



US-China Business Council Comments on Draft Implementing Regulations on the PRC Government Procurement Law

The US-China Business Council (USCBC) represents more than 220 US companies that conduct business across all manufacturing and services sectors in China. Over the years, our member companies operating in China have taken a deep interest in the development and implementation of China's legal framework for government procurement. USCBC would like to thank the State Council Legislative Affairs Office for this opportunity to provide comments on the draft Implementing Regulations for the PRC Government Procurement Law and hopes that these regulations will be finalized and promulgated as soon as possible.

Our comments are focused on the following important areas.

Products Eligible for Government Procurement

We are very pleased to see that Article 10 of the draft law defines “domestic good” and “domestic project and service” in ways that will include all enterprises in China, regardless of ownership. In this era of international trade and investment, it is important that governments adopt definitions of goods, projects, and services that reflect international best practices. We commend the drafters for providing a definition that focuses on the good or service rather than on the company's ownership.

We note, however, that the draft does not quantitatively define local content thresholds, an important aspect for companies to understand when looking to comply with the new regulations. To ensure consistency and transparency, we respectfully request that the draft implementing rules include the specific local content threshold; that this threshold be no greater than 50 percent value added in China (as in the 1999 Ministry of Finance *Interim Measures for the Administration of Government Procurement*); and clearly state that the threshold apply equally to all enterprises in China (or legal persons), including Chinese-owned and foreign-invested enterprises.

USCBC appreciates the drafters' efforts to ensure fairness in the definition of a domestic good, project, and service. Occasionally, foreign-invested enterprises encounter differences with how local governments interpret the term “domestic” or “Chinese.” To minimize implementation inconsistencies, we respectfully suggest that language in the second paragraph of Article 10 be amended to read “Chinese citizen, legal person, or other organization that is established according to Chinese law.”

Finally, the draft designates to relevant authorities the responsibility for drafting specific standards related to determining domestic goods, projects, and services. We respectfully request that all subsequent administrative regulations, notices, and guidance be open for a public comment period of at least 30 days.

Scope of Government Procurement and Use of Fiscal Funds

We recommend that the implementing regulations clearly state that the scope of government procurement be limited to purchases made by government departments and not be expanded to purchases made by state-owned enterprises, as well as by hospitals or other such non-governmental agencies. More specifically clarifying the types of entities covered by the regulations beyond the general description in Article 2 of the Government Procurement Law would help eliminate inconsistencies in implementation.

In addition, Article 2, paragraph 2 of the draft extends the type of funds that can be used for government purchases to include loans obtained by public institutions and organizations that are guaranteed by state assets. In principle, these loans could be repaid using funds that may not be backed by state assets, including the borrower's future available capital. Such a purchase would be a commercial purchase—not a government purchase—since it would not be backed by treasury funds. This causes confusion regarding the scope and nature of government procurement, since all public government agencies should be fully funded by the treasury budget. We respectfully suggest that paragraph two be shortened to “loans that have fiscal funds as the source of repayment shall be treated the same as fiscal funds.”

Article 2 further states that procurement officers can make government purchases using “partial” fiscal funds. Cases in which government procurers lack sufficient funds so that they must source funding through commercial loans to make purchases would normally subject the project to the existing Bidding and Tendering Law. This ensures the legitimate interests of the project's financial backers. To prevent confusion and maintain the distinction between government and commercial projects, we respectfully suggest that the word “partial” be deleted from the final draft.

Threshold for Price Preference

Many countries allow or require government entities to preferentially procure domestically produced items unless they are “unreasonably” expensive relative to a competing import. The draft regulations define “unreasonable commercial terms” to mean that the price of domestic goods, projects, or services is at least 20 percent higher than those of non-domestic competition. If a price of a domestic offering is “unreasonably” higher than its foreign counterpart, it should not receive preference in procurement. The 20 percent price advantage reserved for domestic companies should be balanced against the efficient use of fiscal funds, with the margin not being so large as to distort market mechanisms that incorporate quality and research and development (R&D) investment. For this reason, we respectfully suggest that the threshold be lowered to a specific percentage in the 5 - 10 percent range, which would be consistent with preferences in many other countries.

