THE USE AND REGULATION OF FRAMEWORK AGREEMENTS IN CHINESE PUBLIC PROCUREMENT

KE REN

(LLB, LLM)

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Abstract

Framework agreements have been widely used in Chinese public procurement for over two decades. However, the regulation is far behind the practice. There are currently neither legal rules nor uniform definition of framework agreements in Chinese laws and regulations on public procurement at the national level. Legal uncertainty and inappropriate use of framework agreements in practice, which have attracted a significant amount of public criticism, have not been thoroughly analysed by the literature.

This research aims to firstly investigate how framework agreements are used in Chinese public procurement (including the procurement by State-Owned Enterprises), secondly to analyse the problems and challenges that may undermine the beneficial use of such procurement arrangements, and, informed by the relevant international experiences, to further identify possible and practical options for China to regulate framework agreements to ensure their appropriate use.

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Acronyms and Abbreviations

TL	Tendering and Bidding Law
GPL	Government Procurement Law
IRTL	Implementing Regulation of the Tendering and Biding Law
IRGPL	Implementing Regulation of the Government Procurement Law
MOF	Ministry of Finance
NDRC	National Development and Reform Commission
CPA	Centralised purchasing agency
SOEs	State-owned Enterprises
SASAC	State-owned Assets Supervision and Administration Commission
MOFCOM	Ministry of Commerce
CGPC	Central Government Procurement Centre (the centralised purchasing agency for the central government agencies
WTO	World Trade Organization
GPA	Agreement on Government Procurement of the WTO
UNCITRAL	United Nations Commission on International Trade Law
EU	European Union
CJEU	Court of Justice of the European Union
CCS	Crown Commercial Service
US	United States of America
IDIQ	Indefinite delivery/ indefinite quantity contracts
FAR	Federal Acquisition Regulations
GAO	Government Accountability Office
FSS	Federal Supply Schedule
GSA	General Services Administration
GWAC	Governmentwide Acquisition Contract
MAS	Multiple Award Schedules
OECD	Organization for Economic Co-operation and Development

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Chapter I. Introduction

1 Background

Framework agreements are procurement arrangements that establish terms and conditions for future purchases over a given period. They are becoming increasingly popular worldwide,[1] because they represent a smarter procurement way for repeated purchases with benefits of improved administrative efficiency, greater economy of scale as well as reduced cost and expeditious delivery. On the other hand, however, framework agreements are complex to operate and maintain. The beneficial use of such arrangements requires thorough planning and preparation as well as efficient implementation and management, in the absence of which frameworks are likely to be abused or misused, exerting significant risks to transparency and competition.

In China, framework agreements have been used in public procurement for more than two decades and continue to be widely used. However, to this date, there are neither specific legal rules nor uniform definition of such arrangements in the Chinese procurement laws and regulations at the national level.

[1] G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press 2016), pp. 84-86. C. Nicholas, "A Critical Evaluation of the Revised UNCITRAL Model Law Provisions on Regulating Framework Agreements" (2012) 21 *P.P.L.R.*, p.19

The legal uncertainty and practical problems that arise due to lack of regulation have undermined the benefits of framework agreements, attracting a significant amount of public criticism. Despite the problems checked by the lack of a clear and defined legislative framework, very little research has devoted to these issues so far.

2 Research Questions

This research answers the following questions:

(1) How framework agreements are being used in Chinese public procurement (including procurement by SOEs)?

(2) What are the leading legal issues and factual problems encountered in practice that may detract from the achievement of benefits of framework agreements?

(3) What are the possible and practical options for China to regulate framework agreements effectively to ensure their appropriate use while minimising the potential abuse under the existing regulatory framework?

While the first and second questions as will be answered, an analysis of the Chinese legal framework will be provided. The third question will be answered by reference to other regimes, national and international (including the EU, the US federal procurement and the UNCITRAL Model Law) that provide certain

experiences and lessons in using framework agreements. Detailed sub-questions will supplement the third research question, including how to set up viable and acceptable legal and institutional frameworks to support the regulation of framework agreements and what essential contents the regulatory rules may cover.

3 Structure of the Thesis

The thesis is composed of eight chapters. Following this introductory chapter, Chapter II seeks to provide a survey of the main features of framework agreements, through (i) drawing on the essential elements of framework agreements; (ii) setting out different categories of framework agreements; and (iii) investigating the strengths and weaknesses of using framework agreements.

Chapter III examines how framework agreements and the similar arrangements are dealt with under three selected procurement systems: the UNCITRAL Model Law, the EU system (including the UK) and the US federal system. The purpose of this Chapter is to identify the aspects/ issues that may contribute to or undermine the achievement of benefits of framework agreements, which can provide valuable experiences for China to learn from.

The following three chapters will be devoted to the treatment of framework agreements in Chinese public procurement. Hence, Chapter IV will be an overview of Chinese public procurement regulatory regime, including legal and institutional frameworks, against which context, the current status of framework agreements in China is outlined. The purpose of this chapter is to provide background information and to usher in the further discussion and analysis.

Chapters V and VI will then examine the current use of framework agreements in Chinese government procurement and by State-Owned Enterprises under the dual-legal system in China. The research will identify and analyse the main legal issues and factual problems that may hamper the achievement of benefits of framework agreements in practice.

It is suggested that formal legal rules are needed to enable the use of framework agreements in public procurement with adequate legal basis and to ensure their appropriate use while preventing the potential misuse and abuse. Therefore, Chapter VII will propose a set of options to reform the Chinese public procurement for a more proper use of framework agreements. To that end, it starts with laying down the pillars that should underpin the regulatory framework and then sets out the main contents of the proposed regulatory rules, drawing on the international experiences.

4 Methodology

This thesis is essentially doctrinal, however, given the severe paucity of relevant data in the public domain, the author also uses limited qualitative research elements and conducted semi-structured interviews with selected participants who have been involved in framework agreements procurement in China.

Doctrinal in context

Doctrinal research is the starting point, basis and underpinning of the thesis, like for most legal research projects.[2] Instead of a purely doctrinal method, this research undertakes doctrinal analysis in context, whereby laws are understood in a broader context and political, economic, social and cultural elements that impact on legal decision-making will be factored in. The doctrinal method in context is considered inherently associated with this research, as public procurement laws and regulations are "often very much about economics and politics".[3] For instance, public procurement rules in each system are designed to achieve its particular policy objectives, based on its own administrative and cultural backgrounds. In China, there are no

[2] S. Bartie, "The Lingering Core of Legal Scholarship", (2010) 30 *Legal Studies* (3), pp.345-369

[3] It is stated that most of public procurement research has widely used a more contextual approach. See Ezra Hasson, "Book 3" of the *Legal Research in Public Procurement* (2013/2014), University of Nottingham, School of Law, p.16

unified legal formal rules about framework agreements at the national level and the current practices are transient. Therefore, taking the contextual factors into consideration can significantly assist (i) to investigate the problems and challenges that may lead to the improper use of frameworks in practice; and (ii) to propose options for regulating frameworks in a pragmatic and acceptable manner.

In the Chinese context, the sources for the analysis in the thesis will cover (i) laws and regulations adopted by the central and local governments; (ii) authoritative books and articles; (iii) official documents and other publicly available information from reliable sources, i.e. government websites. In terms of other procurement systems selected, the research focuses on the primary sources, mainly the legislation and official documents, supplemented by the academic literature including textbooks, journal articles and specialised reports.

As indicated above, this research will also investigate how framework agreements are dealt with under three selected procurement systems, namely the EU, US and UNCITRAL Model Law. The comparative element is employed in bringing in additional perspectives on this issue.[4] It is not a *stricto sensu*

[4] Framework agreements are known as "Indefinite delivery indefinite quantities" in the US federal system. They are used here as a generic term, denoting similar procurement methods or techniques in the selected procurement systems.

comparative study, which evaluates and compares the effectiveness of each legal system[5], but rather the analysis aiming at gaining a degree of insight into different regulatory approaches, with a view to identifying the good practice and high-risk areas of using framework agreements and to further informing China of possible ways forward on this issue. For an intuitive presentation, a common structure is used in exploring the use of how in each system, which mainly comprises the definition, conditions for use, operational procedures and supplier review system. The same structure also applies in investigating how framework agreements are being used in Chinese public procurement.

Choice of legal systems

Framework agreements are used and regulated in many countries. However, it would be impossible to provide an exhaustive review of all the international experiences on this issue, given the limits of time and resources. Hence, the author has carefully selected three procurement systems in order to provide valuable and useful outcomes; they include the EU procurement system (including the UK), the US federal system

[5] The comparative study has been done in other contributions. For instance, see L. Ș. Filipon, *Non-Traditional Regular Purchasing Arrangements in Public Procurement- A Doctrinal and Comparative Analysis of Regulation and Implementation Systems*, PhD Thesis, University of Nottingham, School of Law (March 2018)

and the UNCITRAL Model Law. The selection was based on the size of their procurement market, their influence on other procurement systems (mainly on China), their experiences in using and regulating framework agreements, and the accessibility to their sources on account of the author's language competence.

The UNCITRAL Model Law was included in this research because it is intended to serve as a benchmark for all States, including China, to evaluate and modernise their domestic procurement laws.[6] More importantly, as will be explained in Chapter III, it sets a high standard of transparency and competition in regulating framework agreements, which is helpful for China in striking a balance between administrative efficiency and other procurement objectives, mainly integrity. Furthermore, it provides detailed and substantial guidance through *Guide to Enactment* for legislators and policy-makers to support the effective implementation of the laws.

The EU procurement system was selected for several reasons. Apart from its immediate impact on the Member States and significant influence on other procurement systems,[7] the

[6] *Guide to Enactment of the UNCITRAL Model Law on Public Procurement* (New York, 2014), Part I, p.2. Hereinafter Guide to Enactment.

[7] The EU procurement system has an impact on China. Early in 2006, the Chinese central government sent a delegation to Germany and the UK to investigate the EU directives on public procurement and how they were implemented at the national level. See http://www.mof.gov.cn/mofhome/tfs/zhengwuxinxi/faguixinxifanying/2008

EU has relatively long experience in regulating framework agreements with express formal rules. Moreover, the EU Directives and relevant literature are accessible in English.

At the national level of Member States, this research also looks at how the UK implements the EU Directives. The UK was selected because it has a long experience of using frameworks, despite the absence of express regulatory rules before 2004. It was also one of the major contributors to the inclusion of explicit rules on framework agreements in the 2004 EU Directives.[8] Moreover, the primary literature is available in English. At the time of writing, the UK has voted to leave the EU, the fact of which, however, does not affect the research.

The US federal system is necessary to be included in the research, mainly because of its significant influence on Chinese public procurement. There has been a propensity for China to learn from the US procurement practice.[9] Furthermore, it is a system that has extensive experience in dealing with indefinite-

06/t20080603_44469.html (assessed Dec. 28, 2018). On the Chinese Government Procurement Website, the national government procurement information portal, there are many articles about EU procurement.

[8] S. Arrowsmith, "Methods for Purchasing On-going Requirements: The System of Framework Agreements and Dynamic Purchasing Systems under the EU Directives and UK Procurement Regulations", Chapter III of *Reform of the UNCITRAL Model Law on Public Procurement : Public Procurement Regulations in the 21st Century* (Eagan, MN: West, 2010) pp. 144-147

[9] For instance, there are articles that introduce and review the US federal procurement system on the Ministry of Finance's official website, see "The US Federal Acquisition System", May 20, 2013, Chinese text available at http://www.ccgp.gov.cn/wtogpa/zhidu/201310/t20131029_3588886.htm (accessed Sep 26, 2018).

delivery/ indefinite quantity (IDIQ contracts, the equivalent of framework agreements in the US) and can provide rich material on this issue. The constant fine-tuning of the objectives in regulating IDIQ contracts is particularly worth learning.

Qualitative research factor- Interviews

Given the paucity of data regarding framework agreements in China in the public domain,[10] particularly in the procurement of Chinese SOEs, the author conducted semi-structured interviews with 35 participants in China who have involved in or affected by framework agreements in order to explore their perspectives and experiences on framework agreements in China.

The research adopted the convenience sampling method, by which the author identified and selected from population who were available and willing to participate, thanks to personal contacts and sources. This method was chosen on account of two limitations. Firstly, given the time, expertise and resources available, especially in light of China's wide geographical spread and unbalanced quality in implementing procurements between different regions, it would have been impossible for the author

[10] Albano and Nicholas observe that the lack of data on framework agreements is a common issue in many jurisdictions. See Albano and Nicholas, fn. 1 *supra*, at p.124.

to carry out a large-scale empirical project within a PhD thesis.[11] More importantly, a majority of government officials and employees of SOEs that have involved in procurement seem to be reluctant to talk about the research topics since certain data may be considered sensitive.

The interviews involve 35 participants in total, with 29 of them in Chinese government procurement and the other 6 from Chinese SOEs. The former class of participants involve both government officials and practitioners that accepted to respond, which specifically comprise 1 policymaker, 6 officials of procuring entities, 4 officials from centralised purchasing agencies, 3 representatives of suppliers, 6 officials from finance departments, 3 employees from electronic service providers that established online platforms for framework agreements, 2 procurement lawyers and 4 academia. The table below provides the information regarding the participants involved in the interviews in Chinese government procurement:

Table 1.1 Information of Participants Involved in the Interviews in Chinese Government Procurement

Categories of the participants	Levels of governments	Number of the participants relevant	Total number
Policymaker		1	1

[11] It is submitted that large-scale empirical projects are often carried out by teams of researchers from different disciplines, and are rarely seen in PhD research, especially in social-legal studies. D. Watkins and M. Burton (eds.), *Research Methods in Law* (2nd edn., Routledge, 2018), pp.73-74

Centralised Purchasing Agencies	At the central level	Central Government Procurement Centre	1	4
	At the local level	Hubei Province	1	
		A city within Shanxi Province	1	
		Guangdong Province	1	
Procuring entities	At the local level	Hubei Province	6	6
Suppliers			3	3
Supervision authorities	At local level	Hubei Province	3 (with 1 at provincial level and 2 at municipal level)	6
		Jiangsu Province	1	
		Zhejiang Province	1	
		Sichuan Province	1	
Electronic Framework Agreements Service Providers			3	3
Government Procurement Lawyers			2	2
Other Legal Practitioners and Advisors			4	4
In total	29			

Regarding SOEs, given the access difficulty, the researcher only had the chance to reach 6 participants who were

convenient in the proximity. They were procurement personnel from 5 affiliate companies of 4 large central SOEs in Hubei Province.

This study combined three ways to collect data: personal interview, telephone interview and email responses. The personal interview was the primary method, and the other two were deployed as complementary when face-to-face communication was not available, either due to the participants' unwillingness or given the limit of resources.

All the interviews were conducted between January and March 2016. Each personal interview lasted roughly between 25-40 minutes, and the telephone interviews ran for 10-20 minutes. Regarding the email response, while the author prepared and forwarded a series of questions, there was no participant answered all but a few selectively. The author affirms that the interviews were conducted ethically.

It is reiterated that the author has endeavoured to approach more participants to obtain reasonable outcomes. However, reaching a broader sample of officials has proved impossible. Hence, the interviews and the qualitative samples collected are not meant to be reflective of the general practice of how frameworks are implemented in China. Despite the limits, nevertheless, the interviews are valuable in uncovering the problems that need to be addressed in the use of framework

agreements in China and contributing to the final proposals to reform Chinese legislative framework. The interviews are expected to fill the relevant literature gap with empirical evidence as well.

Chapter II. Description and Characterisation of Framework Agreements

1 Introduction

Framework agreements are an "umbrella" term for a broad category of procurement arrangements; they are known as various names in different procurement systems, including "indefinite-delivery/ indefinite quantity (IDIQ)" or "task order contracts" in the US, "supply arrangements" in Canada, "panel arrangements" in Australia, "running and rate contracts" in Africa and India, "periodic purchase arrangements", "periodic supply vehicles", "recurrent purchase arrangements", and "umbrella contracts" in the literature.[1]

Framework agreements are widely used with phenomenal popularity worldwide mainly because they, representing a smart and streamlined procurement way, can facilitate repetitive purchases due to demand aggregation and up-front completion

[1] United Nations Commission on International Trade Law, "Possible Revisions to the UNCITRAL Model Law on Procurement of Goods, Construction and Services- the Use of Framework Agreements in Public Procurement" (24-28 April 2006), UN Doc A/CN.9/WG.I/WP.44, available at http://www.uncitral.org/uncitral/en/commission/working_groups/1Procurement.html (accessed Aug 25, 2018). The term "framework agreements" is used in the EU and UNCITRAL Model Law. Notably, Albano and Nicholas consider the Canadian supply arrangements are closer to supplier lists than framework agreements. See G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press, 2016), p. 14

of various procurement steps.[2] According to an OECD survey, 97% of the OECD countries routinely use framework agreements at the central government level.[3] In the US, the value of procurement through multiple award schedules contracts (a variant of IDIQ contracts) rose dramatically from $4 billion in 1992 to $32.5 billion in 2004.[4] During the fiscal years 2011-2015, more than $130 billion annually was spent on IDIQ contracts, accounting for around one-third of the total government contract value.[5] In the EU, more than 215,000 framework agreements were awarded in 2011, making up 25% of the overall value of the above-EU thresholds procurement contracts awarded.[6]

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[2] Chartered Institute of Procurement and Supply (CIPS), "Framework Arrangements" (2012), available at https://www.cips.org/Documents/Resources/Knowledge%20Summary/Framework%20Arrangements.pdf (accessed Aug 12, 2018).; *Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on Public Procurement* [2014] OJ L94/65 (2014 Public Sector Directive), recital 60

[3] OECD, "Governance at a Glance 2013: Procurement Data", 11-12 Feb. 2013 (Paris, OECD Conference Centre)

[4] United States. Government Accountability Office (GAO), "Contract Management: Opportunities to Improve Pricing of GSA Multiple Award Schedules Contracts", GAO-05-229, 10 (Feb. 2005), available at http://www.gao.gov/assets/250/245293.html (accessed Sep 14, 2018).; D. Gordon and J. Kang, "Task-order Contracting in the U.S. Federal System: The Current System and Its Historical Context", Ch.5 in S. Arrowsmith (ed.), *Reform of the UNCITRAL Model Law on Public Procurement : Public Procurement Regulations in the 21st Century* (Eagan, MN: West, 2010) p.251.

[5] GAO, "Federal Contracts: Agencies Widely Used Indefinite Contracts to Provide Flexibility to Meet Mission Needs", GAO-17-329, (April 2017), available at http://www.gao.gov/products/GAO-17-329 (accessed Sep 18, 2018).

