchases of end products that are used abroad and exceed \$100,000 in cost (WTO 2004a).

4. The Berry amendment has been a subject of debate in recent years. Critics point to the supposed gap between the legislative requirements of the amendment and US productive capacity, particularly in the textile and clothing sector. However, representatives of US textile and clothing firms consistently support the amendment as written.

5. However, the sensitivity of government procurement questions, including the Berry amendment, must be recognized. In the Central American Free Trade Agreement–Dominican Republic (CAFTA-DR) ratification debate, the USTR prominently advertised that the pact made no change in federal or state procurement laws, beyond extending to the new partners procurement opportunities already open to other foreign countries (USTR 2005f).

The Trade Agreements Act of 1979

The Trade Agreements Act of 1979 implemented the General Agreement on Tariffs and Trade (GATT) Government Procurement Code signed in the Tokyo Round. Essentially, it overrides the BAA and related legislation by ensuring national treatment for signatories of the code with respect to scheduled entities and above-threshold contracts (USITC 2004b). Thus, for designated parties the act gives up BAA preferences for civil aircraft and related articles⁶ as well as other end products.⁷

Exemptions and Waivers

Exemptions and waivers to the BAA and Balance of Payments Program are granted if it can be shown that domestic preferences are inconsistent with national interests, and if the supply of a particular material is either unavailable or too expensive in the United States (WTO 2004a).⁸ BAA restrictions have also been waived in acquisitions of defense equipment that originates from countries with which the United States has a reciprocal procurement agreement.⁹

Subchapters VIII and X of Chapter 98 of the BAA list goods that are not subject to customs duties when purchased for use in government contracts. Other supplies may also be eligible for duty-free entry if the contract price is reduced by the amount of duty that would prevail if the supplies did not enter duty free (WTO 2004a). Finally, excepting equipment, supplies destined for government-operated vessels or aircraft are eligible to enter the United States duty free (WTO 2004a).

The WTO GPA and US Bilateral Agreements

As of 2004, the threshold values of procurement contracts covered under the GPA remained at their 1996 levels (WTO 2004a). Table 6.1 shows the

6. Related articles are those that “meet the substantial transformation test of the Act and originate in countries that are parties to the WTO Agreement on Trade in Civil Aircraft” (WTO 2004a).

7. Similar preferences are extended unilaterally to eligible countries through the GPA, NAFTA, other bilateral procurement agreements, and to least-developed countries (WTO 2004a). For example, end products that are granted duty-free entry under the Caribbean Basin Economic Recovery Act (CBERA) are eligible for government contracts.

8. A domestic offer is judged too expensive if the foreign product is priced “below the lowest domestic offer when this offer is from a large business concern” (including import duty and a 6 percent added margin) (WTO 2004a). If the offer is from a small business, the added margin is 12 percent, and for defense-related purchases the price difference has to be a minimum of 50 percent.

9. However, the secretary of defense retains the right to restrict or reject an offer from a qualifying country for national defense reasons.

**Table 6.1 Threshold values of procurement contracts,
WTO GPA and selected US FTAs (dollars)**

Agreement	Supplies	Services	Construction
WTO GPA	169,000	169,000	6,481,000
Canada	25,000	56,190	7,304,733
Mexico	56,190	56,190	7,304,733
Chile	56,190	56,190	6,481,000
Singapore	56,190	56,190	6,481,000

FTA = free trade agreement

WTO GPA = World Trade Organization Government Procurement Agreement

Source: WTO (2004a).

threshold values set by the United States in the WTO GPA schedule, NAFTA, and the US FTAs with Singapore and Chile. Table 6.2 lists the services that the United States has chosen to exclude from the GPA and in selected bilateral FTAs.

The US-Chile and US-Singapore FTAs opened additional state and federal agencies to foreign bids (Schott 2004a). Local procurement is not covered under either the GPA or the two FTAs. Under the US-Singapore FTA, state-level obligations do not extend beyond the sector obligations already committed under the GPA. Under the US-Chile FTA, the 37 US states that have agreed to GPA provisions treat Chilean suppliers in essentially the same manner (USTR 2003c). Finally, the US-Chile and US-Singapore FTAs specify high threshold values, and exclude state set-aside programs for small and minority businesses (Salazar-Xirinachs and Granados 2004).¹⁰

Effect of Restrictions

US government expenditures amounted to \$1.98 trillion in 2002, or 19 percent of GDP. Defense-related expenditures were the largest component, some \$400 billion. Most federal expenditures, however, represent salaries and transfer payments.

