THE INTERNATIONAL PROCUREMENT INSTRUMENT (IPI): PROMOTING A LEVEL PLAYING FIELD AROUND THE WORLD

This article provides a summary of the latest trends and policy developments in the area of international public procurement, with a special focus on the recently adopted International Procurement Instrument by the European Union (EU). The EU public procurement market is one of the largest and most accessible in the world. However, many of the EU’s major trading partners apply restrictive practices in their markets that discriminate against EU businesses. Faced with this asymmetry, the IPI allows the EU to advocate more effectively for open international public procurement markets.

El Instrumento de Contratación Pública Internacional (ICPI): promover la igualdad de condiciones en todo el mundo

Este artículo ofrece un resumen de las últimas tendencias y novedades políticas en el ámbito de la contratación pública internacional, con especial atención al Instrumento de Contratación Pública Internacional, recientemente adoptado por la Unión Europea (UE). El mercado de contratación pública de la UE es uno de los mayores y más accesibles del mundo. Sin embargo, muchos de los principales socios comerciales de la UE aplican en sus mercados prácticas restrictivas que discriminan a las empresas comunitarias. Ante esta asimetría, el ICPI permite a la UE abogar más eficazmente por unos mercados internacionales de contratación pública abiertos.

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1. The importance of public procurement

Public procurement expenditure has always represented an important part of the world economic activity. The relative importance of public procurement has continuously grown, especially in recent years. For instance, across the OECD countries, public procurement (in percentage of GDP) increased from 11.8% of GDP in 2008 to 12.6% of GDP in 2019. In 2020, the COVID-19 pandemic led to a significant increase in public procurement relative to GDP, due to a double effect: an increase in public spending and a GDP contraction. Among those EU countries that are also OECD members, public procurement increased from 13.7% of GDP in 2019 to 14.9% of GDP in 2020. Other countries also saw significant increases in the share of public procurement expenditures (e.g. in Norway from 15.8% to 17.1%, and in the United Kingdom from 13.2% to 16.1%) (OECD, 2021).

Public procurement is not only important for the OECD region. Worldwide, public procurement amounted to $11 trillion, out of global GDP of nearly $90 trillion in 2018 (Bosio & Djankov, 2020). The cumulative size of global public procurement is equivalent to the cumulative GDP of India, Brazil, Mexico, Indonesia, and the entire Sub-Saharan Africa (IMF, 2022). Hence, public procurement is not only important in developed countries but also in the developing world. In countries like Brazil, India, Pakistan, South Africa, Egypt, Morocco, Turkey and Vietnam, the size of public procurement accounts for over 20 percent of their GDP (Bosio & Djankov, 2020).

Just like the private sector, the public sector also requires a combination of domestic and imported goods and services. No single country has a comparative advantage in everything, hence public spending offers significant opportunities for international procurement. However, despite this potential, public procurement is notoriously subject to a «home bias» effect and a large number of discriminatory measures. Historically, public procurement contracts around the world have largely been awarded to domestic companies. In many countries, domestic companies receive more favourable treatment via «buy national» or «buy local» preferences than foreign companies, which may alter the sourcing decisions of both procuring entities and potential bidders.

The combination of a large share of government expenditures in GDP and the «home bias» characteristics makes public procurement one of the few fields in which liberalisation efforts at international level have substantial untapped potential for economic gains, both for public authorities and economic operators.

Many policymakers and academics have strived to promote the best «policy mix» that would maximise the efficiency gains from international procurement. Greater competition from foreign bidders will lead to greater competition for public procurement contracts, leading to lower prices and higher quality products and services, especially in sectors affected by monopolistic competition. Liberalisation efforts in the area of government procurement started at multilateral level as early as 1979, leading to the adoption of the plurilateral Government Procurement Agreement (GPA) under the aegis of the World Trade Organization (WTO).