Definition of Territory

Article 11 of the draft implementing regulations reiterates the definition of an imported product, which was originally codified in the Administrative Measures for Government Procurement of Imported Products released by the Ministry of Finance in December 2007. Subsequently, the August 2008 Notice on Related Issues on Administrative Measures of Government Procurement of Imported Products explained that products made in China's special customs zones from imported materials are not considered imported goods and are not subject to government procurement restrictions for imported products. To ensure regulatory consistency on the treatment of goods produced in China's special customs zones, we respectfully suggest that Article 11 of the draft implementing regulations incorporate the August 2008 notice into its definition and uses "Chinese territory" (defined as including special customs zones) consistently throughout the draft implementing regulations and subsequent related measures.

Indigenous Innovation Products

USCBC supports the PRC government's effort to build its national innovative capacity and understands the role that companies play in elevating a country's industrial base along the value chain. Foreign companies have contributed to China's development as an innovative economy in many ways, such as by training technicians and management in the latest methods, refining marketing and communication systems, developing new products, and establishing R&D centers. USCBC members have typically invested in China to serve China's market. They employ Chinese citizens, pay taxes in China, and contribute to the overall economic and technological development of China. In many cases, US parent companies have licensed certain technology to their China subsidiaries or have adapted or developed new products for China, thereby bringing innovative products, technologies, and best practices to China's market and customers, even if the original patent or trademark is owned in another jurisdiction.

Article 9 of the draft implementing regulations gives preference in government procurement to national indigenous innovative products (NIIP). USCBC respectfully requests that the drafters remove NIIP from the list of preferred products in Article 9 in the draft implementing regulations. More effective and internationally proven ways to promote innovation include the development of various tax incentives, R&D grants and support programs, competitive commercial prizes, and other incentives that are open to all enterprises in China, regardless of ownership.

We also suggest that "compulsory" purchasing be deleted from this article.

Government Procurement Standards

It is apparent from Article 6 that drafters aim to avoid situations where one potential supplier may develop a monopoly in or have their products designated as the standards for government procurement. USCBC appreciates this effort to guarantee due process in government procurement. As currently worded, however, the draft regulations could limit the disclosure of necessary technical information to prospective bidders. We believe this was not the intent of the drafters but rather that the drafters meant to ban any reference to the technical aspects of a

particular supplier's or mark's product. Therefore, we respectfully suggest the clause be revised with the following addition: "shall not designate specific suppliers or specific brands of goods, nor shall they enact technical specifications that point to specific supplier's or mark's products, nor shall they include unreasonable restrictive conditions."

Various provisions within the draft implementing regulations contain within them the principles of civil liability—public liability and professional liability—to ensure quality goods, projects, and services. Another way that drafters can increase accountability of manufacturers and service providers is to require companies that want to provide products and services to the PRC government to submit proof of product liability insurance as part of procurement bid applications.

Central and Local Authority

Articles 8 and 115 allow provincial and county-level governments to issue their own procurement catalogues and implementation measures in accordance with local standards. This, however, appears to be in conflict with Article 87 of the Government Procurement Law, which authorizes only the State Council to enact implementation measures. With more than 2,000 counties nationwide, conflicts in the interpretation of relevant national-level procurement laws and regulations, as well as possible local protection by various provinces, are a real possibility. USCBC therefore respectfully recommends that central-level authorities further limit the scope of Article 8 within which local governments may draft their own catalogues and delete Article 115 entirely.

Conclusion

The US-China Business Council would like to thank the State Council again for providing this opportunity to comment on the draft implementing regulations. We hope these comments will prove constructive and useful to the State Council as it develops China's government procurement system. USCBC welcomes any feedback the State Council may have and hopes to have the opportunity to discuss the contents and provisions of the draft more fully.

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