10. Government procurement was a source of concern in the CAFTA-DR debate. Congressman Benjamin Cardin (D-MD) attempted to withdraw Maryland from the list of states subject to government procurement rules in the FTA package. However, Deputy US Trade Representative Peter Allgeier ultimately informed Cardin that Maryland “will have to remain on the list of states subject to government procurement rules” in CAFTA-DR. See “Maryland to Remain on Government Procurement Annex for CAFTA,” *Inside U.S. Trade*, July 1, 2005, 5.

Table 6.2 Services excluded or included by the United States in the WTO GPA and selected US FTAs

Service	WTO	NAFTA/Chile	Singapore	Australia/Morocco
Purchase of military services overseas	Excluded	Excluded	Excluded	Excluded
Automatic data processing, telecom, and transmission	Excluded	Excluded	Included	Included
Telecom network, automated news services, data services	Excluded	Excluded	Included	Included
Basic telecommunications network services	Included	Included	Excluded	Excluded
Dredging	Excluded	Excluded	Excluded	Excluded
Federally funded research and development centers	Excluded	Included	Excluded	Included
Department of Defense, Energy, Aeronautics/Space facilities	Included	Excluded	Included	Excluded
Research and development	Excluded	Excluded	Excluded	Excluded
Transportation services	Excluded	Excluded	Excluded	Excluded
Utility services	Excluded	Excluded	Excluded	Excluded
Maintenance, repair, rebuilding, installation of equipment related to ships, including nonnuclear ship repair	Included	Excluded	Included	Excluded

FTA = free trade agreement

NAFTA = North American Free Trade Agreement

WTO GPA = World Trade Organization Government Procurement Agreement

Source: Integrated Acquisition Environment, Federal Acquisition Regulation, www.arnet.gov/far.

The European Commission has estimated that BAA restrictions each year affect approximately \$25 billion of public contracts, most noticeably in mass transport and airport improvements (European Commission 2004).¹¹ Restrictions under the BAA and the Berry amendment would discourage Pakistani firms from participating in US procurement of goods such as textiles and clothing or medical devices.¹²

US public procurement restrictions are implemented on three levels: federal restrictions on procurement by federal entities, state restrictions on state and local procurement contracts, and federal restrictions on the use of federal grant money by state and local governments (USITC 2004b). At the federal level, the major restrictions relate to defense procurement contracts and small and minority-owned business contracts. At the state level, federal regulations (mostly BAA restrictions) prohibit the use of federal grant money in transportation and food assistance projects (USITC 2004b).

Public Transportation

Federal aid to state and local governments for public transportation is distributed by the Department of Transportation under the Highway Administration Act, the Urban Mass Transit Act, and the Airports Improvements Act. The federal government may fund 40 to 80 percent of a project while the state funds the rest. Regardless of the percentage of federal funding, all public transportation projects are subject to local content requirements of 60 percent (or, if they fall short of that minimum, a penalty of up to 25 percent of the price) (European Commission 2004).

Highway Construction

Federal assistance for highway projects amounted to \$46 billion in 2002, while federal grants to state and local governments for highway construction totaled \$26 billion (USITC 2004b). Under the BAA, highways must be constructed with domestically produced iron and steel. A waiver is possible but is rarely granted.

Airport Construction

The Federal Aviation Administration monitors BAA restrictions on state and local public procurement for airport construction projects. Some 80

11. This figure is expected to increase to \$35 billion in 2005 (European Commission 2004).

12. According to the latest US notification of government procurement statistics to the WTO, total US federal government procurement of textiles and clothing in 1999, subject to GPA provisions, was around \$70 million. That same source reported expenditures on medical appliances and precision and optical instruments, subject to GPA provisions, of about \$1 billion (WTO document GPA/40/Add.4).

to 90 percent of airport construction spending comes from the federal government. Airport construction projects are obligated to use domestically produced steel and manufactured goods unless a waiver is invoked.

Food Assistance

Many food assistance procurement programs are monitored by the US Department of Agriculture and other federal entities (e.g., the Department of Health and Human Services). These programs, such as the National School Lunch Program and the Child and Adult Care food program, give preferences to local food suppliers. Even donated commodities must be of domestic origin. Some programs require that school food authorities buy domestic commodities to the maximum extent possible (USITC 2004b). However, under NAFTA and the Uruguay Round agreement, the United States retained the right to exempt from its national treatment obligations the “procurement of agricultural goods made in furtherance of agricultural support programs or human feeding programs” (USITC 2004b).