The legal provisions contained in the WTO GPA and in the growing number of FTAs (free trade agreements) that include procurement chapters are important in reducing the «home bias» effect and in promoting openness and participation of foreign bidders across all procurement modes. The GPA agreement has evolved over time in terms of its membership and legal coverage. The fundamental aim of the GPA, having transparency and non-discrimination at its core, is to mutually open government procurement markets among its parties. As a result of several rounds of negotiations and continuous accessions to the GPA, the GPA parties have opened procurement activities estimated to be worth more than US$ 1.7 trillion annually to suppliers from the GPA parties offering goods, services or construction services (WTO, 2022). So far, only a small set of countries (48 WTO members) undertook binding commitments to open up their procurement markets to foreign goods and service suppliers by acceding to the GPA. While the GPA requires the coverage of goods, services and
works at central and sub-central levels for procurements above a certain threshold, a significant share of the GPA parties’ public procurement markets is still not subject to GPA legal commitments. In contrast, the EU has taken legal commitments under the GPA covering around, or in some years above, 70% of the total value of the above-threshold EU procurement (WTO, 2020). While the parties are expected to offer relevant coverage when acceding to the GPA, there is still the possibility to exclude certain goods, services and works as well as procuring entities from its coverage.

Lately, the importance of liberalizing public procurement markets was recognized not only as part of the GPA negotiations but also in a bilateral/regional context. A growing number of recent free trade agreements (FTAs) contains legally binding public procurement provisions with various degrees of liberalization ambition. Binding commitments to liberalise public procurement markets are a standard feature of the modern FTAs negotiated by the EU in recent years.

2. A typology of international public procurement: the three modes of supply

Given the high economic stakes involved, the importance of liberalizing public procurement markets has received growing attention by policymakers in recent years. For instance, two decades ago, no EU FTA had a full-fledged public procurement chapter. Nowadays, virtually all new EU FTAs have an ambitious procurement chapter with binding rules and concrete market opportunities offered for international procurement.

To properly assess the importance of international procurement, it is important to consider the so-called procurement «modes of supply», a concept already widely used in services negotiations. As in the case of services trade, irrespective of the type of contract (i.e. goods, services, works), public procurement contracts can take place under different procurement modalities. Differentiation can be made between three key dimensions in international public procurement:

1) the nationality of the firm;
2) the location of the bidding firm (e.g. located abroad or domestic subsidiary of a foreign firm);
3) the origin of the value-added along the supply chains involved in the execution of the public procurement contract, irrespective of the location and nationality of the companies winning the public contract.

To illustrate these concepts, let us consider an infrastructure project involving either setting up a new 5G mobile telecom network, or a new power grid, a railway upgrade or simply constructing a new public building. In all of these cases foreign companies can participate through the various channels outlined above.

Foreign companies can bid directly from abroad or, if they have a local presence, they could bid via their local subsidiaries. Irrespective of their bidding strategy, if they win the procurement contract, foreign companies will use a combination of domestic and imported goods and services needed for the public project. Even if the public contract is won by a domestic firm, there can still be an element of indirect international procurement that is involved, as foreign companies can be subcontractors or merely suppliers of certain parts and/or intermediate services to a domestic company that will carry out the project.

Based on these key dimensions, Cernat and Kutlina-Dimitrova (2015) defined three modes of supply for international public procurement:

- **Mode 1 procurement** – a foreign company submitting and winning a public contract «from abroad»;
- **Mode 2 procurement** – a domestic subsidiary of a foreign company winning «locally» a public contract;
- **Mode 3 procurement** – a foreign company participating indirectly in a bid by providing intermediate goods and services.

In the case of the EU, where all procurement modes are taken into account, international procurement accounts for a sizeable share of the total value of public procurement that is subject to international commitments. Cernat and Kutlina-Dimitrova (2020) estimated that, in 2017, the value of international procurement across
all modes was in the range of 50 billion euros, with mode 2 accounting for the biggest share of total international procurement (Figure 1). For that year, the value of EU public procurement contracts covered by the GPA amounted to around 360 billion euros. In percentage terms, this means that foreign companies won around 14% of the EU procurement value open for international procurement. The EU openness in public procurement is by and large comparable with the overall openness of the EU economy: in 2017, the share of EU imports (goods and services) in GDP was around 17%.