[6] European Commission, "Annual Public Procurement Implementation Review 2012", (Brussels, 2012) SWD (2012) 342, 26, available at https://ec.europa.eu/taxation_customs/sites/taxation/files/docs/body/swd(2012)16_en.pdf; PwC, London Economics and Ecorys, "Public procurement

This chapter seeks to provide a comprehensive survey of framework agreements through (i) analysing the main legal and economic features of frameworks; (ii) exploring different types of frameworks agreements; and (iii) explaining their strengths and weaknesses. The term "framework agreements" will be used throughout the research for simplicity, as it is the most common English term to denote the arrangements.

2 Description and Essential Elements of Framework Agreements

Drawn on international practices, three broad definitions (or descriptions) of framework agreements can be identified. Firstly, the *UNCITRAL Model Law on Public Procurement*[7] distinguishes a "framework agreement procedure" from a "framework agreement". A framework agreement procedure is "…conducted in two stages: a first stage to select a supplier (or suppliers) or a contractor (or contractors) to be a party (or parties) to a

in Europe: Cost and effectiveness", (March 2011), available at https://publications.europa.eu/en/publication-detail/-/publication/eb5f2d5a-a034-4123-83af-2ea7eb363825/language-en; PwC, ICF GHK and Ecorys, "SME's Access to Public Procurement Markets and Aggregation of Demand in the EU", (DG Internal Market and Services, 2014), available at http://ec.europa.eu/internal_market/publicprocurement/docs/modernising_rules/smes-access-and-aggregation-of-demand_en.pdf (accessed Aug 5, 2018).

[7] *UNCITRAL Model Law on Public Procurement* (2011), Official Records of the General Assembly, UN Doc A/67/17. Hereinafter referred to as the *Model Law.*

framework agreement with a procuring entity, and a second stage to award a procurement contract under the framework agreement to a supplier or contractor party to the framework agreement"[8].

A framework agreement *per se* is referred to as "an agreement between the procuring entity and the selected supplier (or suppliers) or contractor (or contractors) concluded upon the completion of the first stage of the framework agreement procedure". [9] The purpose of a framework agreement is to set out "the terms upon which purchases will be made (or [establish] the main terms and a mechanism to be used to establish the remaining terms or refine the initially established terms)".[10]

The separate definitions indicate that a framework agreement is the result of the first-stage procedure and a procurement contract will not be awarded until the second-stage. Both stages of a framework agreement procedure (concluding a framework agreement and ordering against it) are subject to full procedural safeguards and supplier review.

The EU Directives defines a framework agreement as "an agreement between one or more contracting authorities and

[8] The *Model Law*, Art. 2(e)
[9] *Ibid.* Art 2(e)(i)
[10] *Guide to Enactment of the UNICITRAL Model Law on Public Procurement* (2012) (hereinafter the Guide to Enactment), p.253, available at http://www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/2012Guide.html (accessed Sep 26, 2018).

one or more economic operators, the purpose of which is to establish the terms governing contracts to be awarded during a given period, in particular with regard to price and, where appropriate, the quantity envisaged".[11] Similar to that under the *Model Law*, the definition also draws a clear distinction between a framework agreement itself and a procurement contract awarded against the agreement. In addition, the EU Directives introduce another procurement tool- Dynamic Purchasing System, a variant of framework agreements, which will be considered later.

In the US, the equivalent of framework agreements is "indefinite-Delivery/ indefinite-Quantity contracts" (IDIQ) or task and delivery order contracts. According to the *Federal Acquisition Regulation,* a "delivery-order contract" means "a contract for supplies that does not procure or specify a firm quantity supplies (other than a minimum or maximum quantity) and that provides for the issuance of orders for the delivery supplies during the period of contract." "Task-order contract" has an identical definition but for services.[12] In terms of

[11] Art 33(1) of the *Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on Public Procurement and Repealing Directive 2004/18/EC* (2014 Public Sector Directive), OJ L 94; Art 51(1) of the *Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on Procurement by Entities Operating in the Water, Energy, Transport and Postal Services Sectors and Repealing Directive 2004/17/EC* [2014] (2014 Utilities Directive) OJ L94/243

[12] *Federal Acquisition Regulation* (FAR), Subpart 16.501, available at https://www.acquisition.gov/browsefar (accessed Aug 26, 2018). For more information about task order/ IDIQ contracts, see Chapter III section 4.

wording, task order contracts are explicitly defined as procurement contracts *per se* in the US, in contrast to the approach taken by the EU and the *Model Law*.

The above definitions (descriptions) reflect different approaches to regulating framework agreements in different procurement systems, grounded on the underlying legal and institutional frameworks. On the other hand, several consistent elements/ traits can be identified amongst the various descriptions. These elements are considered as the essence to characterise framework agreements.[13]

The first element concerns the principals that are involved. In a framework agreement, both parties, the procuring entity and supplier, can be single and/or multiple.[14] This is different from many other "traditional" procurement methods that involve a single supplier and a procuring entity in an individual

[13] Given the wide variation in the use of framework agreements in practice, the essential elements of framework agreements may be different from one another from different perspectives. For instance, Albano and Nicolas consider the operational steps as necessary elements of a framework agreement procedure, from the procedural perspective. See G. L. Albano and C. Nicholas, fn. 1 *supra*, at p.13

[14] The *Model Law,* Art 2(3); the *2014 Public Sector Directive*, Art 33(1); and *FAR* 16.503, 504. The terms used to refer to purchasers and sellers in public procurement vary in different legal systems. "Procuring entity" is the term used in the *Model Law*, the counterparts of which in the EU and US are "contracting authority" and "government agency" respectively. While both the *Model Law* and the US adopt the notion of "supplier", the EU Directives use "economic operator". For simplicity, the terms "procuring entity" and "suppliers" are used in the text to refer to bodies governed by public law engaging and persons interested in procurement respectively.

purchase.[15] Moreover, apart from the "traditional" parties (the supplier and procuring entity), a third party-centralised purchasing agencies/bodies-may involve in framework agreements when used for centralised procurement, which is all-too-common in practice. Centralised purchasing agencies, i.e. the General Services Administration (GSA) in the US and *Consip* company in Italy, are in charge of establishing and managing framework agreements against which the procuring entities can place subsequent orders.[16] Thus, the roles of "operator" and "user" are separated in the centralised context.[17]

Secondly, a two-stage procurement process is considered a necessary trait of framework agreements.[18] There are two

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[15] In a procurement project based on open tendering, where several suppliers form a consortium to participate and where more than one procuring entity decides to procure collectively, they are regarded as a "supplier" and "procuring entity" in the procurement.

[16] More information about GSA and Consip is available at https://www.gsa.gov/portal/category/100000 and http://www.consip.it/en/about_us/ (accessed June 26, 2018).

[17] In fact, the clear separation of the roles between users and operator in framework agreements is a legal issue in many jurisdictions, including in China, as discussed in Chapter V. It needs to be noted that the specific roles and responsibilities of centralised purchasing agencies are different in different legal systems. According to an OECD survey, the main activities of these agencies across the OECD countries include carrying out aggregation and procurement for user entities, and/or administrating the system awarding framework agreements and other consolidated instruments from which the user entities can order, and/or coordinate training for the procurement officials, and/or making procurement policies for implementation. See OECD , *Government at a Glance 2015*, (2015) OECD Publishing, Paris, available at http://dx.doi.org/10.1787/gov_glance-2015-en(accessed July 26, 2018).

[18] Albano also identifies a two-stage procurement process as a common trait of different "families" of framework agreements. See G. L. Albano, "Demand Aggregation and Collusion Prevention in Public Procurement", Part III Chapter 1 in G. M. Racca and C. R. Yukins (eds.), *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (Bruylant, 2014), p. 166

stages of operations in each framework agreement: the first stage to conclude a master agreement that sets out the main terms and conditions for future purchases; and the second stage to place subsequent orders when requirements arise. The procurement process is initiated before an actual need being fully specifiable. Thus, there often exists an interval between concluding a framework agreement itself and placing orders.

Indeed, there are other procurement arrangements or tools, such as supplier lists which also involve two-stage operations. A supplier list means a system under which suppliers that are assessed qualified will be registered as potential suppliers for future purchases.[19] On the one hand, framework agreements and supplier lists are both designed to identify potential suppliers to meet future requirements and are closely related, being described as "shades on a spectrum of on-going purchasing arrangements".[20]

On the other hand, framework agreements are different from supplier lists. A framework agreement specifies the scope of future awards at the outset, thus describing the subject mattered to be needed and setting out the terms and conditions for future orders. Accordingly, the first stage in a framework

[19] For analysis of supplier lists, see S. Arrowsmith, "Framework Purchasing and Qualification Lists under the European Procurement Directive" (1999) 8 *P.P.L.R*. p.115
[20] *Ibid.* p.116

agreement involves, first, identifying the suppliers that are interested in and qualified for future purchases, and second, evaluating the submitted tenders responding to the specified needs, albeit to a different extent.

On the contrary, a supplier list concerns a generic type of procurements only. The outcome of the first stage is not to establish terms governing future purchases, but to identify the suppliers who have interest in and may be eligible for all or some broad types of purchases.[21] Qualification systems in the EU utilities sector fall in the category of arrangements.[22] Framework agreements, in most cases if not all, move a step further than supplier lists towards awarding a procurement contract. However, there is no absolute distinction between frameworks and supplier lists due to possible variations. For instance, it is possible that a framework agreement with overly broad specification and very a few terms established may actually function as a supplier list.

Given the above, specifying the scope of future needs and setting out terms and conditions, partly but not all, for future procurement is a third essential trait of framework agreements.

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[21] UNCITRAL, "Possible Revisions to the UNCITRAL Model Law on Procurement of Goods, Construction and Services- Issues Arising from the Use of Supplier Lists" (24-28 April 2006), UN Doc A/CN.9/WG. I/WP.45. See also S. Arrowsmith, fn. 19, *supra*, at p.116; See Albano and Nicholas, fn. 1, *supra*, pp. 13-14

[22] Qualification systems are only allowed in the utilities sector in the EU. See Ch.3 section 3 below.

A framework agreement when concluding can be incomplete, with certain aspects to be finalised later on, such as quantity and delivery schedules.

Fourthly, framework agreements are mainly used to meet frequent and recurrent needs over a period. The rationale of framework agreements is to enhance administrative efficiency by aggregating what otherwise would be a series of small purchases into a single procurement process. [23] Thus, frameworks are particularly suitable for purchasing relatively standard goods and services that are commonly needed, such as office supplies and maintenance service. On the other hand, the established practice also suggests that framework agreements can provide an effective solution to emergency procurement for enabling swift and expedient purchases and deliveries of certain types of items that can be reasonably expected, for instance, medicines and tents in disasters.[24]

Taking into consideration the above, "framework agreements" in this research are defined as a two-stage

[23] "Efficiency" in the procurement context is not an economic term and refers to the "relationship between the transaction costs and administrative time of each procurement procedure and its value are proportionate" See the *Guide to Enactment*, para 3 p.26. It is identified by Albano that the aggregation of demands to be supplied from time to time is a common trait in framework agreements shared in the EU and US systems and under the Model Law. See G. L. Albano, A. Ballarin and M. Sparro, "Framework Agreements and Repeated Purchases: The Basic Economics and A Case Study on the Acquisition of IT Services", *International Public Procurement Conference* (Seoul, 2010), pp.13-14

[24] W. S. Curry, *Government Contracting – Promises and Perils* (2nd edn., Routledge, 2016), pp.209-235

arrangement where one or more than one suppliers, at the first stage, are selected to enter into a framework/master agreement with procuring entity/entities, which sets out the terms and conditions for future purchases, before an actual requirement arises, enabling subsequent issuance of orders as per the pre-established method and terms over a specified period (the second stage or call-off stage).

3 A Taxonomy of Framework Agreements

Framework agreements can be divided into various categories based on different variables. The common variables include the number of the parties involved, whether or not the second-stage competition is involved, the degree of openness to new suppliers, and whether the agreements are of binding nature. It needs to be noted that the different categorisations are not necessarily mutually exclusive but interact with each other. The taxonomy draws on the enlightening classifications that have been already developed by Arrowsmith, Nicholas and Albano.[25]

[25] S. Arrowsmith and C. Nicholas, "Regulating Framework Agreements Under the UNCITRAL Model Law on procurement", Ch. 2 in S. Arrowsmith (ed.), *Reform of the UNCITRAL Model Law on Procurement: Procurement Regulation for the 21st Century* (Eagan, MN: West, 2010), pp. 102-116; See Albano and Nicholas, fn. 1, *supra.* pp. 12-22

3.1 Single-supplier or Multi-Supplier Framework Agreements; Single-user or Multi-user Framework Agreements

A procuring entity may conclude a framework agreement for its own use (single-user framework agreement) or letting use by multiple procuring entities (multi-user framework agreement). Multi-user frameworks may particularly manifest in centralised purchasing. A centralised purchasing agency may initiate a multi-user framework agreement on behalf of a number of procuring entities. A single-user framework agreement is an arrangement established by a procuring entity to fulfil its own repetitive requirements over a period.

In practice, centralised framework agreements (multi-user frameworks) seem to be the most popular form in many systems. It is preferred arguably because centralised purchases can help leverage the purchasing power, facilitate economies of scale due to demand aggregation and thus lead to cheap prices and cost-savings. Moreover, procuring entities are expected to take advantage of procurement expertise of centralised purchasing bodies. On the other hand, however, there is always a risk of conflict of interest, whereby centralised purchasing bodies may overuse or misuse frameworks for their own

interest.[26] Moreover, excessive demand aggregation may have an adverse impact on competition and distort the relevant market. Centralised frameworks may also facilitate collusion and corruption through providing frequent chances of interacting between suppliers and/or between suppliers and procuring entities.[27]

Similarly, a framework agreement may involve one (single-supplier framework) or more than one supplier (multi-supplier framework). Ordering process under single-supplier frameworks is rather straightforward. In a multi-supplier framework, the procuring entity should select from the suppliers admitted for a specific call-off.

A procuring entity may enter into a single-supplier framework agreement with the expectation of obtaining favourable terms or an advantageous price "in return for the exclusivity" or building a long-term relationship with the supplier.[28] However, a single-supplier framework may pose risks to security of supply, for instance, where there is an urgent demand of large volume.[29] Single-supplier frameworks may

[26] For instance, where centralised purchasing bodies charge a fee for each use of framework agreements, there a risk that they may encourage over-using frameworks for their gains. Conflict of interests has been discussed in Arrowsmith and Nicholas, fn. 25 *supra*, p. 116

[27] Albano and Nicholas provide that repeated frameworks and demand fragmentation of call-offs are pro-collusive traits of public procurement market. See Albano and Nicholas, fn. 1, *supra.* pp. 186-190

[28] See S. Arrowsmith, fn. 19, *supra.* p.119

[29] *Ibid.*

facilitate nurturing a very few suppliers and increasing their market share, thus having adverse impact on the general market, beyond the procurement at hand, being anti-competitive, especially in China where the government and SOEs are the major purchaser.

In practice, multi-supplier framework agreements tend to be more preferred for many reasons. First, the availability of multiple suppliers allows more freedom to choose for the purchaser(s) to satisfy diverse supply requirements, especially where the framework is used by more than one procuring entity whose needs may be heterogeneous. Moreover, multi-supplier frameworks are envisaged to provide on-going competition amongst the supplier parties throughout the procurement process. The other benefits of multi-supplier frameworks include better security of supply and encouraged participation of SMEs.[30] For the above, multi-supplier frameworks tend to be the norm of the arrangements in many procurement systems, including China. In the US federal system, the *Federal Acquisition Regulation* (FAR) established a statutory preference

[30] S. Arrowsmith, *The Law of Public and Utilities Procurement: Regulation in the EU and UK Volume 1* (3rd edn, Sweet & Maxwell 2014), p.1109; M. M. Linthorst and J. Telgen, "Public Purchasing Future: Buying from Multiple Suppliers", Ch. 21 in G. Piga and K.V. Thai (eds), *Advancing Public Procurement: Practices, Innovation and Knowledge-sharing* (PrAcademics Press, 2007), p.473.

for multiple award contracts (equivalent to multi-supplier framework agreements).[31]

On the other hand, however, concerns and problem also emerge in the use of multi-supplier frameworks. For instance, the call-off stage may be administratively complex and time-consuming, specially where the second-stage competition is reopened. The involvement of multiple suppliers poses additional challenges to the management and monitoring of the procurement process. There is a further risk of collusion amongst the supplier parties, which problem may exacerbate where there is a lack of transparency at the second stage. On account of the above, the decision regarding the type of framework agreements to be selected in a procurement project should be made on a case-by-case basis, depending on the nature of demands, the anticipation of the market, as part of procurement planning.[32]

[31] *FAR*, 16.504(c). See Chapter III section 4 below.
[32] L. Ș. Filipon, *Non-Traditional Regular Purchasing Arrangements in Public Procurement- A Doctrinal and Comparative Analysis of Regulation and Implementation Systems*, PhD Thesis, University of Nottingham, School of Law (March 2018), 300-317

3.2 Framework Agreements Binding or Non-binding on the Parties

Based on whether the parties are committed to buying and/or to supplying under the agreement, there are four possible permutations of framework agreements: (i) binding on both the purchaser(s) and the supplier(s); (ii) binding on the purchaser(s) but not on the supplier(s)[33]; (iii) binding on the supplier(s) only but not on the purchaser(s); and (vi) non-binding on either the purchaser(s) or the supplier(s). A framework agreement of each permutation can be multi-supplier and/or multi-user.

The content and extent of commitment in a binding framework agreement are situation-based. A framework may obligate the purchaser(s) to buy all or part (either a minimum or fixed quantities) of the future purchases. The supplier(s) may undertake to supply all or part of the requirements up to a defined maximum. Determining the proper commitment is critical to the overall efficacy of a framework agreement, because it impacts the "level of uncertainty" between parties.