Small Business Set-Asides

Federal grants and subcontracts awarded to small business firms are governed by the Small Business Act of 1958 (SBA) (as amended), which establishes certain targets for the procurement of goods and services: 23 percent of prime contracts must be awarded to small businesses, 5 percent of prime and subcontracts to minority-owned businesses, 5 percent to woman-owned businesses, 3 percent to service-disabled veteran-owned businesses, and prime contracts for Historically Underutilized Business Zone (HUBZone) firms were phased in from 1 percent in fiscal 1999 to 2.5 percent in fiscal 2002 and 3 percent in fiscal 2003 (USITC 2004b). The SBA requires that all owners of small businesses be US citizens to qualify for preferential procurement. Because SBA regulations require that receipts of all domestic and foreign affiliates of the business be counted in determining whether the firm qualifies as a small business, US affiliates of foreign-owned corporations usually cannot obtain small business status. Most federal purchases under the SBA programs face BAA restrictions, although a general waiver may be granted for federal purchases of less than \$2,500 (USITC 2004b).

Defense Procurement

The BAA governs domestic sourcing requirements for defense procurement. In addition, the Defense Federal Acquisition Regulations System (DFARS) covers defense-related procurement of specific products such as

food, clothing and fibers, vessels, and anchor chain (USITC 2004b). DFARS is also intended to ensure that government procurement contracts comply with the memorandum of understanding (MoU) between the Department of Defense and SBA with respect to the small-business goals mentioned above (USITC 2004b). The North Atlantic Treaty Organization (NATO) countries that have ratified the MoU can obtain a waiver from the Department of Defense's domestic preferences (USITC 2004b).

State and Local Government Procurement

States impose procurement restrictions over and above the restrictions imposed by federal rules. So far, all negotiated US trade agreements have given states the choice to retain their state procurement rules or accede to the agreement; 37 of the 50 states have chosen to accept the GPA provisions in the WTO, and the same states have generally accepted similar FTA provisions. According to the most recent data reported by the United States to the WTO, in 1999 total procurement by all states that had acceded to GPA provisions reached \$306 billion (WTO document GPA/40/Add.4). For the US FTA partner, the benefits of state accession include the opportunity to transcend the large number and diverse nature of state programs (USITC 2004b). As of 2005, Georgia, Indiana, New Jersey, Ohio, and Virginia were among the important holdout states.

Subfederal Selective Purchasing Laws

Selective purchasing laws at the subfederal level often block transactions with foreign firms that have links to "offensive" third countries, such as Burma. Penalty laws have been adopted by Massachusetts as well as 20 cities and local authorities (European Commission 2004). While the Supreme Court ruled that a Massachusetts law was preempted by federal legislation (*Crosby et al. v. National Foreign Trade Council*, U.S. Sup. Ct., No. 99-474, June 19, 2000), the holding had a narrow legal focus. Hence municipal selective purchases on foreign policy grounds can still be a problem. For example, in 2001, New York attempted to apply selective purchasing legislation based on the so-called MacBride principles, which are a code of conduct developed in Northern Ireland to address the problem of workplace religious discrimination. (European Commission 2004). The proposal was dropped, but it flagged a continuing concern.

Services

While the BAA is not supposed to apply to procurement of services, the offshore outsourcing debate has inspired new legislative forays, mainly at the state level. In 2002, New Jersey (followed by Michigan in 2004) enacted legislation stating that "only citizens of the United States and

persons authorized to work in the United States pursuant to federal law may be employed in the performance of services [funded by the state]" (European Commission 2004). Connecticut, Florida, Maryland, Missouri, and Wisconsin have announced the implementation of similar provisions (European Commission 2004). The aim of this legislation is to discourage the establishment of "call centers" and data processing services abroad (European Commission 2004).

Recent Developments

Recent initiatives have attempted to improve the efficiency of federal government procurement. The E-Government Act of 2002 led to the creation of an Internet portal for government procurement known as the Integrated Acquisition Environment initiative. In addition, the General Services Administration (GSA) has promoted two new programs. GSA Global Supply identifies an array of goods and services that conform to government acquisition policies and socioeconomic regulations (WTO 2004a). GSA Advantage is an Internet program that allows interested parties to communicate with authorized contractors online; under this program, 5,298 contracting foreign firms registered online in 2004 (WTO 2004a).