Hence, one can consider this difference in import penetration shares as an indication of a potential «home bias» effect in EU public procurement compared to the private sector. However, a limited «home bias» effect in EU public procurement covered by international obligations can be expected and is most likely driven by structural features, rather than triggered by discriminatory policies or protectionist measures. As argued by Mulabdic and Rotunno (2022), a certain degree of «home bias» in public procurement compared to private markets is to be expected due to two reasons: i) they tend to source more goods and services locally; and ii) they spend more on certain services (e.g., construction, public works, education, health services) where the share of imports is lower than for goods or business-related services. So, whereas the first effect can be considered potentially discriminatory, the second cause of «home bias» in public procurement is structural.

Compared to the 2017 data, the importance of reciprocal openness in public procurement across all modes of supply (but notably in terms of resilient global supply chains underpinning mode 3) has increased in the post-COVID-19 period. Many policymakers have realised that no country is an island, and no country can cope alone with the sudden, multiple shocks that affected our economies and societies in recent years. Even the most developed and diversified economies would need to procure certain goods and services from abroad. To ensure an effective and efficient public policy

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**FIGURE 1**

FOREIGN PARTICIPATION IN THE EU PROCUREMENT MARKET BY MODES OF SUPPLY

EU procurement is open to foreign firms

Value of EU public contracts won by foreign firms, under different modes of supply

50 billion euros/year

Mode 1

Mode 2

Mode 3

SOURCE: Based on Cernat and Kutlina-Dimitrova (2020).
response, governments around the world had to increase public spending and the share of public procurement in GDP increased since 2019. A simple extrapolation from 2017 to 2022 would suggest (as a rough, indicative estimate of its magnitude) that the size of the EU procurement covered by international commitments has surpassed 500 billion euros in 2022.

When taking into account the health-related spending during the COVID-19 pandemic, as well as the inflationary tendencies in recent years, one can well imagine that the size of EU public procurement covered by international commitments reached close to 600 billion euros in 2022. Hence, if we assume the same level of EU procurement openness (14%) across all three modes of supply as indicated above, one could estimate that the value of EU public procurement awarded to foreign companies was around 80 billion euros in 2022. In recent years, there are reasons to believe that the share of international procurement has probably increased, at least in some critical sectors, faced with an acute need to rely on diversified and resilient global supply chains to guarantee that public authorities have at their disposal all the necessary equipment, goods and services required to carry on their responsibilities during challenging times. Think of the importance of international trade in medical equipment (protective equipment, masks, ventilators) and vaccines during the COVID-19 pandemic. The WTO estimated that over 15 billion doses of COVID-19 vaccines were produced worldwide, as of May 2022. Out of them, more than six billion doses (more than 40%) were produced for third countries and exported. As vaccines are typically part of public procurement procedures, this example is illustrative of the growing need for a well-functioning international procurement market.

3. The growing trend towards protectionist measures in international procurement

Despite the multiple reasons for governments to promote open procurement and the fact that many trade agreements introduce legal obligations to ensure such openness, there is a tendency in the opposite direction to introduce discriminatory measures in favour of domestic firms in public procurement procedures. Although some procurement barriers have been in place for decades, the current geopolitical and economic environment is conducive to a record number of protectionist and discriminatory measures affecting international public procurement.

One major difficulty that hampered any systematic effort to quantify and address the extent to which various barriers are detrimental to international procurement was the lack of a clear taxonomy of barriers and their level of restrictiveness. A first notable attempt to address this gap has been undertaken by OECD (2017) as part of their efforts to establish a global taxonomy of public procurement barriers that is comparable across countries and aligned with the WTO GPA provisions and the UNCITRAL Model Law on Public Procurement. Another valuable effort has been carried out by the Global Trade Alert (GTA) project, an independent initiative aimed at monitoring policies affecting global trade since 2008, including those affecting public procurement based on the OECD taxonomy. The GTA database indicates a worrying upward trend in the number of restrictive and discriminatory measures against international procurement (Figure 2).