In general, a commitment on the supply-side can better achieve security of supply and prevent "cherry-picking", whereby the supplier(s) may selectively respond to those orders

[33] This type of framework agreements rarely takes place in practice. S. Arrowsmith, fn. 30, *supra*, p.1108

they consider profitable, i.e. large orders, and refuse those with expected low returns.[34] However, the effect of commitment to supply is positively correlated to the extent of the reliable anticipation of future purchases, in the absence of which suppliers are less willing to participate, *a fortiori* offering competitive terms.[35]

A commitment on the demand-side, for instance making the use of framework agreements mandatory, can provide the supplier(s) with reasonable expectation of the future orders, who are more willing to offer favourable terms and lower prices, especially in centralised frameworks due to demand aggregation. According to the international experience, a number of countries run centralised framework agreements at the central government level and many of them, such as the UK and Italy, make the use of such centralised frameworks mandatory for the relevant procuring entities.[36] In the US, the General Schedule Administration Schedules (GSA Schedules, the largest

[34] *Ibid.*, p.1108
[35] See Albano and Nicholas, fn. 1, *supra*, at p.291
[36] In Italy and the UK, Consip and Crown Commercial Service (CCS)-the respective centralised procurement bodies at the central government level-operate framework agreements at the central level, the use of which is mandatory. For detailed analysis on the impact of commitment in centralised framework agreements, See Albano and Nicholas, fn. 1 *supra*, pp.287-292. As explained in Ch. V, in China, framework agreements are generally binding on both parties.

centralised IDIQ contracts) were compulsory for federal agencies until 1990.[37]

On the other hand, the decision to make the purchaser(s) be bound by a framework, in turn, depends on the offers that suppliers submit, forming a "chicken-and-egg" question.[38] Given the "puzzle", in practice procuring entities often opt to guarantee a minimum quantity or a retainer to attract suppliers,[39] as is the case of IDIQ contracts in the US.

It is possible that the purchaser(s) and supplier(s) set up the terms for future purchases, whereas neither party undertakes any obligation. In such case, procuring entities are allowed to buy outside where there are more competitive offers. When ordering under the frameworks, they can also benefit from administrative efficiency and convenience. On the other hand, frameworks non-binding on the supply-side may entail the risk to the security of supply. Concerns further exist that suppliers may be unwilling to participate or may submit less favourable offers because there are no future orders guaranteed.

According to Albano and Nicholas, the effectiveness of such non-binding frameworks is hinged on the level of planning and

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[37] D. I. Gordon and G.M. Racca, "Integrity challenges in the EU and U.S. procurement systems", Ch.1 in G. M. Racca and C. R. Yukins (eds.), *Integrity and Efficiency in Sustainable Public Contracts – Balancing Corruption Concerns in Public Procurement Internationally* (Bruylant, 2014) 137

[38] See Albano and Nicholas, fn. 1, *supra*, at p.291

[39] A. Hagiu and J. Wright, "Multi-Sided Platforms", Harvard Business School Working Paper, No. 15-037, Nov. 2014 (Revised March 2015)

design. "Where the framework agreement offers good terms and value for money", or where its procedural advantages may overweigh the benefits of other methods, it may generate benefits that are "an equivalent to strong commitment".[40]

3.3 Framework Agreements Involving and Not Involving a Second-stage Competition

Depending on whether a further round of competition is involved to place an order, framework agreements can be classified into those with the second-stage competition and those involving direct awards. Frameworks with a second-stage competition must involve multiple suppliers.

Where no second-stage competition is involved, substantive terms and conditions for future purchases should be established in the framework agreement itself to enable direct awards. Substantial competition takes place at the first stage, where the suppliers' qualifications and their tenders will be subject to full evaluation.[41] Framework agreements without the second-stage competition are all "closed", because the first-stage involves substantive comparisons of offers. They are often used for

[40] See Albano and Nicholas, fn. 1, *supra*, at p. 287
[41] This can be demonstrated by framework agreements without second stage competition under the *Model Law*, Art.2(3) and that under the *2014 Public Sector Directive*, art.33(4)(a).

simple purchases, such as office supplies, the nature of which can be specified in advance and are less likely to change rapidly.[42]

A framework agreement without a second-stage competition can be awarded single or multiple suppliers. When multiple suppliers are awarded, the method of choosing a supplier to perform an order at the call-off stage should be clarified beforehand for transparency and fair competition. In practice, many methods are being used to allocate orders under frameworks with direct awards, including "cascading" and "rotation" in different systems. However, as Albano and Nicholas have analysed, many of these systems often fail to achieve fair and best value procurement outcomes.[43]

Framework agreements with the second-stage competition often take place when it is not possible or appropriate to establish all the terms at the first stage, and a further round of competition is reopened to determine the best offer until a specific requirement arises. For instance, in a procurement project for legal consultancy services, the requirement cannot be determined until it actually arises, and therefore the effective competition will emerge at the second stage.

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[42] See Arrowsmith and Nicholas, fn. 25 *supra*, p.110

[43] For more analysis about the direct awards methods, such as "cascading", rotation, random allocation and queuing, see Albano and Nicholas, fn. 1, *supra*, pp. 60-69.

Notably, where the full terms are already established in a concluded framework agreement, it is also possible to reopen competition to allow the supplier parties to supplement or update their original orders. The EU Directives explicitly authorise such possibility.[44] By a mini-competition, procuring entities may wish to obtain more favourable offers that reflect the specific requirements (i.e. in large volume orders) and the current market (i.e. in cases of volatile prices).

The extent and scope of the second-stage competition, reflecting the dynamics between competition at two stages, may vary, depending on the specific circumstances. At one end, the first-stage competition can be substantial, involving a full evaluation of tenders. The second-stage competition, thus, merely focuses on limited "outstanding variables", such as quantity.[45] At the other end, the competition at the first stage may be "weak", as a result of which a large number of suppliers may be admitted and the second-stage competition for each call-off can be complex and onerous.

As highlighted by Albano and Nicholas, "the greater the extent of second-stage competition, the more administratively complex and lengthy the second-stage competition will be".[46]

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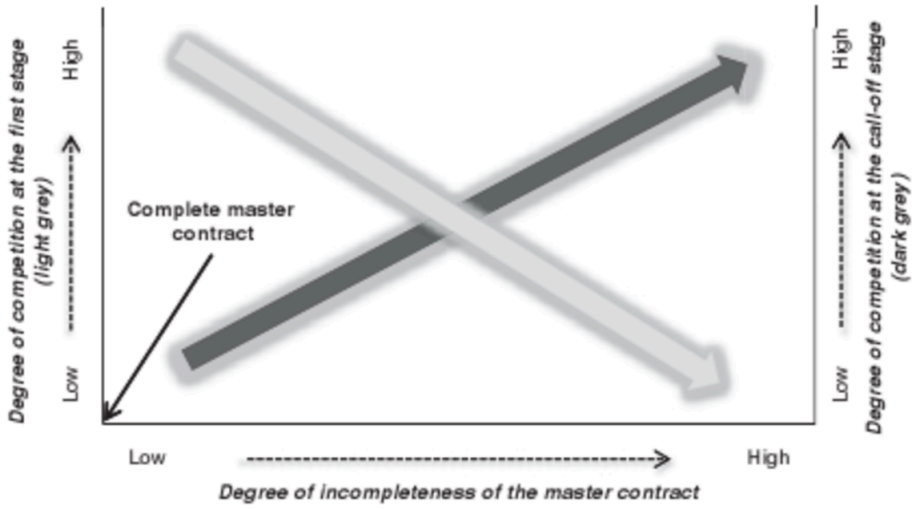
[44] *Directive 2014/24/EU of the European Parliament and of the Council on public procurement and repealing Directive 2004/18/EC* [2014] OJ L94/65 (*The EU 2014 Public Sector Directive*) art. 33(4)(b)
[45] See Albano and Nicholas, fn. 1, *supra*, at p.18; Arrowsmith and Nicholas, fn. 25, *supra*, p.108
[46] See Albano and Nicholas, fn. 1, *supra*, at p. 320

Nonetheless, in any case, the ordering stage should be a "simple, rapid and efficient process", because an excessively onerous ordering process will jeopardise the overall efficiency- the core of framework agreements.[47]

It is an important but complex task to determine the appropriate extent of the second-stage competition and to properly balance the competition between two stages, with a view to achieving the best value in call-offs while ensuring the efficiency of the overall procurement process. The decision on this issue should be part of procurement planning and design, requiring relevant experience and skills, and, more importantly, the in-depth market and demand analysis. Albano and Nicholas have intuitively demonstrated the dynamics of competition between two stages of framework agreement relative to the degree of incompleteness of the master agreement through a figure, which was reproduced below in Figure 2.1 for clarity.

[47] *Ibid*. p. 215

Figure 2.1 Balancing Competition Between Two Stages of a Framework Agreement



Source: G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement*

3.4 Open and Closed Framework Agreements

Framework agreements can be closed or open, depending on whether new suppliers can join the framework agreement after its conclusion. [48] Closed frameworks-the "archetype" frameworks-can be single-supplier or multi-supplier. The establishment of a closed framework actually carves out a mini-procurement market, which is walled off within the duration. In order to establish competitive terms, the first stage of closed frameworks usually involves a reduction on the number of admitted suppliers, thus involving substantive competition.

Closed frameworks may be at ease in terms of management and supervision, due to the involvement of a limited number of

[48] Such classification is expressly provided under the *Model Law*. See Chapter III below.

supplier parties. More favourable terms may also be anticipated as a result of a fierce first-stage competition. On the other hand, however, they may be anti-competitive and pro-collusive, as they arguably restrict entrance to the procurement market.[49] The smaller the number of suppliers admitted to a framework agreement, the easier for them to "share the pie" and the higher the level of risk of collusion there may be at the call-off stage. Although a closed framework is established in an open and competitive environment, as Yukins argued, the second-stage tends to be "below the radar".[50] As explained in Chapter III, lack of transparency and competition is a common problem in using framework agreements in the EU and US federal systems.

Open framework agreements can only be multi-supplier and usually involve the second-stage competition. Dynamic purchasing systems in the EU and the GSA Schedules in the US can fall in this category. They are operated on a fully electronic basis to fulfil the open-ended solicitation and admission at the first stage. Notably, the "openness" is limited to the entrance of frameworks, but not the call-offs. At the second stage, however, call-offs will be only awarded to those that are parties to the framework and new suppliers are not able to directly receive

[49] For instance, see P. Trepte, *Public Procurement in the EU – A Practitioner's Guide* (2nd edn., OUP, 2007) p.212; Albano, Ballarin and Sparro, fn. 23 *supra*, p.5

[50] C. R. Yukins, "Are IDIQs Inefficient? Sharing Lessons with the European Framework Contracting" (2008) 37 *P.C.L.J.* p.547

orders. In other words, in all framework agreements, only the supplier parties will be considered for the call-offs under the agreements. The key difference of open frameworks from the closed ones is that new suppliers can subsequently become the parties and be eligible for the awards thereafter. There is no clear-cut division between two stages in open frameworks.

As new suppliers may join at any time, the first stage of open frameworks usually focuses on assessing qualification and, in some cases, responsiveness of suppliers to the requirements. Given that, open frameworks may be closer to supplier lists. In practice, the subject matter in some framework agreements are described in such a broad and generic manner, leaving substantial terms to be added later on. Such a broad framework may actually function no more than a supplier list.[51]

Open framework agreements presuppose that the relevant market is competitive, with a large number of suppliers available to fulfil the requirements to ensure sufficient and on-going interest and wide participation. They are appropriate to purchase off-the-shelf items that are generally available on the market, i.e. stationary.[52] Because new suppliers can apply to enter at any time, it is not possible and unnecessary to carry

[51] See Albano and Nicholas, fn. 1, *supra*, pp. 320-322
[52] This can be exemplified by the condition for the use of dynamic purchasing system in the EU. See art. 34(1) of the *2014 Public Sector Directive.*

out head-to-head competition or to fully evaluate tenders to reduce the number of admitted suppliers at the first stage.

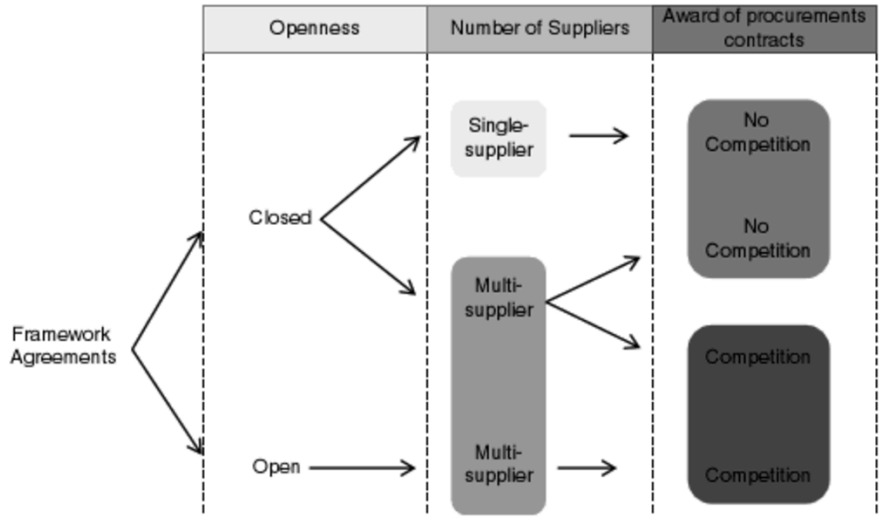
The open nature welcomes wide participation, mitigating the barriers to market entrance. Therefore, there is always a large number of supplier parties competing for the call-offs, and the "pool" of the supplier parties is dynamic. As Albano and Nicholas stated, collusion is less likely in open frameworks than closed frameworks.[53] Moreover, greater transparency is enabled as open frameworks are an entirely electronic/automatic process.

In practice, it is impossible to draw a clear delimitation among different types of framework agreements. The complex and ever-changing practices often lead to the combination of different types of frameworks, catering to different circumstances. Based on the international practice, three combinations are most commonly seen and used: (i) closed framework agreements without second-stage competition; (ii) closed framework agreements with second stage competition and (iii) open framework agreements.[54] The *Model Law* adopts this classification in regulating framework agreements, as explained soon in Chapter III.

[53] Albano and Nicholas, fn. 1, *supra*, pp. 193-194. According to them, "…the higher number of awardees, the more difficult the coordination among them to split procurement contracts…"
[54] *Ibid.,* pp.16-20

Albano and Nicholas have provided a figure that intuitively demonstrate different models of framework agreements and their interaction. The figure was extracted and reproduced here for clarity.

Figure 2.2 Models of Framework Agreements



Source: G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement*

4 Strengths and Weaknesses of Framework Agreements

The core motivation of using framework agreements is to improve administrative efficiency.[55] Framework agreements can allow for aggregation of what otherwise would be a series

[55] C. Nicholas, "A Critical Evaluation of the Revised UNCITRAL Model Law provisions on Regulating Framework Agreements" (2012) 2 *P.P.L.R*. p.21. From the Guide to Enactment para.3 at p.26. "Efficiency" in the procurement context refers to the "relationship between the transaction costs and administrative time of each procurement procedure and its value are proportionate". According to *Schooner et al*., "The key to efficiency is speed". See S. L. Schooner, D. I. Gordon and J. I. Clark, "Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations", (2008) *GW Law Faculty Publications and Other Works*, at p.9

of similar purchases into a single procurement proceeding, thus generating administrative savings, for both procuring entities and suppliers. Many steps, such as solicitation and qualification and responsiveness assessment can be conducted once in advance. Procuring entities, therefore, do not need to repeat the procurement process, and time and cost in carrying out the procurement exercise can be amortised across the subsequent orders. The benefit of administrative efficiency exists not only for the purchaser, but also for the suppliers, especially SMEs.

Where framework agreements are used in centralised purchases, they can facilitate economy of scale and allow procuring entities access to volume discount.[56] Moreover, centralised frameworks allow procuring entities to take advantage of procurement expertise and skills of others, especially where centralised purchasing bodies are involved. They can also foster information-sharing in the procurement market for common solutions to similar problems.

The increasing use of electronic techniques, such as electronic reverse auctions and electronic catalogues, is facilitating the increasing use of framework agreements. They can enhance transparency and competition but impose

[56] OECD, "The Korean Public Procurement Service: Innovating for Effectiveness" (2016), 62, available at http://www.oecd.org/gov/the-korean-public-procurement-service-9789264249431-en.htm (accessed Aug 15, 2018); See Albano, Ballarin and Sparro, fn. 23, *supra*, pp.3-4

minimum administrative burdens. Many procurement systems invest efforts and resources into constructing and operating electronic procurement systems. The development of e-procurement is envisaged to further optimise the benefit of framework agreements.

However, administrative efficiency is never the only procurement objective, the achievement of which may compromise others, such as integrity and value for money.[57] In order to obtain and maximise administrative efficiency, transparency and competition requirements that apply in other procurement methods are usually loosened in the context of framework agreements, especially at the second stage. Informed by the EU and US experiences on the issue, the call-off stage is often observed to be "a much darker and uncompetitive world".[58] The relaxed safeguards create great opportunities for abuse and misuse, leading to problems such as corruptive practice and procurement frauds, which may occur without being noticed or checked. In fact, the orders under

[57] For more analysis regarding procurement objectives, see S. L. Schooner, "Desiderata: Objectives for a System of Government Contract Law" (2011) GW Law Faculty Publications and Other Work; S. Arrowsmith, J. Linarelli and D. Wallace, *Regulating Public Procurement: National and International Perspectives* (Kluwer Law International, 2000)

[58] C. R. Yukins, "Are IDIQs Inefficient? Sharing Lessons with the European Framework Contracting" (2008) 37 *P.C.L.J* p,547; Europe Economics, *Evaluation of Public Procurement Directives*, Market/2004/10/D, (2006) p.21, available at https://ec.europa.eu/docsroom/documents/15450/attachments/1/translations/en/renditions/native (accessed Sep 26, 2018).

framework agreements are often exempt from supplier review to different extent, leading to less accountability. Despite the above, it is not uncommon that procuring entities use frameworks simply for administrative convenience, whereas other awarding procedures turn out to be more appropriate. Value for money can hardly be achieved in this case.[59]

On the other hand, the time and cost for operating two-stage procedures in a framework agreement, with or without the second-stage competition, tend to be higher than that to run the single-stage award procedures when purchasing similar items. [60] A framework agreement would be considered administrative efficient only when the expected benefits, which may derive from economy of scale and effective amortisation over a large amount, overweigh the additional costs and time to deliver two stages of operation.