Pakistan

Pakistan's total government procurement market for goods and services in 2004–05 was roughly estimated at Rs. 224 billion (\$3.8 billion) or 5 percent of GDP (Government of Pakistan 2005a, IMF 2003). However, Pakistan is not a signatory of the GPA and has not made a commitment to begin accession negotiations. Political influence on procurement decisions, charges of official corruption, and long delays in bureaucratic decision making have been noted. Investors have also reported instances of the government using the lowest bid as a basis for further negotiations rather than accepting it under the established tender rules. Occasionally the government has "disqualified" experienced and technically proficient bidders that were qualified under tender specifications (USTR 2005d). Reducing corruption in the civil service, particularly at the provincial and local levels, is a major challenge for Pakistan,¹³ and procurement practices are on the front line of this battle.

Pakistan's National Accountability Bureau has a mandate to investigate alleged corruption. Its efforts are complemented by individual re-

13. Pakistan ranks 144 out of 158 nations in Transparency International's 2005 Corruption Perceptions Index.

gional accountability bureaus in each of the country's four provincial capitals and one in the federal area. If effective, these accountability bodies will help reduce corruption in public procurement.

Domestic legislation on government procurement dates back to 1972, and was amended most recently when the Pakistani government established the Public Procurement Regulatory Authority (PPRA) in May 2002 to strengthen procurement practices through increased transparency, accountability, and governance. In June 2004, the authority published detailed public procurement rules that are compatible with international best practices and that cover all agencies owned or controlled by the federal government, except those related to national security or the defense forces (PPRA 2004).

In accordance with the PPRA rules, work performed for federal agencies, including the purchase of imported equipment and services, is now customarily awarded through tenders that are publicly announced or issued to registered suppliers. The procurement of services is generally subject to the same procedures as the procurement of goods, although additional technical negotiations are required for services. Sole source contracting using company-specific specifications has been eliminated (USTR 2005d). All procurement opportunities over Rs. 40,000 (\$675) must be published on the PPRA's Web site, and opportunities exceeding Rs. 1 million (\$16,860) must also be published in the print media. In addition, an "integrity pact" must be signed between the procuring agency and the suppliers or contractors for procurements exceeding Rs. 10 million (\$168,600) (ADB/OECD 2004).

While Pakistan has no "buy national" policies, the government does not invite private tenders for the transportation of crude oil. All transport of crude oil must be conducted by the state-owned Pakistan National Shipping Corporation.

Transparency International has monitored the enforcement of Pakistan's public procurement rules 2004 and has been consulted in connection with procurement contracts awarded by various bodies—the City of Karachi, Pakistan Steel, Pakistan Telecommunication Company Ltd., and the Ministry of Irrigation and Power of Sindh Province. Transparency International's findings indicate better governance, with the prospect of sustained improvement (Transparency International 2005).

Recommendations

Practices that impede competition in public procurement cannot be abolished overnight. Nevertheless, the US-Pakistan FTA should be ambitious and forward-looking. For budget reasons alone, public authorities in both countries should welcome greater competition. In addition, Pakistan should welcome the salutary impact of open procurement rules in its

anticorruption campaign. With those goals in mind, we offer the following recommendations.

For the United States

- The US-Pakistan FTA should grant Pakistani firms the best terms enjoyed both under the GPA and by the NAFTA partners, Australia, Chile, Singapore, and future US bilateral FTA partners (i.e., an unconditional most favored nation [MFN] provision). The MFN provision should apply to both federal and state procurement.
- Without undercutting the thrust of the BAA or the Berry amendment, the United States should work toward extending its procurement coverage for Pakistani exports such as textiles and clothing and medical instruments. For example, negotiators of a US-Pakistan FTA should explore the possibility of relaxing origin requirements to facilitate procurement of Pakistani goods by US firms that supply the Department of Defense, particularly in overseas contracts.
- The USTR should seek to include two or three “holdout” states (in addition to states that have previously agreed to GPA or FTA procurement provisions). Likely candidates might be Georgia, New Jersey, and Virginia.

For Pakistan

- Pakistan should commit to accede to the GPA, in the context of the Doha Round. Accession will help Pakistan rationalize its own public procurement system and ensure the continued progress of domestic reform.
- In the proposed FTA, Pakistan should schedule the same type of procurement obligations (allowing for similar reservations) as the United States has scheduled in the GPA and in its FTAs. Pakistan’s commitments should mirror those stipulated by the GPA for developing countries and those of Central American Free Trade Agreement-Dominican Republic (CAFTA-DR) for US partners.
- The FTA should grant US firms the best terms enjoyed under the GPA as well as by Pakistan’s current and future bilateral FTA partners (i.e., an unconditional MFN provision). The unconditional MFN provision should apply to both federal and provincial procurement.