The GTA data collection effort indicates that, over time the number of liberalising measures nearly disappeared during the 2009-2017 period. In contrast, the number of protectionist measures increased steadily from 2009 until 2017 and quadrupled between 2017 and 2022, reaching almost 700 protectionist measures. Among the countries driving these trends we find both developing countries but also developed ones. A similar picture emerges from the OECD-led effort as part of its procurement taxonomy development, or the EU International Public Procurement data collection project. Some of the types of procurement barriers identified are illustrated in Figure 3.

One interesting finding from these data collection efforts is the prevalence of traditional procurement
barriers, such as market access restrictions (e.g. contracts reserved to domestic suppliers only) domestic price preferences (e.g. in India and Tunisia local suppliers are preferred over foreign competitors even if their offers are several percentages more expensive), or local content requirements (e.g. requirements for local employment and job creation, the mandatory use of domestic inputs, etc.). Some countries also impose discriminatory qualification or technical evaluation requirements (e.g. requirements for local employment and job creation, the mandatory use of domestic inputs, etc.). Some countries also impose discriminatory qualification or technical evaluation requirements (e.g. prior experience in the country required, use of technical standards that favour domestic producers, certification and licensing requirements, nationality requirements for key experts, etc.).

Another interesting finding is that some procurement barriers stem from collateral policy actions. This type of barrier is prevalent in countries such as China, Indonesia, or Thailand. In many cases, such restrictions are related to foreign direct investment (FDI) barriers. As shown in Figure 1, given the importance of mode 2 procurement, if foreign companies are prevented from investing in certain sectors, FDI barriers become procurement barriers for those sectors. Barriers to FDI in the country where the procurement takes place can prevent access to procurement in sectors where local presence or joint ventures are required for the execution of the contract. Similarly, discriminatory subsidies or tax measures may prevent foreign bidders from competing on a level playing field for public procurement contracts. Finally, lack of transparency in investment and trade policies are also likely to discourage or disadvantage foreign bidders who are interested in public procurement contracts.

![Figure 2: The Evolution of Public Procurement Measures Across the World (2009-2022)](image-url)
4. The EU policy response: why the International Procurement Instrument (IPI) is more relevant than ever?

Faced with the growing number of protectionist measures affecting international procurement, and in the absence of international commitments by the vast majority of WTO members in this area, the European Union had to consider alternative instruments to tackle these procurement barriers and, in 2022, the EU adopted the International Procurement Instrument (IPI). The adoption of the IPI was a long and protracted process. The European Commission Communication on Trade, Growth and World Affairs launched in 2010, and the Single Market Act adopted in 2011 highlighted fair competition and access to public procurement markets as one of the key tools for economic growth and job creation. In October 2011, the European Council urged the Commission to present a proposal for an International Procurement Instrument (IPI). The Commission followed up on the Council recommendation and, in 2012, proposed a draft IPI Regulation aimed at opening up public procurement markets in third countries and ensuring EU business had fair access to them. In spite of strong and unanimous political endorsing of the imperative need for a level playing field in international public procurement, the EU Member States were unable to reach an agreement on several key parameters in the IPI legislative proposal for several years. Faced with a gridlock in the Council, the European Commission submitted a revised version of the IPI Regulation in 2016. Although the revised and simplified IPI proposal...
addressed some of the concerns laid out by various Member States, it remained a difficult file in the Council. It was only during the Portuguese Presidency in the first half of 2021 that the IPI file made significant progress in the Council. One year later, the IPI Regulation became a key priority for the French presidency and was finally adopted by the co-legislators in June 2022.