Apart from improving administrative efficiency, framework agreements can provide an effective solution to responding to urgency procurement, for instance, in catastrophes. The occurrence of urgencies/emergencies is inevitable, and many items that are commonly required in disasters can be reasonable predicted (i.e. water, tents, medicines, and etc.). Once a framework agreement is put in place for those expected

[59] S. Arrowsmith, fn. 30 *supra*, p.1102; See Nicholas, fn. 56, *supra*, p.21. See also Guide to Enactment, p.199
[60] See Albano and Nicholas, fn. 1, *supra,* pp.23-24

items in advance, it enables direct awards, expedite deliveries and secures supply when requirements arise, which is especially the case when the framework is binding on the supply-side. Because the supplier parties are selected on a competitive basis before the advent of disasters, framework agreements can reduce or avoid the use of other none or less competitive and transparent procedures, such as single-source procurement. Problems of excessively high prices, poor quality, and short of supply are less likely in the context of frameworks.[61]

Moreover, using framework agreements is also likely to deliver better outcomes for smaller (low value) procurements.[62] In many systems, smaller purchases of simple supplies and services are often exempt from formal procurement proceedings. Framework agreements through demand aggregation can subject these small purchases to a more transparent and competitive proceeding.[63]

Furthermore, the use of framework agreements may encourage SMEs to participate in the procurement market, i.e. through lots division. In the EU, procuring entities are encouraged to divide large contracts into lots to facilitate access

[61] See J. I. Schwartz, "Katrina's Lessons for Ongoing US Procurement Reform Efforts", (2006) 15 *P.P.L.R.* 362
[62] Guide to Enactment, p.196 para. 4 (c)(d)
[63] *Ibid.*, p196 para. 4(c); C. Nicholas, "Framework Agreements and the UNCITRAL Model Law on Procurement" (2008) 17 *P.P.L.R.,* 228

of SMEs.[64] On the other hand, however, aggregation may have negative impact on competition, putting SMEs at a disadvantaged position, as further discussed at the next page. Where a number of smaller purchases converge into a single arrangement, SMEs may be deterred by the aggregated value, sizeable quantity and/or the composition of diversified requirements, especially in centralised purchases.[65] In this regard, framework agreements may limit the market access of SMEs, instead of encouragement.[66]

Also, framework agreements can enable procuring entities to exploit the full potential of centralised purchasing.[67] Through greater demand aggregation, centralised frameworks can leverage the bargaining power of the public purchaser and facilitate economies of scale, thus leading to cheaper prices and better terms. Meanwhile, they also retain certain flexibility in allowing customisation of requirements of different user entities.[68] The use of centralised frameworks may further foster uniformity and standardisation of the "procurement language" in the public procurement market. Uniformity could encourage

[64] The *2014 Public Sector Directive*, Recital 66; Crown Commercial Service, *A Brief Guide to the EU Public Contracts Directive* (2014), 3, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/407236/A_Brief_Guide_to_the_EU_Public_Contract_Directive_2014_-_Feb_2015_update.pdf (accessed Aug 26, 2018).
[65] See Arrowsmith and Nicholas, fn. 25, *supra,* p.109
[66] See Nicholas, fn.55, *supra,* p.2
[67] See Albano, Ballarin and Sparro, fn. 23, *supra*, p.6
[68] Arrowsmith and Nicholas, fn. 25, *supra*, p.106

participation, especially for SMEs, as they need not invest a lot of time and resources in conforming to various requirements in different procurements.[69]

However, the above benefits of centralised purchases, especially economies of scale, may come at a cost. Concerns were expressed about the potential adverse impact on competition that frameworks may have in the long term. The large and sizeable contracts, implied by central purchases, tend to favour large suppliers over SMEs due to more stringent economic requirements. In practice, a trend has been observed towards large-scale contracting in the use of framework agreements, to which only large suppliers can respond, and SMEs would be driven out.[70]

By restricting participation and competition, excessive aggregation may facilitate anti-competitive activities and may nurture the market power of very a few suppliers, usually the large suppliers, leading to an oligopolistic market. Consequently, the larger the contract is, the harder SMEs are possible to participate and the fewer the participants there will be in the competition "tomorrow".[71] There is, thus, a risk that unduly

[69] See Albano, Ballarin and Sparro, fn. 23, *supra*, p7
[70] See Albano and Nicholas, fn. 1, *supra*, p.29
[71] Recital 59 of the *2014 Public Sector Directive* provides "…the aggregation and centralisation of purchases should be carefully monitored in order to avoid excessive concentration of purchasing power and collusion…". See also European Commission, *Executive Summary. Impact Assessment Accompanying the Proposal for a Directive on Public Procurement*,

pursuing the short-term savings may jeopardise the long-term value for money and sustainable competition.

Thus, as Albano points out, "market intelligence and experiences are crucial to fine-turning the appropriate degree of demand aggregation."[72] Where centralised purchasing bodies are involved, framework agreements tend to be vulnerable to organisational conflicts of interest, whereby these bodies may abuse or overuse frameworks for their own interest, i.e. for commission fees.[73] Some centralised purchasing bodies may be more sensitive to the input from the supply-side instead of the purchasers. Consequently, centralised framework agreements may not best satisfy the real needs of the user entities. The main reason for the above "failed" procurement outcomes is arguably the separation of roles between the user and purchaser of framework agreements.

Further, better supply chain management is envisaged in using framework agreements, as they allow better scheduling of deliveries and thus reduce the significant consequences costs, i.e. warehousing expenses and inventory control.[74] Framework agreements, as mentioned above, can assist in ensuring

20.12.2011, SEC (2011) 1586 final; OECD, "Public Procurement in Neuvo Leon, Mexico: Promoting Efficiency Through Centralisation and Professionalisation" (OECD Public Governance Reviews, 2018), p.34

[72] See Albano, fn. 18, *supra*, p.160

[73] See Nicholas, fn. 55, *supra,* p.37

[74] *Ibid.* p.2

security of supply, particularly in the multi-supplier context and where frameworks are binding on the supplier(s).

On consideration of the above, procuring entities should make trade-offs between the expected benefits and risks/costs in determining whether a framework agreement is the appropriate solution to the procurement at issue. The decision-making will be an important and complicated process, which should be based on comprehensive analysis of demands and market and careful design considerations, calling on high levels of procurement capacity. The decision should also be premised on and reflect the balance between different procurement objectives in a specific procurement system.

5 Summary

This chapter provides a relatively comprehensive survey of the main features of framework agreements. They are procurement arrangements comprising two stages of operations: the first stage used to conclude a master agreement with selected supplier(s) and the second stage for awarding specific call-offs when requirements arise. The primary incentive for using framework agreements is to improve administrative efficiency particularly in repeated purchases of standard goods and simple services. The other main motivations include ensuring security

of supply, greater transparency and competition for smaller purchases, effective responsiveness for urgent procurements and greater economy of scale in centralised purchases.

Framework agreements can manifest in various types based on different elements. The common elements mainly include the number of the parties involved, the involvement of second-stage competition, the degree of openness to new suppliers, and whether the agreements are binding on the parties. These variables are not mutually exclusive but interact with each other, forming different permutations of framework agreements that can be seen in practice. The decision to choose among the types can be complex and should be on a case-by-case basis.

Chapter III. Experience in Framework Agreements in the UNCITRAL Model Law, the EU and US Federal Systems

1 Introduction

Framework agreements are globally popular procurement arrangements. Much long-established experience with framework agreements can be found on both sides of the Atlantic, in the EU (especially in some Member States including the UK), and the US. In light of the benefits as explained in Chapter I, and to reflect their international take-up, the *2011 UNCITRAL Model Law on Public Procurement* (the *Model Law*)[1] introduced framework agreements with specific rules, which are recommended to the enacting States as part of their national law.

The purpose of this chapter is to review the different approaches to practicing and regulating framework agreements taken by the *Model Law*, in the EU (including the UK), and the US federal systems, with the aim of indicating the good practice and high-risk areas in addressing frameworks. The relevant international experiences and lessons are expected to support and "navigate" other developing procurement systems, such as

[1] *2011 UNCITRAL Model Law on Public Procurement* (Vienna, June 27th –July 8th, 2011), 44th session, available at http://www.uncitral.org/uncitral/en/uncitral_texts/procurement_infrastructure/2011Model.html (accessed Oct 1, 2018).

China, when designing and improving their domestic procurement regulations on this issue.

2 Framework Agreements Under the UNCITRAL Model Law on Public Procurement

2.1 Overview

The express provisions dedicated to framework agreements were introduced in the 2011 *Model Law*. The late debut allowed the UNCITRAL to draw on the earlier experiences in regulating frameworks from the EU and US. The *Model Law* is aimed to serve as a "model" for the enacting States, mainly developing countries, to establish and modernise their procurement laws and to facilitate harmonisation of procurement regulation internationally.[2] Therefore, it adopts the most comprehensive and "strict" regulation on framework agreements, representing a high "benchmark" and with extensive guidance. The provisions of the *Model Law* are designed to help achieve the benefits of framework agreements on the one hand and to mitigate their potential risks, i.e. the competition and transparency concerns, on the other.[3]

[2] *Guide to Enactment of the UNCITRAL Model Law on Public Procurement* (2014, New York), p.2 para.5. Hereinafter referred to as Guide to Enactment.
[3] Guide to Enactment, p.197 para.7

2.2 Definitions and Types of Framework Agreements

The *Model Law* distinguishes a framework agreement itself from a procurement contract by providing separate definitions of "framework agreement procedure" and "framework agreement". A framework agreement *per se* is the outcome of the first stage procedure of a "framework agreement procedure" and a procurement contract is awarded at the second.[4] This means all procedural safeguards and challenge proceedings apply at both stages of a "framework agreement procedure". Thus, full transparency and competition requirements cover the entire procurement process.[5]

Under the *Model Law*, three basic types of framework agreements are provided: (i) closed framework agreements without second-stage competition; (ii) closed framework agreements with second-stage competition; and (iii) open framework agreements.

The *Model Law* actually provides all types of framework agreements identified in Chapter II, which are mutually inclusive. The former two types are closed frameworks, while

[4] *The Model Law*, art. 2. The difference between a procurement contract and a framework agreement is not affected by the fact whether the latter may be an enforceable contract based on the domestic contract law of the enacting state.

[5] By contrast, the equivalents in the US (IDIQ contracts) are defined as contracts, as a result of which the ordering stage is excluded from full transparency and competition, as explained later.

the type (iii) is open one. A closed framework agreement without second-stage competition may be awarded with single or multiple suppliers, whereas a closed framework with second-stage competition and an open framework can only be multi-supplier. Under the *Model Law*, the second-stage competition takes place where not all terms and conditions are established at the time of concluding a framework agreement itself.[6]

2.3 The Conditions for the Use of Framework Agreements

Article 32 of the *Model Law* sets out two conditions for use of framework agreements, which should apply before actually embarking on a framework agreement procedure. The aim is to assist procuring entities in determining whether a framework agreement is more appropriate in a given procurement project.[7]

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[6] Article 2 of *the Model Law* provides definitions of "open framework agreement", "closed framework agreement", "framework agreement without second-stage competition" and "framework agreement with second-stage competition".

[7] Considerable discussions were brought out regarding whether there should be express conditions for the use of framework agreements in the process of drafting framework agreements-related provisions. The Working Group finally decided to retain conditions for use in light of the inherently anti-competitive potential of framework agreements that may be easily abused and abused. For more discussion, see UNCITRAL, "Report of Working Group I (Procurement) on the Work of Its Thirteenth Session", *(*New York, 2-11 April, 2008*)* A/CN.9/648; "Report of Working Group I (Procurement) on the Work of Its Fifteenth Session" (New York, 2-6 February, 2009), A/CN.9/668, available at http://www.uncitral.org/uncitral/en/commission/working_groups/1Procurement.html (accessed Aug 26, 2018). There are no equivalents of such requirement in the EU or US federal system.

Two conditions for use are established, covering all three types of framework agreements, including (i) the need is expected to arise on an indefinite or repeated basis during a given period; or (ii) the need may arise on an urgent basis by virtue of the nature of the subject matter.

With regard to the first circumstance, the need is considered "indefinite" where "the extent, timing and/or quantity are unknown, or it is expected to be repeated".[8] Thus, it is argued that setting out two parallel conditions by using terms of "indefinite" and "repeated" seems unnecessary, because repeated purchases can be absorbed by the "indefinite" any way. On the other hand, the explanation further suggests that the needs on "indefinite" basis can but not necessarily cover repeated cases. Other situations subject to "indefinite" nature may also be included, for instance, a framework agreement with an uncertain one-off purchase in the future.

Another issue related to this condition regards the term "expected". Both the *Model Law* and the *Guide to Enactment* are silent on how to construe "expected".[9] It therefore remains unclear how a procuring entity can objectively assess the likelihood of the indefinite or repeated need. Such unclarity may leave some room for discretion and improper use of frameworks.

[8] Guide to Enactment p.268 para.2
[9] Guide to Enactment provides that the "expectation" should be addressed at the level of enacting states through "rules and guidance" at p.260

The second condition allows framework agreements being used to respond to urgent procurement, which may result from natural disasters, catastrophes, pandemics and others. [10] Establishing a framework for items that are anticipated to be usually needed in urgent situations enables the government to promptly and easily place orders when urgent events take place.[11] Doubts are expressed whether and why such condition should be separately listed, as the uncertainty in urgency purchases is essentially of "indefinite" nature. Thus, urgency cases can be considered as a sub-situation of the condition (i).[12] According to Nicholas, providing a separate condition (ii) was intended to accentuate the adoption of framework agreements in urgent circumstances, thus avoiding the use of other less transparency methods.[13]

Apart from the above two express conditions for use under the *Model Law*, the Guide to Enactment additionally suggests procuring entities to conduct a cost-effective analysis to determine whether to use a framework agreement procedure.[14]

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[10] *Ibid*., pp.206-207 para.2
[11] The lesson from Hurricane Katrina in the US particularly proves the potential benefits in urgency procurement. See J. I. Schwartz, "Katrina's Lessons for Ongoing US Procurement Reform Efforts" (2006) 6 *P.P.L.R*. 362
[12] C. Nicholas, "A Critical Evaluation of the Revised UNCITRAL Model Law Provisions on Regulating Framework Agreements" (2012) 2 *P.P.L.R* p.25
[13] *Ibid.* See also UNCITRAL, Report of Working Group I (Procurement) on the work of its thirteenth session, 41st session (New York, 16th June-11th July 2008), A/CN.9/648 para32, available at http://daccess-dds-ny.un.org/doc/UNDOC/GEN/V08/531/47/PDF/V0853147.pdf?OpenElement (accessed July 28, 2018)
[14] Guide to Enactment, p269, para.4

As aforementioned in Chapter II, framework agreements, especially those with second-stage competition, tend to incur higher administrative costs than that in other single-stage arrangements or methods.[15] Therefore, the use of framework agreements in a given procurement can be rightly justified where the analysis demonstrates the potential benefits could outweigh the extra costs. For instance, the positive outcome is more likely to arise in repeated purchases of relatively standard items as the extra costs can be amortised over a stream of orders.[16] However, a difficulty that may reside with a procuring entity is that some potential benefits, such as administrative efficiency, may not be easily quantified and converted into monetary value and would complicate the analysis.[17]

Art.32(2) requires the procuring entity to record the reasons and circumstances that justify first, the decision to use a framework agreement procedure *per se* and secondly, the specific type of framework agreements selected. However, the *Model Law* itself is silent on specifying conditions for use for any particular type of framework agreements, whilst the Guide to Enactment provides some guidance. The selection of the appropriate type of framework agreements is hinged on the

[15] *Ibid*. p.207 para.4
[16] *Ibid*. pp. 200-201
[17] C. Nicholas, fn. 12, *supra*, at p33

circumstances of the given procurement, and the enacting states are suggested to issue guidance in this respect.[18] Broadly speaking, such recording requirement alerts procuring entities to ponder whether and how to use framework agreements, serving as a safeguard of integrity and accountability.

2.4 The Operation Procedures of Framework Agreements

The *Model Law* regulates both stages of a framework agreement procedure in detail. The detailed provisions, especially those regarding the second-stage, are to ensure transparency and competition, which are often at risk in using frameworks in the EU and US. Moreover, the Guide to Enactment points out the importance of appropriate planning and design in striking a balance between safeguarding transparency and competition on the one hand and ensuring administrative efficiency on the other.

[18] Guide to Enactment pp.261-263. Arrowsmith and Nicholas provide that further considerations on the structure and operation of framework agreements, such as whether the second-stage competition is involved, whether and to what extent the framework agreement is binding on the parties, etc., should also be factored into the decision regarding whether a framework agreement should be used in the given procurement. See C. Nicholas, fn. 12, *supra*, at p.34; S. Arrowsmith, "Methods for Purchasing On-going Requirements: The System of Framework Agreements and Dynamic Purchasing Systems Under the EC Directives and UK Procurement Regulations" in S. Arrowsmith (ed.) *Reform of the UNCITRAL Model Law on Public Procurement : Public Procurement Regulations in the 21st Century* (Eagan, MN: West, 2010), pp.158-160

2.4.1 *The first stage*

2.4.1.1 First stage of a closed framework agreement

A closed framework agreement, with or without the second-stage competition, should be established via open tendering, or other methods in exceptional cases with justification.[19] It means open tendering should be considered as the default option to conclude a framework while the use of other methods may be allowed when the relevant conditions for use apply.[20] The "conclusion" procedure to be used should be factored into the fundamental decition whether a framework agreement is appropriate in the given procurement. The procuring entity should justify and record the use of any methods other than open tendering.[21]

The *Model Law* requires detailed information to be included in the solicitation. The purposes of such disclosure requirement are three-holds: (i) to provide potential suppliers with information as complete as possible, enabling them to assess whether they have interest in participation and how to prepare tenders; (ii) to drive the procuring entity to conduct planning

[19] The *Model Law*, art. 58(1)
[20] Nicholas submits that methods other than open tendering, in most cases, tend to be inappropriate for setting up a closed framework agreement, especially in one with second-stage competition, as it may add to complexity of the planning. See C. Nicholas, fn. 12, *supra*, pp.39-40. Mandating open tendering at the first stage of closed framework agreements seems to be more appropriate with fewer risks of abuse, especially for developing systems where there is a low level of procurement capacity and integrity is considered a priority objective, such as China as analysed later.
[21] *The Model Law*, art.25(e)

based on careful market and demand analysis; (iii) to ensure consistency between two stages, avoiding potential abuses.

The main contents of the solicitation include: (i) a clear statement of a framework agreement procedure is involved; (ii) whether one or multiple suppliers will be involved, and if the latter case, any minimum or maximum limit on the number of suppliers admitted to the framework agreement[22]; (iii) the duration of the framework agreement; (iv) the description of the subject matter to be procured; (v) terms and conditions established at the first stage; (vi) the manner and award criteria for awarding subsequent contracts under the framework agreement; (vii) where the second-stage competition is involved, the necessary information pertinent to the competition required under Article 59(1)(d), including the procedure, estimated frequency of call-offs and award criteria.[23] The information will be repeated and consolidated in the framework agreement itself.