Although it took a decade for the IPI to be adopted, it is an essential instrument for the EU strategy aimed at strengthening global competitiveness of EU companies and the bargaining power of the European Union in the field of public procurement. Several EU sectoral associations for whom access to third countries procurement markets is crucial (e.g., construction, rail equipment, public transport, healthcare, power generation, etc.) have been advocating in favour of IPI to be adopted and welcomed its successful conclusion. Public procurement remains a difficult area to liberalise via binding trade agreements and a large share of international procurement at global level is not covered by any legal commitments. Therefore, the IPI as a new element to the EU trade policy toolbox, fills an important gap in EU policymaking.

The IPI empowers the EU to initiate investigations in cases of alleged restrictions in third country procurement markets, engage in consultations with the country concerned on the opening of its procurement market and, if all attempts failed, reciprocate with proportionate restrictions in the EU procurement market against those countries. The functioning of the IPI Regulation can be summarised in several steps (Figure 4).

The main objective of the IPI Regulation is to provide the EU with a legal instrument to remove barriers abroad and obtain a level playing field in third country procurement markets for EU businesses. Under article 5 of the IPI Regulation, the Commission may initiate an investigation into an alleged third-country measure, either based on a substantiated complaint by a Union interested party or a Member State, or as an ex officio investigation. The European Commission will publish a notice of initiation in the Official Journal of the European Union. At the same time, in line with article 5(2), the Commission shall invite the third country concerned to submit its views, provide relevant information and enter into consultations with the Commission in order to eliminate or remedy the alleged third-country measure or practice. The investigation and consultations shall be concluded within a period of nine months after the date of their initiation. In justified cases, the Commission may extend this period by five months by publishing a notice in the Official Journal of the European Union and informing the third country, interested parties and Member States of that extension.

Where the Commission, based on its investigation and consultation process with the third country, determines that the third country has taken satisfactory corrective actions to eliminate or remedy the serious and recurrent impairment of access of EU companies, goods or services to the public procurement market of the third country, it will terminate the IPI investigation and publish a notice of termination in the Official Journal.

As a last resort, the Commission could apply measures that would result in restricted access to the EU procurement market. To avoid the application of such measures, third countries would only need to rectify the restrictive practices that are subject to an IPI investigation. The Commission could apply restrictions to the access to the EU’s procurement markets and, as per article 6 of the IPI Regulation, adopt IPI measures in a form of adjustment in the assessment of the tenders from the country concerned (so called price and score adjustment measure\(^1\)), or in a form of an exclusion\(^2\) of the tenders from the country concerned. These measures will then be in practice applied by all contracting authorities across Europe.

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\(^1\) The score adjustment measure is a decrease in the score obtained by an IPI targeted company. This will apply if the contracting authority will use quality criteria (e.g., social and environmental criteria) in addition to price. It will exclude companies from IPI targeted countries by making the IPI targeted offer less competitive on the final score criteria.

\(^2\) The exclusion will simply reject outright offers from companies that are based in IPI countries.
FIGURE 4
THE IPI PROCESS: MAJOR STEPS AND PROCEDURAL ELEMENTS

### Investigation

- **Pre-initiation**
  - Two possible triggers for investigation:
    - Ex-officio case
    - Complaint from EU business or MS

- **Notice of Initiation**
  - Launching formal investigation and invitation to consultations to third country concerned

- **Investigation**
  - Investigation report will indicate two options:
    - Successful consultations/termination of investigation
    - IPI measures

### Consultations

- **Parallel to investigation**
  - Start consultations with third country to remove protectionist measures

- **Possible suspension**
  - EC can terminate/suspend the investigation when the third country removes barriers or commits to take satisfactory measures within 6 months

- **IPI measures**
  - If consultations fail, EC proposes imposing IPI measures

### IPI measures

- **Imposition of IPI measures**
  - EC may impose two types of IPI measures:
    - Score adjustment measures and/or price penalty
    - Exclusion of foreign bidders