Despite the detailed disclosure requirement, the *Model Law* also allows possible flexibility. For instance, the estimated terms are required to the extent of known only, for instance, quantity, because they cannot be defined with sufficient precision at the

[22] Incorporating the limit on the number of suppliers to award the framework agreement is not an obligatory but an encouraging practice. Mandating provision of such limit may have enforcement difficulty, as there would be no consequence if the established limited number fails to be observed. See C. Nicholas, fn. 12, *supra*, p41

[23] *The Model Law*, arts. 58(2) and 59

first stage. Moreover, procuring entities may use evaluation criteria (and the relative weighting) in call-offs different from those used in concluding the framework agreement itself, provided that they are pre-disclosed, and the variation cannot lead to a change of the description of the subject matter.[24] Thus, the basis of the award will normally but not necessarily be the same between two stages, whereas both the conclusion and the subsequent call-offs should be awarded to either the lowest-priced bid or the most advantageous bid.[25]

To avoid any doubts, Article 58(3) expresses that the notification of successful submission and standstill periods, which apply to the award of procurement contracts in Article 22, should apply *mutatis mutandis* to the conclusion of a closed framework agreement.[26] The selection of supplier parties and the conclusion of the master agreement should be made public, including the identities of the supplier parties.[27] It needs to be particularly noted that "price" is not required being disclosed when concluding a framework. According to Albano and Nicholas,

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[24] *The Model Law*, art. 63; Guide to Enactment p.211 para.14.
[25] *The Model Law,* arts.59(1)(e), 61(1)(e). This means that rotation, an award method in practice, is not allowed at the second-stage of framework agreements under the Model Law.
[26] According to the *Model Law*, art.2(r), "standstill period" means the period starting from the dispatch of a notice, during which the procuring entity cannot accept the successful submission and during which the suppliers or contractors can challenge the decision. This article is considered necessary because as mentioned earlier, a "framework agreement" itself is not considered as a procurement contract, which is only awarded at the second stage of a "framework agreement procedure" under the *Model Law*.
[27] *The Model Law*, art. 23(1)

this is mainly based on considerations that prices cannot be sufficiently finalised at this stage and are therefore less indicative. However, an unintentional by-product of withholding the information on price may be a reduced risk of collusion through disrupting the flow of information.[28]

2.4.1.2 First stage of an open framework agreement

All open framework agreements should be on fully electronic basis. Since they involve on-going application and submission from new suppliers at any time, a specific first-stage procedure is provided under the *Model Law* for open frameworks.[29]

The procuring entity, to set up an open framework agreement, starts soliciting participation in accordance with the requirements for open tendering.[30] The information to be included in the solicitation for an open framework is largely identical to that in a closed one, including a clear statement that an open framework agreement procedure is involved, the description of the subject matter, the terms and conditions for suppliers to be admitted in the framework and other information regarding how the framework will operate.[31]

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[28] G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press, 2016), p.234
[29] *The Model Law*, art. 60 and 61
[30] *Ibid*. art. 62
[31] *Ibid.* art. 60 (3)

In the case of multi-user frameworks, including centralised purchases, the identities of all procuring entities that have right to use the framework agreement should be identified in the solicitation. This requirement tends to imply that new entities are desisted from ordering under the existing framework.[32]

Apart from that, the solicitation must expressly declare that suppliers can join the open framework at any time.[33] The solicitation is standing during the lifespan of the framework, and the procuring entity should republish the solicitation "at least annually".[34] Thus, the suppliers who missed the initial advertisement, who had no interest or capability in participating at an earlier point, who entered the procurement market recently can apply to join the open framework at any time.[35]

The first stage of an open framework, due to its very "open" nature, does not involve full comparisons and evaluation between tenders, in contrast to the full and head-to-head competition in a closed one. At this stage, only qualification and responsiveness of suppliers will be examined.[36] The tenders submitted at the first stage are "indicative" and each tender is

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[32] *Ibid.* art. 60 (3)(a)
[33] *Ibid.* art. 60 (4)
[34] *Ibid*. art 61(2)
[35] S. Arrowsmith and C. Nicholas, "Regulation Framework Agreements Under the UNCITRAL Model Law on Procurement", Ch.2 in S. Arrowsmith (ed.), *Reform of the UNCITRAL Model Law on Procurement: Procurement Regulation for the 21st Century* (Eagan, MN: West, 2010) p.134
[36] Guide to Enactment, pp.284-285

evaluated on its own. And all qualified suppliers with responsive tenders should be admitted to the framework agreement.[37] There is no limit on the maximum number of suppliers to be accepted unless such limitation derives from the technical capacity deficiency subject to justification.[38] Once the procuring entity has made a decision regarding a submission, it should promptly notify the supplier of whether it has become a party to the framework agreement, and of the reasons for rejecting the submission if it has not.[39]

Article 60(5) provides a maximum time limit for the examination and decisions of applications to join the framework. Such time limit should be short because first, only qualifications and responsiveness are subject to examination and secondly, dilatory processing may impede the applicants from participating in an imminent order.[40] The procuring entity should ensure "unrestricted, direct and full access" to the terms and conditions of the framework as well as any necessary information regarding its operation throughout the process.[41]

[37] *The Model Law*, art. 60 (6)
[38] *Ibid.* art. 60 (3)(d)(ii) and (7)
[39] *Ibid.* art. 60 (8)
[40] Guide to Enactment p.223 para.4. Similarly, the EU Directives set out an explicit requirement of prompt decision-making regarding request to join the Dynamic Purchasing System, the equivalent of open framework agreements.
[41] *The Model Law*, art. 61(2)

2.4.2 *The second stage*

The second stage of a framework agreement of all types is regulated under Article 62, most of which pertains to frameworks with second-stage competition, closed or open. It is reiterated that under all framework agreements, only the supplier(s) admitted will be considered for the contracts awarded under it.[42] Among the three procurement systems selected, the *Model Law* is submitted to provide more robust transparency and competition safeguards at the second stage.

Where no second-stage competition is involved, the procuring entity simply selects among the supplier parties of the framework, and awards a contract following the pre-established terms and conditions and based on the pre-disclosed evaluation criteria disclosed.[43] Simply put it, the contracts must be awarded within the original scope of the framework agreement.

In the context of multi-supplier frameworks, the procuring entity is under no obligation to (i) notify the supplier parties of any upcoming call-off opportunity; and (ii) apprise the supplier parties of its decision regarding a specific award or the reasons.[44] There is a huge information asymmetry regarding

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[42] *The Model Law*, art. 62(2)
[43] *Ibid.,* art. 62(1)(2)
[44] According to Article 62, the notification of upcoming call-offs only applies to contracts awarded under a framework agreement with second-stage competition. Article 22 is cross-referenced under Article 62(3) regarding the acceptance of successful submission, with the standstill periods requirement exempt in framework agreements without second-stage competition in paragraph (3)

the call-off stage, which is fully known to the procuring entity and the successful supplier in a specific order, but unknown to the other supplier parties. They may have been unaware of the award opportunity until the contract is performed. As Nicholas says, the lack of transparency regarding the call-off stage of framework agreements without second-stage competition is an "exception" to the generally "high standard" of the *Model Law*.[45]

Furthermore, Article 22(3) expressly exempts the awards under a closed framework agreement with direct awards from the application of the standstill periods. The compromised transparency, together with the standstill exemption may create breeding grounds opportunities for potential abuses of frameworks. For instance, a procuring entity may favour a specific supplier who may not provide the best value offer.

Where a second-stage competition is reopened (in some closed frameworks and all open frameworks), the call-off procedure is regulated in a more detailed manner under Article 62(4), the "heart" of which is to ensure transparency and competition. To that end, the *Model Law* imposes stringent information obligations regarding awards based on second-stage competition.

[45] See C. Nicholas, fn. 12 *supra*, p. 43

When an actual requirement arises, the procuring entity should issue invitations either to all the supplier parties or only to those "capable of meeting the needs".[46] In the latter case, an *ex-ante* notice of the upcoming call-offs must be issued to all the supplier parties simultaneously, who can request to participate in the competition if being considered "incapable".[47] The option to limit the tenders to the capable suppliers could avoid evaluation of unresponsive submissions and thus enhance efficiency. A prior notice of future awards can ease the risk of abuse associated with the above selective invitation.[48] On the other hand, concerns are also raised regarding the extra administrative costs and burdens of mandating a prior notice to all supplier parties. Nevertheless, in light of the rapid development of information technology in public procurement, it is considered that operating such notification on electronic basis can fulfil the requirement but with minimised costs.

Notably, the *Model Law* is silent on what "capability" means and how to objectively assess the "capability". It seems more sensible the "capability" herein refers to the eligibility to fulfil

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[46] *The Model Law*, art 62 (4)(a)
[47] *Ibid.* art 62 (4)(a)(ii)
[48] Mandating the notification of any upcoming competition is suggested to be a way forward to address the general transparency loophole of the second-stage of framework agreements in the EU. See M. Andrecka, "Framework Agreements: Transparency in the Call-off Award Process", presented in the *Public Procurement: Global Revolution VII* (Nottingham June 2015)

each specific call-off, rather than the suppliers' basic qualification, which has been assessed at the outset.[49]

The content of the invitation for a second-stage competition is provided under Article 62(4)(b), which to a large extent repeats those articulated in the framework agreement itself and includes the terms and conditions to be finalised or refined through the competition and the information regarding how the second-stage competition operates.

The procuring entity should evaluate the submissions received from the invited suppliers based on the award criteria and procedures indicated in the invitation. The acceptance of the successful submission and the award of a procurement contract should fully comply with the requirements under Article 22, including notifying the tenderers of the decision and applying the standstill periods.[50]

Once a contract is awarded, the procuring entity shall promptly publish an award notice.[51] Alternatively, to reduce administrative burden, a cumulative notice of low-value awards is required at least once a year. The "loose" notification

[49] C. Nicholas, "Framework agreements and the UNCITRAL Model Law on Procurement" (2008) 5 *P.P.L.R.*, NA227

[50] *The Model Law*, art 62(4)(c). The only exemption on awards under a framework agreement without second-stage competition under Article 22(3) means that in the conclusion of a framework itself, either open or closed, and in all contracts awarded under a framework agreement with second-stage competition, the standstill periods apply.

[51] *The Model Law*, art 23. Public notice regarding the awards at the second stage is required for Framework agreements of all types.

obligation is intended to make a trade-off between transparency and administrative efficiency.

2.5 Challenges

The existence of an effective challenge mechanism is considered as a necessary part of an integrated public procurement system.[52] It plays a crucial part in self-policing and self-enforcing the procurement rules, by virtue of its "deterrent and corrective effects". The *Model Law* provides the challenge proceedings in Chapter VIII and makes it mandatory for enacting States to incorporate into their national systems.[53] Under the *Model Law*, challenges may be brought to the procuring entity, an independent body and to the court.[54]

De jure, the full package of challenge proceedings applies to both stages of a framework agreement, subject to very limited exceptions. Particularly noteworthy is the application of the challenge proceedings to the second stage of framework agreements, which may be an effective safeguard that deters

[52] Guide to Enactment p.228 para.1; X. Zhang, "Supplier Review as a Mechanism for Securing Compliance with Government Public Procurement Rules: A Critical Perspective" (2007) 5 *P.P.L.R.* pp. 325-332
[53] In the 1994 *Model Law*, the supplier review mechanism was optional for enacting States and could be excluded. However, such optional nature has been removed and providing a challenge system is mandatory if an enacting State wishes to incorporate the *Model Law*.
[54] *The Model Law*, art 64(2)

the improper use of such arrangements, i.e. awards based on favouritism.

Such "extension" of the challenge mechanism represents a high and advanced standard of integrity and accountability among the selected procurement systems. By contrast, the EU Directives are silent on the remedies on call-offs under framework agreements while in the US federal system, protests against task order or delivery orders (against IDIQ contracts) are explicitly banned to a large extent, as explained later.

Taking a holistic view, it is logical to subject the second stage of frameworks to the challenge mechanism under the *Model Law* for several reasons. Firstly, Article 64(1) provides that challenges may be against any decision or action without exception, which arguably implies any decision or action at both stages in the context of framework agreements.[55] Secondly, as explained in Chapter II, the *Model Law* differentiates a framework agreement itself from a procurement contract, which is concluded at the end of a framework agreement procedure. In this regard, all transparency and challenge safeguards should apply until the award of a procurement contract, thus covering

[55] The right to challenge is addressed under Article 64(1) of *the Model Law*, according to which a supplier or contractor has the standing to file a challenge if it has suffered or may suffer from loss or injury because of the alleged non-compliance of a decision or action of the procuring entity. Thus, the standing is restricted to potential suppliers and contractors only that have actually participated in the procurement process. It further means the sub-contractors and the general public are excluded from "the ambit of the right to challenge." See Guide to Enactment, p. 306, para.2.

the second stage. Moreover, the robust transparency requirements that apply at the second stage make the challenge proceedings meaningful.

Thirdly, the *Model Law* is intended to help the enacting States, mainly the developing countries that do not have adequate legal and institutional frameworks for public procurement, to strike a proper balance between integrity and administrative efficiency, in order to promote the beneficial use of framework agreements and to avoid their inappropriate use. The application of the challenge proceedings to the second stage is squarely in line with the very "objective" of the *Model Law.* Furthermore, several provisions particularly affirm the availability of challenge proceedings at both stages. For instance, Articles 58 and 62 expressly state that the acceptance and notification of successful submissions and standstill periods do apply to both stages of frameworks, with limited exceptions.

In respect of the first stage of a framework agreement, challenges may be filed against the terms of the solicitation, the decision excluding a potential supplier from the qualification process, or the conclusion of the framework itself. As mentioned above, the standstill periods apply to the conclusion of a framework agreement of all types.

Regarding the second stage, it is necessary to make a difference between frameworks with a second-stage

competition (open or closed) and those without. Under a framework without reopening a mini-competition, the procuring entity can place an order directly. There are few problems if the framework is single-supplier.

Where multiple suppliers are involved, however, the challenge mechanism is less effective. As aforementioned, the procuring entity is not obliged to notify the supplier parties of any order opportunities or its decision of award. In fact, this arguably means challenges against the call-offs can, in most cases if not all, only be filed after the contract awards. Nevertheless, aggrieved suppliers may have missed the opportunity to challenge the breach at issue. More importantly, taking post-award remedial actions tend to be more challenging and less effective. Apart from the uneven transparency, the exemption of the application of standstill periods in awards under frameworks without second-stage competition, as mentioned in the earlier section, particularly exacerbates the difficulty concerning the second-stage challenges.[56]

In the cases of framework agreements with second-stage competition, all actions and decisions regarding the second-stage competition can be challenged, including the decision being considered "incapable" for the call-off in question and not

[56] *The Model Law*, articles 58(3), 62(3) and 22.

being invited for the mini-competition concerned.[57] The standstill periods should apply to all contracts awarded through second-stage competition, except for smaller awards valued below the specified threshold.[58] The thorough coverage of challenges is supported by the robust transparency safeguards imposed at the second stage of frameworks of this type.

As explained earlier, the procuring entity is obliged to notify all supplier parties of (i) the upcoming competition under Article 64; (ii) the successful submission under Article 22. It is required to further publish notice regarding the contract award under Article 23. These information obligations provide opportunities for aggrieved suppliers to challenge timely, reflecting the entrenched integrity objective in the context of framework agreements.[59]

In general, the *Model Law* sets a high benchmark of supplier review in framework agreements. Robust transparency and review safeguards are fully applicable to framework agreements with second-stage competition, which are "discounted" in frameworks where call-offs are based on direct awards.

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[57] *Ibid.*, art.62(4)(b)(ix)

[58] *Ibid.*, art. 22(3)(c). As explained earlier, in the exceptional case, a cumulative notice of all smaller awards is required at least once a year.

[59] Where the procuring entity chooses to invite those "capable" suppliers to the second-stage competition, complaints may be raised by the non-invited supplier parties who requested to participate but were rejected, in which case they should be lodged within the standstill period, or if no standstill period applied, prior the entry into force of the contract, in accordance with the *Model Law*, arts.66(2), 67(2)(b)

3 Framework Agreements and Dynamic Purchasing Systems: Under the 2014 EU Directives and UK Implementing Regulations

3.1 Overview

In the EU Directives, two procurement arrangements are provided that are relevant to framework agreements as described in Chapter II: framework agreements and dynamic purchasing systems. As per the classification in chapter II, framework agreements can fall into the category of "closed framework agreements", and dynamic purchasing systems may fall into "open framework agreements". Both of them are available in both the public and utilities sectors.

This section examines how framework agreements and dynamic purchasing system are dealt with at the EU level and in the national procurement system of the UK. The research will also take a brief look at qualification systems (often known as supplier lists in other procurement systems), a procurement tool permitted in the utilities sector only since they are closely related to and are often confused with framework agreements.

At present,[1] the legal instruments at the EU law level on public procurement include the *Directive 2014/24/EU*[2] (2014 PSD), the *Directive 2014/25/EU*[3] (2014 UD), as well as the *Remedies Directives*[4] when it comes to remedy issue. In the UK, these Directives are implemented through the *Public Contracts*

[1] The formal rules governing the use of framework agreements and dynamic purchasing systems were generally introduced to the EU public procurement rules in 2004. Before the formal authorisation, the use of framework-type techniques had been used in some member states already, including the UK, France and Sweden. In fact, in as early as 1993, the use of framework agreements was dealt with under the then 1993 Utilities Directive. In 1997, the European Commission challenged the improper use of framework contracts by Northern Ireland Department of the Environment for procuring architecture, engineering and other construction-related services. This case and the UK's discussion with the Commission became an impetus, ultimately driving the inclusion of framework agreements within the *Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the Coordination of Procedures for the Award of Public Works Contracts, Public Supply Contracts and Public Service Contracts* [2004] L 134/122 (2004 Public Sector Directive). Regarding dynamic purchasing systems, their advent initially stemmed intuitively from the marked development of electronic techniques and burgeoning voice of the governments for flexibility for standard purchases via e-catalogues. It was first introduced in the 2004 Public Sector Directive. However, the previous rules made them administratively cumbersome and inefficient, which had been rarely used in the Member States. Given that, the 2014 EU Directives significantly simplify the relevant rules to make them laudable.

[2] *Directive 2014/24/EU of the European Parliament and of the Council on public procurement and repealing Directive 2004/18/EC* [2014] OJ L94/65

[3] *Directive 2014/25/EU of the European Parliament and of the Council on procurement by entities operating in the water, transport, energy and postal services sectors and repealing Directive 2004/17/EC* [2014] OJ L94/243

[4] *Council Directive of 21 December 1989 on the Coordination of the Laws, Regulations and Administrative Provisions Relating to the Application of Review Procedures to the Award of Public Supply and Public Works Contracts* (89/665/EEC) [1992] OJ L 076; *Council Directive 92/13/EEC Of 25 February 1992 Coordinating The Laws, Regulations and Administrative Provisions Relating to The Application Of Community Rules on the Procurement Procedures Of Entities Operating in the Water, Energy, Transport And Telecommunications Sectors* [1992] OJ L 395. They are amended by the *Directive 2007/66/EC of the European Parliament and of the Council of 11 December 2007 Amending Directives 89/665/EEC and 92/13/EEC with regard to Improving the Effectiveness Procedures Concerning the Award of Public Contracts* [2007] OJ L335/3.

Regulations 2015 (2015 PCR) [5] and *Utilities Contracts Regulations 2006* (2016 UCR)[6]. The Directives apply only to procurements whose value is above the prescribed thresholds under the Directives, and those procurements that are outside the scope of the EU Directives, namely those below the thresholds are not considered in this research.

In the UK[7], the procurement system relies significantly on the judgment of individual government departments and procuring entities and officials who are given broad discretion.[8] Following the "tradition", the UK's approach to transposing the EU Directives has been largely copying the texts, with minor common law omits and additions.[9] Therefore, this research will specifically refer to the UK implementation practice where they vary from or develop the EU Directives on the same issue.

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[5] *The Public Contracts Regulations 2015*, available at http://www.legislation.gov.uk/uksi/2015/102/pdfs/uksi_20150102_en.pdf (accessed Aug 5, 2018)

[6] *The Utilities Contracts Regulations 2006*, available at http://www.legislation.gov.uk/uksi/2006/6/pdfs/uksi_20060006_en.pdf (accessed Aug 25, 2018)

[7] See the "methodology" section in Chapter I for the reason of selecting the UK system.

[8] S. Arrowsmith, *The Law of Public and Utilities Procurement: Regulation in the EU and UK Volume 1* (3rd edn., Sweet & Maxwell 2014), pp. 12-13

[9] S. Arrowsmith, "Implementing of the New EC Procurement Directives and the Alcatel Ruling in England and Wales and Northern Ireland: A Review of the New Legislation and Guidance" (2006) 3 *P.P.L.R.* p.90; M. Bowsher, L. E. John, and M. Chambers, "The Use (and abuses) of Framework Agreements in the United Kingdom" in R. H. Garcia (ed.), *International Public Procurement: A Guide to Best Practice* (Globe Law and Business, 2009) p.349

Furthermore, despite the tighter regulation of framework agreements under the *2014 Utilities Directive*, the relevant rules in the public sector are still much more prescriptive than the equivalent in the utilities sector.[10] Thus, this research will mention those issues in the utilities sector where relevant and necessary.

It needs to be noted that in 2016, the UK voted to leave the EU. However, as "Brexit" has not occurred at the time of the research, the research result based on the UK's implementing rules remain unaffected.

3.2 Framework Agreements

3.2.1 *Definition of framework agreements*

In the EU, a framework agreement is defined as "an agreement between one or more contracting authorities and one or more economic operators, the purpose of which is to establish the terms governing contracts to be awarded during a given period, in particular with regard to price and, where appropriate, the

[10] The introduction of separate rules in the utilities sector is due to first, "the different circumstances under which entities operate in Member States", and secondly "the closed nature of the markets in which they operate". The utilities sector are regulated by more flexible procurement rules. However, as mentioned in Chapter III section 3, the provisions on framework agreements under the 2014 Utilities Directive have enhanced transparency requirements than the old provisions. "Public Procurement in the Utilities Sector: Water, Energy, Transport and Postal Services" (April 18, 2016) on European Commission official website, available at https://ec.europa.eu/growth/content/public-procurement-utilities-sector-water-energy-transport-and-postal-services-0_en

quantity envisaged".[11] Apparently, from the definition, a framework agreement is differentiated from a procurement contract, in a similar vein to that under the *Model Law.*[12] A framework agreement itself is established at the first stage, and a procurement contract will only be awarded at the second stage in specific call-offs. What is known as a "framework agreement procedure" under the *Model Law* is classified as an aggregated procurement technique and instrument in the EU.[13]

It is apparent from the definition that single-supplier, multi-supplier, single-user and multi-user frameworks are permitted for use.[14] The definition does not refer to other types of frameworks. The procedural rules, however, make it clear that only closed framework agreements are allowed at the EU level by stating that the second stage procedures for awarding contracts under framework agreements only apply to "…between those contracting authorities clearly identified …and

[11] *The 2014 PSD*, Art 33(1) para.2; *the 2014 UD*, Art.51(1). The definition is essentially reproduced in the *2015 PCR*, reg.33(2) and *the 2016 UCR*, reg. 51(1), according to which a framework agreement is defined as "an agreement or arrangement which establishes the terms in particularly the terms as to price under which an economic operator will enter into one or more contracts with the contracting authority in the period during which the framework agreement applies".

[12] See Chapter II section 2 above.

[13] What is known as a "framework agreement procedure" under the *Model Law* is classified as a procurement technique in the EU. "Framework agreements" and "dynamic purchasing systems" are provided under Chapter titled "Techniques and instruments for electronic and aggregated procurement" in the EU Directives, rather than the "Procedures" Chapter.

[14] "Economic operator" is the term used under the EU directives to denote the supply-side in public procurement. Single-provider and multi-provider framework agreements are used for uniform and simplification purposes.

those economic operators party to the framework agreement as concluded". [15] The closed nature essentially distinguishes framework agreements with dynamic purchasing systems, which are fully open arrangements. The procedural rules further indicate that framework agreements may or may not involve a second-stage competition, both of which are allowed in the EU.

The legal definition itself does not mention whether a framework agreement should be binding on the parties or not.[16] In fact, both binding and non-binding frameworks are allowed. Whether a framework agreement has binding obligations among the parties should depend on the intent of the parties in accordance with the national laws in the Member States.

Notably, a distinction should be made between a framework agreement that is binding on both parties and a procurement contract. As Arrowsmith argues, a binding framework will not automatically convert itself into a procurement contract, thus generating any contractual obligations. The only exception is single-supplier frameworks where all terms and conditions are

[15] *The 2014 PSD*, Art 33(2) para.2; *the 2014 UD*, Art.29(2); the *2015 PCR*, reg.33(5) and the *2016 UCR* reg. 51(4). According to recital 60 of the *2014 PSD,* "…a framework agreement should not be open to entry of new economic operators once it has been concluded…".

[16] European Commission classifies framework agreements under the EU Directives into two types: framework contracts and framework agreements *stricto sensu*. Framework contracts are framework agreements that establish all the terms and are binding on the parties. Framework agreements *stricto sensu* are frameworks that do not establish all the terms and are not binding. See European Commission, "Explanatory Note: Framework Agreements – Classic Directive", CC/2005/03 rev. 1, (July 2005, Brussels)

established in the agreements and when both the purchaser and supplier are committed to buy and sell all the requirements. In this case, no subsequent call-offs are envisaged, with the second stage involving only the execution of the agreement.[17]

3.2.2 *Conditions for Use*

The EU Directives do not provide any condition for the use of framework agreements. The fact that the main provisions on framework agreements are under the title of "techniques and instruments for electronic and aggregated procurement" suggests that repeated procurement is the contemplated circumstance for their use. This, however, does not prevent frameworks being used in other circumstances, and it is possible to use them to respond to urgency procurement.

Contracting authorities are not required to justify the use of framework agreements over other procurement methods or techniques. It follows that they are at full discretion in determining whether to use a framework agreement, which type to use and how to structure it in a given procurement project,

[17] See S. Arrowsmith, fn. 8 *supra*, p.1114 para. 11-14; see also Procurement Lawyers' Association (PLA), *The Use of Framework Agreements in Public Procurement* (March 2012), p.10; The Office of Government Commerce (OGC), "Framework Agreements: OGC Guidance on Framework Agreements in the Procurement Regulations" (September 2008). The OGC Guidance focused on the previous UK regulations that transposed the 2004 EU Directives. However, since the 2014 Directives leave most of the provisions on framework agreements under the 2004 Directives unchanged, the early analysis and commentary on them under the previous Directives can be used for reference.

provided it complies with the EU Directives. Despite the absence of conditions for use at the EU level, Member States may and are encouraged to issue guidance to ensure the appropriate use of framework agreements by contracting authorities. For instance, in the UK, the Crown Commercial Service (CCS) at the central government level, and the regional governments including the Wales Government and Scottish Government all provide guidance on what should go into the decision to use framework agreements.[18]

In the utilities sector, article 51(2) of the 2014 *UD* provides that framework agreements must not be used "improperly or in such as a way to prevent, restrict or distort competition". Recital 61 of the *2014 PSD* provides a similar statement. Instead of conditions that restrict their use, these provisions are more considered as the application of the principles of the Directive in framework agreements, to ensure their appropriate use.

[18] CCS, "Guidance on Framework Agreements" (updated Oct. 2016); Scottish Government, "Scottish Government Guidance on Framework Agreements" SPNN 05/2010, available at http://www.gov.scot/Topics/archive/spdlowlevel/framework (accessed Aug 12, 2018).; Welsh Government, "Framework Agreements: Procurement Advice Note (PAN) for the Welsh Public Sector" (July 2017)

3.2.3 *Main procedures of framework agreements in the EU and UK*

3.2.3.1 The first stage: Concluding a framework agreement

The first-stage procedures for the conclusion of a framework agreement are identical to awarding a procurement contract. All award procedures provided under the Directives are available to conclude a framework. Thus, a contracting authority, in theory, is free to determine whether to solicit submissions through open and restricted tendering, negotiated procedures or competitive dialogue where appropriate. In fact, however, open and restricted tendering are used in many cases, arguably because frameworks are mainly used for standard items, and the use of other procedures is less likely to be justified.[19]

Notably, a framework agreement is caught at the EU level only when the total value of all expected orders under the framework exceeds the prescribed thresholds, irrespective of whether the value of individual orders is below the threshold or not. [20] In a multi-supplier framework, it is necessary to aggregate all contracts that may be awarded by all users within the duration to calculate the totality of the framework.[21]

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[19] Welsh government goes further in that contracting authorities are encouraged to recourse to open procedures as a "default" choice. See Welsh Government, fn. 18, *supra*, p23

[20] The *2014 PSD* Art. 5(5), the *2014 UD* Art. 15(5); the *2015 PCR.* reg.6(8), the *2016 UCR* reg. 17(8)

[21] See OGC, fn. 16 *supra*, p.5 para.3.3-3.4; See PLA, fn. 16 *supra*, pp14-15

A contracting authority starts the procedure with advertising on the *Official Journal of the European Union* (OJEU).[22] It may also publish the advertisement at the national level after the EU-level publication.[23] The solicitation, apart from including the information that is generally required in a contract notice should specifically clarify: (i) the notice leads to a framework agreement; (ii) whether it is a single or multiple-supplier framework agreement, and the maximum number of the suppliers to be admitted in the latter case; (iii) the duration of the framework; (iv) the estimated overall value of all the contracts envisaged under the framework; (v) the identity of all potential contracting authorities that can use the framework; (vi) the award criteria for concluding the framework; (vii) the description of the subject matter; and (viii) the terms and conditions for subsequent contracts to the extent of known.[24] The contents are mostly similar to those required in concluding framework agreements under the UNCITRAL *Model Law*.[25]

The requirement of identifying all users entitled to call off under the framework means that new authorities are prohibited from using the framework once it is concluded. In the context

[22] *The 2014 PSD,* Art 51(2); *the 2014 UD,* Art. 71(2). The Article 48(2) of the 2014 PSD provides that sub-central contracting authorities when adopting restricted procedures and competitive procedures with negotiation could use Prior information notices as a call for competition. The OJEU is available at http://www.ojec.com/ (accessed Aug 26, 2018)
[23] *The 2014 PSD,* Art. 52(2)
[24] *The 2014 PSD,* Annex V Part C; *the 2014 UD,* Annex XI
[25] See section 2 above.

of multi-user frameworks, the identity can be disclosed either by name or "by other means, such as a reference to a given category of contracting authorities within a clearly delimited geographical area so that the contracting authorities concerned can be easily and unequivocally identified".[26]

It would be impossible or unrealistic to calculate the overall value of all future contracts within a period with precision. However, there is a need to provide such an expected value as accurate as possible, and either over-estimate or under-estimate may trigger adverse effects. At one end, under-estimate may circumvent the framework agreement from applying the Directives. At the other end, over-estimate may deter SMEs from participating due to the higher financial qualification requirements.[27] The requirement of disclosing the estimated value as well as the identities of all users, particularly aceturate the importance of effective *ex-ante* planning, because they impact the market response and factually determine the mini-market within the framework.[28] Transparency required at

[26] Recital 60, *the 2014 PSD*.
[27] PLA, fn. 17, *supra* pp.15-16
[28] S. Arrowsmith, fn. 8, *supra*, at p1121. Welsh government highlights the importance of effective planning and early considerations. See "Framework Agreements: Procurement Advice Note (PAN) for the Welsh Public Sector", Welsh Government (July 2017), p.14. It also mentions the significance to provide information as much as possible from the very outset, so that unsuitable suppliers can "deselect themselves as early as possible". Besides, concerns were raised regarding the little attention paid to preparing an intelligent specification in the planning stage. See R. Boyle, "EU Procurement Green Paper on the Modernisation of EU Public Procurement Policy: A Personal Response", (2011) 20 *P.P.L.R.* pp. 171-174.

this stage is also crucial in safeguarding the consistency between two stages. On the other hand, however, such an extensive disclosure can be pro-collusive for allowing the "pie-sharing" among the suppliers and thus facilitating detection of any "cheaters".

Duration, which is determined on a case-by-case basis, is a must-term in the solicitation, to be repeated in the framework agreement itself. A maximum four-year limit is imposed on frameworks in the public sector; in the utilities sector, the maximum limit is extended to eight years, with exceptional extensions allowed where justified.[29] Setting maximum limits is to reduce the anti-competitive risks deriving from excessively long frameworks. Despite that, however, in the UK, the National Audit Office reported that framework agreements used at the central government level were often extended, and the user departments usually continued placing orders under the already-expired frameworks.[30]

Based on the award criteria, the contracting authority selects the supplier(s) to enter into a framework agreement. The agreement itself must articulate the terms governing future contracts as completely as possible, with particular regard to

[29] *The 2014 PSD*, Art. 33(1); *the 2014 UD*, Art. 51(1)
[30] National Audit Office (NAO), "Cabinet Office - Crown Commercial Service. Report by the Comptroller and Auditor General" (HC786, Session 2016-17), p.39

the estimated price and quantity, as highlighted in the legal definition. Most of the terms are established by the contracting authority as disclosed in the solicitation, and the suppliers' submissions supplement some aspects.[31]

In respect of the "price" that should be set out at the first stage, it does not have to be a fixed or precise figure. Given the uncertainty concerning requirements, it is possible for the contracting authority to establish a price mechanism or structure that can determine the exact price for a future contract in a transparent and objective manner.

The contracting authority should promptly notify the suppliers that have submitted tenders of the decision concerning the conclusion of the framework and apply the standstill periods, as is the case in the traditional procurements. [32] Upon request, it should inform the unsuccessful suppliers of the reasons for being rejected.[33] The

[31] There have been discussions about whether price must be established in concluding the framework agreement. Usually, price is considered one fundamental basis of award in any procurement, from a value for money perspective. For more discussion, see S. Arrowsmith, fn. 8 *supra*, pp.1133-1134; M. Bowsher *et al*. fn. 9, *supra*, p.357

[32] *The 2014 PSD,* Art 55(1); *the 2014 UD,* Art. 75(1); the *Remedies Directive* 89/665 Art 2(a); the *Remedies Directive* 92/13/EEC Art. 2(2); *the 2015 PCR,* reg.87 (1); the *2016 UCR,* reg.102(1)

[33] According to *the 2014 PSD*, Art 55(2), procuring entities are to provide to the rejected tenderer of the "characteristics and relative advantages of the tender selected as well as the name of the successful tenderer or the parties to the framework agreement". The European Court of Justice further reinforced the debriefing requirement and requires procuring entities to provide substantial information about the bids of other tenderers. Albano and Nicholas emphasised that the "very extensive disclosure of information on bids" raises a significant risk of collusion in facilitating collusive strategies

UK takes a further step in requiring that the contracting authority should proactively, instead of on request, provide full reasons to rejected tenderers.[34] The conclusion result should also be made to the public.[35]

3.2.3.2 Second-stage: Call-offs

The rules governing the second stage in the public sector are still more prescriptive than those in the utilities sector. Therefore, this section focuses on the second-stage procedures under the public sector rules. The *2014 Utilities Directive* seems to regulate the ordering process through a more principle-based approach, by generally requiring that all contracts should be based on the objective rules and criteria that are disclosed in advance. [36] It further states that the contracting entity is prohibited to "… use framework agreements improperly or in such a way as to prevent, restrict or distort competition."[37] The less detailed provision confers greater flexibility in the use of

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and enforcement. See Albano and Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press, 2016), pp. 232-233

[34] *The 2015 PCR,* reg.86(4); the *2016 UCR,* reg. 101(4)

[35] *The 2014 PSD*, Art. 50(1); *the 2014 UD*, Art. 70(1); *the 2015 PCR*, reg. 50(1); *the 2016 UCR*, reg. 70(1)

[36] *The 2014 UD*, Art. 51(2)

[37] *The 2014 UD,* Art. 51(2) para.3

framework agreements in the utilities sector, taking account of the more commercial-like environment where utilities operate.[38]

Where the framework is awarded a single supplier, contracts must be awarded within the ambit of the pre-established terms.[39] On account of any practical need to cater to specific requirements, the contracting authority may consult and request the supplier party to supplement the original tender when necessary.[40] Such flexibility further allows the contracting authority to improve specific terms, provided that the development will not substantially modify the framework.[41]

Where multiple supplier parties are involved, the second-stage procedures are different between a framework that establishes all terms and conditions with one that does not set out all. In the latter case, call-offs are awarded through reopening a mini-competition among the supplier parties to firstly, refine or finalise the terms that are left incomplete and secondly, to select the supplier for a specific call-off.

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[38] T. Kotsonis, "The 2014 Utilities Directive of the EU: codification, Flexibilisation and Other Misdemeanours" (2014) 4 *P.P.L.R.* p.169; S. Torricelli, "Utilities Procurement", Ch.9 in M. Trybus, R. Caranta and G. Edelstam (eds.), *EU Public Contract Law – Public Procurement and Beyond* (Bruylant, 2014) p.223

[39] *The 2014 PSD*, Art. 33(3); *the 2015 PCR*, reg. 33(7)

[40] *Ibid.*

[41] Since full competition takes place at the first stage of a single supplier framework, any substantial change afterwards will infringe the principles of equal treatment and transparency. The substantial test is articulated under the *2014 PSD,* Art. 72(4), transposed in the *2015 PCR,* reg. 72(8) in the UK.