- **Expiry review**
  - EC COM may launch an expiry review process
  - If warranted, IPI measures can extended for 5 years

SOURCE: Author’s elaboration.
As IPI measures are targeting foreign bidders, there are also anti-circumvention provisions (Article 8) that require successful bidders not to subcontract more than 50% of the total value of the contract to economic operators originating in a third country which is subject to an IPI measure. Successful bidders also have a legal obligation to ensure that goods or services supplied or provided in the execution of the contract and originating in a country subject to IPI measures represent not more than 50% of the total value of the contract. All winning bidders (including from EU Member States or third countries not subject to the IPI measures) will have to comply with these obligations.

The IPI Regulation aims at following a proportionate, balanced approach that takes into account not only the size and the nature of procurement barriers abroad but also the possible administrative costs of implementing IPI measures. The crucial parameters in this equation that was subject to long and careful discussions between co-legislators are the value thresholds above which IPI measures will apply. The idea behind introducing IPI thresholds was to ensure the maximum negotiating advantage in addressing potential restrictions imposed against third countries, while reducing the number of EU procurement contracts that would be subject to potential IPI measures. Article 6(4) of the IPI Regulation stipulates that IPI measures shall only apply to public procurement procedures above a minimum threshold of 5 million euros for goods and services contracts and 15 million euros for works and concession contracts. These thresholds provided the best combination of negotiating leverage and administrative costs (Figure 5).
In sum, the IPI provides for a balanced package that maintains uniform application of IPI measures by all contracting authorities, with well-justified and limited possible exceptions for some sub-central authorities. The IPI also has certain flexibilities concerning the application of IPI measures for complex, recurrent contracts and for reasons relating to public interest. Finally, the IPI clearly stipulates that the public procurement markets that are subject to international obligations (e.g. under the WTO Government Procurement Agreement or in bilateral FTAs with different trading partners) are excluded from its scope of application. Given the overall development objectives of EU policies, the IPI Regulation does not apply to goods and services originating in least developed countries (LDCs), unless there is evidence of a circumvention of any IPI measure via least developed countries (article 4).

5. Conclusions

Public procurement is a major economic component of the global GDP. At the same time, international public procurement is one of the most difficult areas to ensure a level playing field. The vast majority of WTO members have not taken any legal commitments to ensure an open procedural environment based on transparency and non-discrimination. Even in countries that took legal commitments as part of the WTO GPA or in various FTAs, significant barriers affect a large proportion of their public procurement markets. The EU has been a longstanding proponent of open procurement markets. Promoting cross-border procurement and a level playing field is part of the European legal DNA, and underpinning the creation of the Single Market. Unfortunately, this approach is not prevalent in many other trading partners and EU companies are at a comparative disadvantage when trying to win public procurement contracts abroad. The EU public procurement market is one of the largest and most accessible in the world. However, many of the EU’s major trading partners apply restrictive practices in their markets that discriminate against EU businesses.

Faced with this asymmetry and given the difficulties to establish global rules on public procurement, the EU had no choice but to adopt the IPI, as an instrument that could be used to ensure reciprocity and a level playing field in international procurement. The IPI took a long time to come into effect but its rationale is more valid than ever. The main objective of this legal instrument is to provide the EU with negotiating leverage to remove barriers abroad and obtain a level playing field in third country procurement markets for EU businesses.

With the IPI Regulation as part of its trade toolbox, the EU is better equipped to advocate for open international public procurement markets. The objective of IPI is not to close the EU markets, but to open public procurement markets in third countries by removing restrictive measures. The IPI is complementary to the broader EU trade policy agenda. The EU will continue to engage in trade rule-making for international procurement both as part of the WTO GPA process, as well as part of its FTA negotiating agenda. However, as long as a large share of international procurement remains outside the existing international agreements and is affected by growing restrictive measures, the IPI has a profound raison d’être in the EU policy toolbox.

Bibliographic references