Where all terms have already been established in the framework agreement itself, call-offs are normally awarded directly based on the original terms and the "objective conditions" pre-disclosed in the procurement document, which include the award criteria for call-offs.[42] However, the *2014 PSD* includes the possibility of reopening competition, even where all terms are established already. Therefore, contracting authorities can choose to award call-offs partly through direct awards and partly through re-opening competition, provided such choice should be based on objective criteria, which should be specified in the procurement document.[43] Such a "hybrid" option is envisaged for improvement or adjustment of the terms to reflect specific requirements, such as the large orders with high value or involving a large quantity.[44] Such flexibility is more needed in centralised framework agreements where the needs of different users may vary.[45]

Where a framework agreement is incomplete, a second-stage competition would be reopened among the supplier

[42] *The 2014 PSD,* Art 33(4). It is not clear whether the call-offs should be awarded by applying the general award criteria, namely the Most Economically Advantageous Tender under Article 67. For more discussion on this respect, see S. Arrowsmith, fn. 8, *supra*, pp.1141-1146
[43] *The 2014 PSD,* Art 33(4) and *2015 PCR,* reg. 33(8)(b). According to recital 61 of the 2014 PSD, the objective criteria can relate to the quantity, value or characteristics of the subject matter.
[44] See Albano and Nicholas, fn. 33 *supra* p.97
[45] C. R. Hamer, "Regular Purchases and Aggregated Procurement: The Changes in the New Public Procurement Directive Regarding Framework Agreements, Dynamic Purchasing Systems and Central Purchasing Bodies", (2014) 4 *P.P.L.R*., p.204 note 22

parties for awarding contracts. For each contract, the contracting authority is not obliged to reach every supplier party. Instead, it can limit the invitations to those "that are capable of performing the call-off" only, indicating the specific requirement and the time-limit for re-submissions.[46] However, the *2014 Public Sector Directive* is silent on what "capable" means and provides few "checks and balances" on how the "capable" selection and invitation should be implemented in practice.[47]

The second-stage competition should be based on the original terms established at the first stage, and more precisely formulated terms, and "…where appropriate, other terms referred to in the procurement documents…". It is submitted that the possibility to consider "other terms", again, may leave a transparency "loophole".

Regarding the award criteria used in call-offs, they need not necessarily be the same with those for concluding the framework agreement. However, as Arrowsmith submits, there should be significant correlations between them, with a view of ensuring consistency between two stages.[48]

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[46] *The 2014 PSD,* Art 33(5) and *2015 PCR,* reg.33(11)(a). It needs to be noted that the *2014 Model Law* "borrowed" the rule of inviting "capable" suppliers capable under its Article 62(4).

[47] As Arrowsmith submitted, the "capability" here refers more to the eligibility to deliver a specific order, rather than the basic qualification for admission to the framework. See S. Arrowsmith, fn. 8, *supra*, pp. 1166-1168

[48] *Ibid.,* p1162

The 2014 Public Sector Directive provides no obligation on contracting authorities to notify the non-inviting supplier parties of the second-stage competitions. The lack of communication may allow contracting authorities to favour certain specific suppliers and exclude others who are considered "incapable" for the call-off at issue and not invited but in fact, may submit better offers. More importantly, the lack of transparency may in fact deprive the excluded suppliers of the opportunity to challenge of the deselection decision.[49]

Furthermore, award notices are not required being issued after a contract is awarded under a framework agreement.[50] On the one hand, requiring individual award notices for each call-off may impede the efficiency of the call-off process. However, it is equally imperative to ensure certain extent of transparency at this stage; otherwise the potential improper use is more likely.[51] The EU Directives provide the Member States with the option, rather than the obligation as in the case of dynamic

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[49] M. Andrecka, "Framework Agreements: Transparency in the Call-off Award Process", presented in the *Public Procurement: Global Revolution VII* (Nottingham June 2015)

[50] Furthermore, the Art.50(2)1of the *2014 PSD* and Art.70(2)1of the *2014 UD* explicitly provide that contracting authorities "shall not be bound to send a notice of the results of the procurement procedure for each contract based on that agreement".

[51] A. S. Graells, "What Level of Transparency for Award/Call-off Decisions Within Framework Agreements?" blog post on 19 June 2015 available at http://howtocrackanut.blogspot.co.uk/2015/06/what-level-of-transparency-for.html (accessed Aug 3, 2018). Albert considers the publication of the procurement results is the main instrument for transparency.

purchasing systems, to require quarterly publication of grouped award notices for call-offs under frameworks.

The UK chose not to include that requirement.[52] However, it takes a step further and introduces enhanced information obligation on contracting authorities in call-offs. In the public sector, the UK *2015 PCR* additionally requires publication of award notices regarding contracts awarded based on framework agreements, individually valued above and below the EU threshold, on the domestic platform-*Contracts Finder.*[53] The information includes the name of the contractor, the date on which the contract is awarded and the value of the contract [54]

In the utilities sector, as explained at the outset of the section, the relevant provisions do not distinguish frameworks that establish full terms and those that do not. All contracts should be awarded "on the basis of objective rules and criteria" that have been set out in the procurement document.[55] While all the options provided under *the 2014 PSD* are available in the

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[52] *The 2015 PCR*, reg.50(4)
[53] *The 2015 PCR,* reg.108(1)(b) and 112. *Contracts Finder* is available at https://www.contractsfinder.service.gov.uk/Search (accessed Aug 15, 2018). The reg. 108(1)(b) states that the obligation of publishing award notices applies where a contracting authority "…awards a contract based on a framework agreement", which literally covers all call-offs under framework agreements, no matter how small the value of an individual call-off is. However, it is argued by Arrowsmith and Smith that the full coverage of all call-offs "was not intended". For more discussion, see S. Arrowsmith, "The "Lord Young" Reforms on Transparency of Information and Selection of Firms to Be Invited to Tender Under the Public Contracts Regulations 2015: A Practical Analysis of The Legal Provisions", (2018) 2 *P.P.L.R.* 75-95
[54] *The 2015 PCR,* regs.108(1)(b), 112
[55] *The 2014 UD*, Art. 51(2)(1)

utilities sector, additional flexibility is permitted here, provided the general principles of the *Directives* be followed. For instance, negotiations between the contracting authority with the supplier parties are allowed in call-offs.

3.2.4 *Monitoring and Review Procedures*

In both the public and utilities sectors, the first stage of framework agreements is subject to full review and remedies measures, including the award notification and standstill period, just like other traditional procurements.[56] In respect of the review measures at the call-off stage, their application is greatly "relaxed".

In theory, the second stage of frameworks should be covered by the remedy mechanism, as procurement contracts are awarded at this stage. Despite the *de jure* availability, the transparency flaw at this stage arguably makes the remedies meaningless and ineffective. As explained above, an aggrieved supplier may not challenge the decision being excluded from the second-stage competition simply because contracting authorities are not obligated to inform them so. Similarly, a disappointed supplier is unlikely to challenge the award of a

[56] A framework agreement must not be concluded until the standstill period has elapsed after the contracting authority has notified the award. See the Directive 89/665 Art.2(a) and Directive 92/13 Art. 2(a), transposed in the UK under the *2015 PCR,* reg. 85-87 and the *2016 UCR,* reg.100-102

contract timely and to seek pre-award remedies, as standstill period and award notices can be exempt regarding the contracts based on frameworks.

Under Article 2b(c) of the *Directive 2007/66/EC*[57], Member States are permitted to derogate from the application of standstill periods for awarding contracts based on framework agreements. The derogation possibility reflects the EU's tilt towards efficiency, as applying standstill period for each call-off may be unnecessarily burdensome and disruptive.[58]

Where the derogation of standstill periods is involved, Member States should provide the remedy of ineffectiveness for the contracts awarded, which only applies where the contract is above the EU threshold and there is any breach of the procedural rules in reopening competition.[59] It means, a contract is at the risk of being declared ineffective if it exceeds the EU threshold and is awarded through reopening competition, unless award notices and standstill periods have been applied.

It also follows that both the "ineffectiveness" remedy and the standstill period are exempted in call-offs based on direct awards. The "waived" remedies, together with the lack of

[57] *Directive 2007/66/EC of the European Parliament and of the Council of 11 December 2007 amending Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness procedures concerning the award of public contracts* [2007] OJ L335/31 (Directive 2007/66)
[58] S. Arrowsmith, fn. 8, *supra*, pp. 1367, 1155-1156
[59] *Directive 2007/66*, Art. 2b(c)

transparency as identified earlier, may particularly mire the call-off stage into a "blackhole", which operates "below the radar".

The UK has opted for the derogation approach, as a result of which contracting authorities are under no obligations to notify and wait for the expiration of the standstill period before awarding a call-off based on a framework, with or without the second-stage competition involved.[60] However, the Crown Commercial Service (CCS) has strongly suggested the contracting authorities to apply the standstill period voluntarily,[61] because the standstill period serves not only as a sword for aggrieved suppliers, but also a "shield for a contracting authority from potential ineffectiveness claims."[62]

Furthermore, the UK regulations, taking a further step than the EU Directive, deals specifically with the effect of the "ineffectiveness" of a framework agreement itself on the contracts awarded under it. In both the public and utilities sectors, a declaration of ineffectiveness of the framework agreement does not automatically lead to the "ineffectiveness" of the contracts awarded based on it.[63]

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[60] *The 2015 PCR,* reg.86(5), the *2016 UCR,* reg.101(5)
[61] CCS, "Guidance on the Standstill Period", p5 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/417945/Guidance_on_Standstill.pdf (accessed Aug 27, 2018)
[62] OGC, "Implementation of the Remedies Directive: OGC Guidance on the 2009 Amending Regulations", para.7 p.4, available at http://webarchive.nationalarchives.gov.uk/20110601212617/http:/ogc.gov.uk/documents/Remedies_Guidance_Part_2_Standstill_Rules%282%29.pdf (accessed Aug 27, 2018).
[63] *The 2015 PCR,* reg.103(2), t*he 2016 UCR,* reg.118(2)

Given the above, there are uneven transparency and inadequate remedies in the second stage of framework agreements in the EU, which deficiencies arguably provide fertile grounds for improper use of such arrangements. More robust transparency and strengthened oversight are needed to ensure their beneficial use.

3.3 Dynamic Purchasing Systems

3.3.1 *Characterising dynamic purchasing system*

The 2014 Directives do not provide a unitary legal definition for dynamic purchasing systems (DPS) but describe the general feathers of such procurement technique.[64] Basically, DPS are an electronic procurement system "for contracts for works, services and goods commonly available on the market"; they are available in the both public and utilities sectors.[65] They should be maintained open throughout their validity period and allow new qualified suppliers to join at any time. They are

[64] *The 2014 PSD,* Art. 34(1), *the 2014 UD,* Art. 52(1); transposed into *the 2015 PCR* reg. 34*, the 2016 UCR* reg.52. Different from frameworks, which had already been used before the introduction of formal rules, dynamic purchasing systems were firstly introduced in the 2004 EU Directives given the development of electronic development and without reflecting any de facto practices. For more about the introduction process, see European Commission, "Communication on Public Procurement in the European Union" (Brussels, March 11, 1998) COM (98) 143.

[65] CCS, "Guidance on Dynamic Purchasing System", (updated Oct. 2016), available at https://www.gov.uk/guidance/transposing-eu-procurement-directives (accessed Aug 29, 2018).

designed to expedite the procurement process and mitigate the administrative burden of recurrent purchases.[66]

As a novel procurement tool, DPS resemble framework agreements, especially those operated on an electronic basis in many aspects. For instance, both comprise two stages of operation. The primary rationale of both is to streamline the process for improving administrative efficiency.

On the other hand, DPS are different from frameworks in several aspects. For instance, they should be operated on a fully electronic process. Each DPS is kept open to new suppliers during its lifetime, whereas framework agreements in the EU are intrinsically "closed" after the conclusion. Moreover, under DPS, the first stage is not "competitive", and the second-stage competition is necessarily involved for all the contracts to be awarded. By contrast, in framework agreements, the first stage competition is usually substantive, which involves eliminating suppliers, and the second-stage may or may not take place for the award of subsequent contracts. DPS are largely analogous to open framework agreements under the *Model Law*.[67]

[66] *The 2014 PSD,* recital 63; A. S. Graells, *Public Procurement and the EU Competition Rules* (2nd edn., Hart, Oxford, 2015), p.363
[67] See Chapter III section 2 and Chapter II section 3 above.

3.3.2 *The operational procedures of dynamic purchasing systems*

The 2004 EU Directives provided "flawed and unnecessarily onerous procedural rules" on DPS, so they had been rarely used in practice.[68] The 2014 Directives significantly simplify the procedural rules, with a view of increasing their uptake.[69] In fact, the transformative changes are submitted to make DPS much more usable, which are gradually becoming popular.[70]

DPS involve two stages of operations: an on-going process for assessing and accepting qualified suppliers to the system and awarding subsequent contracts through the second-stage competition among the supplier parties.

3.3.2.1 The first stage procedure

Under the current procurement rules, a contracting authority should follow the rules of the restricted procedure in all its phases from establishing a DPS up to awarding the contracts

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[68] "United Kingdom response to the European Commission Green Paper on the Modernisation of EU Public Procurement Policy" (COM (2011) 15 final), p.9, available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/61554/0707UKGPpbResponsefinal_20_2_.pdf (accessed Aug 29, 2018). For more discussion about the inflexibility of using DPS under the old rules, see S. Arrowsmith, "Modernising the EU's Public Procurement Regime: A Blueprint for Real Simplicity and Flexibility" (2012) 21 *P.P.L.R.* 71–82; C. R. Hamer, fn. 45, *supra*, p. 206

[69] European Parliament Committee on the Internal Market and Consumer Protection, *Cluster 6 "Aggregation of demand" Council document* 6907/12 of February 28, 2015, p.5

[70] Ama Eyo, "Evidence on Use of Dynamic Purchasing System in the United Kingdom", (2017) 6 *P.P.L.R*. p. 237

based on it.[71] It should start the first stage with publishing a call for competition in OJEU. The solicitation should clarify that a DPS is involved, the award criteria for awarding the subsequent contracts, the nature of the requirements and the estimated quantities of purchases, and other necessary information concerning how the DPS operates.[72] Any division into categories of items should be indicated, along with the characteristics defining them. The characteristics used to define a category may include the size of the subsequent contracts or geographical area of the contract delivery.[73] The procurement documents should be fully accessible throughout the DPS.[74]

At least thirty days must be allowed for suppliers to respond to the solicitation for setting up the DPS.[75] The solicitation should be standing to allow new suppliers to join at any time during the validity. Upon receipt of requests, the contracting authority should evaluate and make admission decisions within a maximum of 10 working days subject to a justified extension to 15 working days.[76] All suppliers who satisfy the selection

[71] *The 2014 PSD,* Art 34(2), *the 2014 UD,* Art. 52(2), transposed in *the 2015 PCR,* reg. 34(5) and *the 2016 UCR* reg. 52(5)
[72] *The 2014 PSD,* Art 34(4)(6), *the 2014 UD,* Art. 52(4)(6)
[73] *The 2014 PSD,* Art 34(1)(4), *the 2014 UD,* Art. 52(1)(4)
[74] *The 2014 PSD*, Art 34(4), *the 2014 UD,* Art. 52(4)
[75] *The 2014 PSD*, Art 34(2), *the 2014 UD*, Art. 52(2)
[76] *Ibid.*

criteria must be admitted to the DPS, and no limit can be imposed on the number of suppliers.[77]

The EU Directives provide no restriction on the duration of DPS, because the "open" nature reduces the risks to competition and transparency.[78] No notices are required regarding the establishment of a DPS itself or the admission of each new supplier party.

3.3.2.2 The second stage procedure

The ordering procedures are the centre of simplification regarding DPS under the 2014 Directives. Where a specific requirement arises, the contracting authority should invite all the suppliers admitted to the DPS or those admitted to the relevant category divided if any.[79] The electronic process enables the invitation being issued to all the suppliers simultaneously at negligible cost. The award of a contract is based on the award criteria pre-disclosed in the solicitation document. The criteria may be more precisely formulated in the invitation to tender for the specific contract.[80]

It needs to be particularly noted that award notices are compulsory for the awards of contracts under DPS. Contracting

[77] *The 2014 PSD*, Art 34(5), *the 2014 UD*, Art. 52(5)
[78] See A. S. Graells, fn. 66, *supra*, pp.365-366
[79] *The 2014 PSD*, Art 34(6), *the 2014 UD*, Art. 52(6)
[80] *Ibid.*

authorities can choose to issue separate award notices after each contract is made or to publish quarterly grouped notices.[81] This bifurcated approach with the possibility of periodic publicity, as submitted by Arrowsmith, is a "useful compromise between the need to make information available and the need to avoid undue administrative burde". [82] In the UK, contracting authorities should further follow the publication requirements at the national level on *Contracts Finder*.[83]

It is puzzling that the award notices are not required in call-offs under framework agreements but are compulsory in DPS at the EU level, while "closed" frameworks arguably pose higher risks to competition. It would make more sense to align the transparency requirements for frameworks with those for DPS.[84]

3.3.3 *Monitoring and Review Procedures*

In principle, both stages of DPS are covered by the remedy mechanism.[85] However, given the structural particularity, the

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[81] *The 2014 PSD*, Art 50(3); *the 2015 PCR*, reg.50(5), (6)
[82] See S. Arrowsmith, fn. 8, *supra*, p196
[83] CCS, "Guidance on Dynamic Purchasing System", (updated Oct. 2016), p.4
[84] See S. Arrowsmith, fn. 8, *supra*, p1371; see also A. S. Graells, "Contract award notices under Reg. 50 Public Contracts Regulations 2015" blog post on 7 May 2015, http://www.howtocrackanut.com/blog/2015/05/contract-award-notices-under-reg-50.html (accessed Sep 2, 2018).
[85] According to *Directive 2007/66* Art.1, "Contracts within the meaning of this Directive include public contracts, framework agreements, public works concessions and dynamic purchasing systems".

application of review measures in DPS is different from that in other traditional procurements.

Regarding the first stage, applying a standstill period is not necessary and makes no sense, because there are not award notices regarding the conclusion of the DPS.[86] Therefore, no challenges are envisaged against the setup of the DPS. However, a supplier may challenge any inappropriateness regarding the solicitation or other procurement documents. An unsuccessful supplier may also challenge the decision of itself being rejected for entering the system. Given the absence of award notices, a supplier is less likely to challenge an abusive decision by the contracting authority on the admission of other suppliers.

Regarding the second stage, Member States may choose to derogate from the applying standstill periods for the contracts based on a DPS, while imposing the remedy of ineffectiveness instead, as in the case of framework agreements.[87] The UK has opted for the derogation approach.[88] Similarly, for above-threshold contracts, it is advisable for contracting authorities to voluntarily observe the standstill period before awarding a contract, to de-risk the contract being declared ineffective.[89]

[86] CCS, fn. 82, *supra*, p.7
[87] *The Directive 2007/66,* Art. 2b(c)
[88] *The 2015 PCR,* reg.86(5)(c), *the 2016 UCR*, reg.101(5)(c)
[89] The Directive 2007/66, Art. 2d (5)

3.4 Qualification Systems

Qualification systems are permitted in the utilities sector only and are mainly regulated under article 77 of the *2014 Utilities Directive*.[90] A legal definition of qualification systems is not provided under the Directive. They are often known as "supplier lists" in other procurement systems.[91] Basically, a qualification system is used to establish a list of suppliers who are assessed qualified for various types of works, supplies or services. They are operated in two stages: at the first stage, the contracting authority registers the suppliers who are assessed qualified based on pre-established rules and criteria; when a requirement arises, the contracting authority advertises within the system

[90] In the public sector, article 64 of the 2014 PSD (transposed in reg. 64 of the *2015 PCR* in the UK) recognises and permits the use of official lists of approved economic operators/suppliers and certification by certification bodies to facilitate the qualification assessment of suppliers. The logic of official lists is to reduce administrative costs and simplify the documentary requirements involved in tendering procedures. The purpose of official lists is to allow economic operator from other Member States to use lists as proof of their suitability in said Member State, therefore to prevent unjustified exclusions of suppliers that may derive from "improper" documentary formality or proof produced in other Member States. Official lists are distinguished from the qualification systems, because, first, they are managed and operated by assigned bodies instead of contracting authorities. Therefore, official lists are less likely serving as the full qualitative selection towards a particular procurement (including a framework agreement by a contracting authority). Moreover, the participation/ registration of economic operators is optional and subject to "or the equivalent test". Thus, they cannot be excluded for non-registration on a particular list if they have certificate to prove their qualification requirements. For more discussion and analysis about "official lists", see S. Arrowsmith, fn. 8 *supra*, pp. 1305-1319.

[91] For more discussion about supplier lists, see S. Arrowsmith, "Framework Purchasing and Qualification Lists under the European Procurement Directives: Part I" (1999) 3 *P.P.L.R.* 115

and invites amongst the registered suppliers to present tenders or to negotiate on the contracts.[92]

Each qualification system is an open process, as is the case of DPS. Thus, new suppliers can request to be registered at any time.[93] Qualification systems in the EU utilities sector can be classified as "mandatory supplier lists", by which only the registered suppliers have access to the future contracts.[94]

The contracting authority should establish criteria and rules to assess the qualifications of suppliers that request to enter into the qualification system. The "criteria and rules" may include the criteria for exclusion and selection of suppliers for qualification under the 2014 PSD or technical specifications.[95] Thus, the potential ambit of the first-stage assessment in qualification systems can be wide. At one end, only interest and the suitability of a supplier, i.e. financial capacity, will be reviewed. At the other end, it is also possible for assessment of the supplier's capacity of fulfilling the technical specifications requested for specific contracts. Where the first-stage assessment concerns substantive aspects of future contracts, it is possible, though not necessarily, to involve the reduction of the number of "qualified" suppliers.

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[92] *The 2014 UD,* Art.77, transposed in *the 2016 UCR,* reg. 77 in the UK
[93] *Ibid.*
[94] *The 2014 UD,* Art.77(5), 44(4); *the 2016 UCR,* reg. 77(9)
[95] *The 2014 UD,* Art.77(2)

Qualification systems are not permitted in the public sector due to their elevated risks to competition.[96] For instance, suppliers will be excluded from the procurement relevant simply because they are not registered, even if they are proved more competitive and qualified, such as SMEs, new firms and foreign suppliers. Concerns may also be raised regarding the abuse of qualification systems by contracting authorities to favour specific suppliers or to avoid full transparency and competition requirements.

Nevertheless, the "open" nature of qualification systems with permanent solicitation and entrance can mitigate the anti-competitive effects.[97] The suppliers with interest can request to enter at any time, like in DPS. In fact, qualification systems share many similarities with DPS, such as being kept open and the solicitation being standing. Some practitioners call DPS as electronic qualification systems.[98]

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[96] Supplier lists are not provided under the *Model Law* for identical considerations. However, they are available under the *WTO Agreement on Government Procurement*, Article IX, text available at https://www.wto.org/english/docs_e/legal_e/rev-gpr-94_01_e.htm (accessed Sep 2, 2018)

[97] The experience of mandating qualification systems open in the EU may be drawn on in mitigating the competitive concerns in the use of supplier lists in other procurement systems, i.e. in the procurement of Chinese SOEs, as explored in Chapter VI and VII.

[98] See CMS, "Guide to the EU Laws Governing Utilities Procurement in the UK" (Oct. 2014) p.8 available at https://cms.law/en/GBR/Publication/Guide-to-the-EU-public-procurement-rules-in-the-UK (accessed Sep 4, 2018). It is considered that DPS are a "halfway house" between framework agreements and qualification systems. As open arrangements, they differ from closed frameworks. Meanwhile, they go beyond qualification systems in most cases as DPS usually envisage more specific scope of future contracts and involve

Qualification systems are also valuable in streamlining the procurement process and driving up efficiency by reducing administrative costs and lead-time for both suppliers and purchasers. They may also assist contracting authorities in developing a close relationship with the preferred suppliers with for the benefit of improved quality and contract performance.[99] In light of the benefits, it makes sense to allow qualification systems being used in the public sector, as early suggested by Arrowsmith.[100]

screening qualifications for the identified requirements. Under the new Directives, DPS tend to move towards qualification systems, as no responsive tenders are required for entrance.

[99] For more analysis about the benefits of supplier lists, see S. Arrowsmith, *Government Procurement in the WTO* (London: Kluwer Law International, 2003), pp.232-234; S. Arrowsmith, J. Linarelli and D. Wallace, *Regulating Public Procurement, National and International Perspectives* (Kluwer Law International, 2000), pp. 639-645

[100] S. Arrowsmith, "Framework Purchasing and Qualification Lists under the European Procurement Directives: Part I" (1999) 3 *P.P.L.R.* 115, p.116; See also Arrowsmith, fn. 8, *supra*, p.71

4 Indefinite Delivery/Indefinite Quantity Contracts in the US Federal System

"Indefinite-Delivery/ indefinite-Quantity contracts" (IDIQ) contracts have played an important role in federal procurement for long and continue being widely used.[1] They enable the government to benefit from the streamlined ordering process, short lead-time, better scheduling, improved administrative efficiency, cost savings and the possibility of using more current technologies.[2]

4.1 A Brief History of IDIQ Contracts

The history of IDIQ contracts can be traced back to the 1950s when the General Services Administration launched the program of Federal Supply Schedule (FSS), known as GSA

[1] Task-order and delivery-order contracts mean "contracts for supplies or services respectively that do not require a firm quantity of supplies and services and that provide for the issuance of orders for the delivery of supplies or the performance of tasks during the validity". See *Federal Acquisition Regulation* (*FAR*) Subpart 16.501-1. For simplicity, the term "task order" is used hereinafter to refer to both supplies and services. This thesis focuses on the procurement system at the federal level, while the rules for government in states vary greatly by their jurisdictions.

[2] U.S. Office of Management & Budget (OMB), Office of Federal Procurement Policy (OFPP), "Best Practices for Multiple Task and Delivery Contracting", (Washington, D.C., July 1997, last updated in Feb, 1999), available at https://www.gsa.gov/portal/getMediaData?mediaId=155590 (accessed Aug 2, 2018)

Schedules today, as a simplified mechanism for acquiring office supplies, and other common-use items for federal agencies.[3]

Until the early 1990s, IDIQ contracts were regularly used in federal procurement, whereas their legality remained unsettled. The concerns arising from lack of guidance and inadequate oversight were raised and led the clamour for statutory regulation on such contracting vehicle.[4]

In 1994, the *Federal Acquisition Streamlining Act* (FASA)[5] explicitly authorised the IDIQ contracts and established "parameters under which IDIQ contracts could be formed and administered". It further establishes a statutory preference for multiple award contracts (similar to multi-supplier framework agreements).[6] Moreover, the FASA allows for a signification relaxation of competition and transparency requirements for small orders based on IDIQs to expand the use of this streamlined vehicle, with a view to facilitating commercial-liking

[3] For more information about the history of task order contracting, see D. Gordon and J. Kang, "Task-order Contracting in the US Federal System: The Current System and its Historical Context", Ch. 5 in S. Arrowsmith (ed.), *Public Procurement Regulation in the 21st Century: Reform of the UNCITRAL Model Law on Procurement* (Eagan, MN: West, 2010)

[4] P. Ritenberg, "Task-Order Contracts: Popular but Are They Legal?", 22 NAT'L CONT. MGMT. J. 33 (Summer 1988); J. A. Howell, "Governmentwide Agency Contracts: Vehicle Overcrowding on the Procurement Highway" (1998) 27 PUB. CONT. L.J. p.395

[5] *Public Law* No. 103-355, 108 Stat. 3249 and 3250.

[6] K. J. Wilkinson, "More Effective Federal Procurement Response to Disasters: Maximizing the Extraordinary Flexibilities of IDIQ Contracting", (2007) 59 *Air Force Law Review Volume*, p.259

purchases and promoting administrative efficiency.[7] To that end, task orders under IDIQs are exempt from protests under the *FASA*, subject to limited exceptions.

As a result of the *FASA* reform, the use of IDIQs grew markedly since then. In 1996, the *Clinger-Cohen Act* further introduced Government Wide Acquisition Contracts (GWACs) to simplify and facilitate access to IT items.[8] On the other hand, however, the "relaxed" procedures, combined with the protest ban created opportunities for unfettered discretion. Federal agencies were observed to have abused IDIQ contracts, which caused strong criticism from the practitioners and academia.[9]

To address the problems, FASA has been amended several times since then to ensure the appropriate use of IDIQs. The Congress enacted the *National Defence Authorization Act for Fiscal Year 2000*, by which all the suppliers under an IDIQ should be given a "fair opportunity" being considered for future task orders.[10] Subsequently, enhanced transparency and

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[7] S. L. Schooner, D.I. Gordan and J.L. Clark, "Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations", GWU Law School Public Research Paper (2008).

[8] GWACs are IDIQ contracts established by an agency pursuant to the *Clinger-Cohen Act* and open for use by all federal agencies with an administrative fee.

[9] For instance, see U.S. GAO, "Civilian Agency Compliance with Task and Delivery Order Contracts", GAO-03-983 (2003); T. F. Burke and S. C. Dees, "Feature Comment: The Impact of Multiple-Award Contracts on the Underlying Values of the Federal Procurement System", (2002) 44 GOV'T CONT. 431

[10] *National Defense Authorization Act for Fiscal Year 2000*, Public Law, No.106-65, 113 Stat.704

competition requirements regarding task orders under IDIQs were imposed in both defense and civilian procurement.[11]

Apart from the above, efforts have also been devoted to enhancing accountability in IDIQs. In 2008, the *National Defense Authorization Act for Fiscal Year 2008* "temporarily" restored part of the jurisdiction taken away from Government Accountability Office (GAO) by FASA, authorising protests on orders in excess of USD 10 million.[12] In 2012, GAO gained such permanent authority over defense task orders.[13] In civilian procurement, in contrast, GAO obtained permanent jurisdiction over protests on task orders (exceeding USD 10 million) in 2016, through *GAO Civilian Task and Delivery Order Protest Authority Act* of 2016.[14] One caveat is that the "protest ban" regarding task orders based on IDIQs does not apply in GSA Schedules, and task orders against which of any value can be protested.[15]

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[11] *National Defense Authorization Act for Fiscal Year 2002*, Public Law, No.107-107, 115 Stat.1012; *National Defense Authorization Act for Fiscal Year 2009*, Public Law No. 110-417, 122, Stat. 4548.

[12] *National Defense Authorization Act for Fiscal Year 2008*, Public Law No. 110-181, 122, §843. The legislation has a sunset provision and the authority would expire after three years.

[13] *GAO Civilian Task and Delivery Order Protest Authority Act of 2016,* available at https://www.congress.gov/114/crpt/hrpt779/CRPT-114hrpt779.pdf (accessed Aug 4, 2018). The threshold was amended, increasing from USD 10 to 25 million under the *National Defense Authorization Act for Fiscal Year* 2013, Public Law No. 112-239, 126 Stat.1842.

[14] *Public Law* No: 114-260 (12/14/2016)

[15] GAO is entitled to hear such protests. Court of Federal Claims confirmed the non-application of the protest ban on GSA Schedules. See *Labat-Anderson Inc. v. United States,* 50 Fed. CI. 99, 102 (Fed.C1.2001); Group Seven Associates. LLC v. United States. COFC No. 05-867C (Oct. 13,2005); *Idea International, Inc. v. United States*, 74 Fed. Cl. 129 (2006). *Data Management Services Joint Venture v. the United States*, No.07-597C (September 24, 2007)

4.2 The Relevant Definitions

IDIQs are governed under Subpart 16.5 of the *Federal Acquisition Regulation* (FAR). An IDIQ is a contract that "provides for an indefinite quantity, within stated limited, of supplies or services during a fixed period of time".

As explained earlier, in the EU and under the *Model Law*, a "framework agreement" itself is distinguished from a procurement contract. By contrary, an IDIQ, as the definition reveals, is a contract *per se* in the US federal procurement, binding on both parties. Within an IDIQ, the purchaser is committed to buying at least a guaranteed minimum quantity of goods or services and the supplier should furnish accordingly, up to a specified maximum quantity.[16] Once the purchaser reaches the minimum quantity, it has fulfilled the obligation and is free to decide whether to continue ordering under the IDIQ. As for the supplier, it is only obligated to supply within the maximum quantity.[17]

An IDIQ can involve single or multiple suppliers, like framework agreements in the EU and under the *Model Law*.

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[16] *FAR* 16.504(a)(1). To make the contract binding, the minimum should be more than "nominal". See J. Cibinic, R. C. Nash, and C. R. Yukins (eds.), *Formation of Government Contracts* (4th edn., Wolters Kluwer, 2011), pp.1387-1389.
[17] *FAR* 16.504(a)(1)

However, as already mentioned, there is a statutory preference for multiple awards in the US to enhance competition in awarding task orders.[18] Therefore, multi-award IDIQs (multi-supplier framework agreements) have become the norm of such arrangements, and single-supplier IDIQs are only allowed in limited circumstances with justification.[19]

IDIQ contracts have been used for decades, during which process they have evolved into several variants for centralised and joint procurements. The most common include the GSA Schedules, Governmentwide Acquisition Contracts (GWACs) and Multi-Agency Contracts (MACs).

GSA Schedules programme, interchangeably referred to as Federal Supply Schedule (FSS) and Multiple Award Schedules (MAS), was originally created for simple purchases of furniture and supplies. Now it is "one of the largest and most preferred for commercial products and services".[20] It offers easy access to a wide variety of common-use items from pre-selected qualified suppliers through "schedules" at volume discount prices.[21] The use of the GSA Schedules was compulsory for all

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[18] *FAR* 16.504(c)
[19] *Ibid.*
[20] Quoted from the GSA official website at https://www.gsa.gov/acquisition/new-to-gsa-acquisitions/how-to-sell-to-the-government/how-gsa-buys-schedules-and-contracts (accessed Aug 28, 2018)
[21] *FAR* 8.402(a). For a general overview of and more information about the GSA Schedules, see https://www.gsa.gov/portal/content/197989 (accessed Aug 28, 2018)

federal agencies, whilst the situation was changed after the 1990s.[22]

GWACs, are prepositioned multiple-award IDIQs for IT purchases and are available to all federal agencies.[23] Each GWAC is operated by an executive agent designated by the Office of Management and Budget (OMB).

MACs are also essentially IDIQs for the use of multiple federal agencies, similar to GWACs.[24] The agency that sets up a MAC or a GWAC can charge other user agencies a commission fee for using the contract. The main differences between them include firstly GWACs should be set up by GSA- authorised agencies, and there is no such restriction in MACs. Secondly, MACs are not necessarily for IT purchases. Thirdly, the *Economy Act* applies to issuance of task orders under MACs, but not under GWACs.[25]

The GSA Schedules, GWACs and MACs are referred to as interagency contracting.[26] They are akin to multi-user and

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[22] D. I. Gordon and G.M. Racca, "Integrity challenges in the EU and U.S. procurement systems", Ch.1 in G.M. Racca and C. R. Yukins (eds.), *Integrity and Efficiency in Sustainable Public Contracts – Balancing Corruption Concerns in Public Procurement Internationally* (Bruylant, 2014), p. 137

[23] *FAR* 2.101. For more information about GWACs, see https://www.gsa.gov/portal/category/101711 (accessed Aug 28, 2018)

[24] *Ibid*. Multi-agency contract means "a task-order or delivery-order contract established by one agency for use by Government agencies to obtain supplies and services, consistent with the *Economy Act*."

[25] *FAR* 17.5

[26] According to *FAR* 2.101, "interagency acquisition" means "a procedure by which an agency needing supplies or services (the requesting agency) obtains them from another agency (the servicing agency), by an assisted acquisition or a direct acquisition".

multi-supplier framework agreements, as per the classification in Chapter II. These vehicles allow user agencies to leverage the specialised expertise of others and to benefit from greater efficiency and cost-savings. On the other hand, however, there are always concerns regarding the abuse and overuse of interagency contracts, mainly due to the lack of oversight and accountability.[27] Government Audit Office (GAO) has identified them as a governmentwide "high-risk area".[28]

4.3 Operational Procedures of an IDIQ Contract

4.3.1 *The first stage procedures*

The first stage of an IDIQ follows the general procedures applicable to any other procurement. The *FAR* does not define the specific conditions for the use of IDIQs, but broadly describes the circumstances where they are most often used. Generally, IDIQs may be used "…to acquire goods and/or services when exact times and/or exact quantities of future deliveries are not known at the time of contract award".[29] In practice, IDIQs are mainly used (i) in repeated purchases of

[27] J. Cibinic *et al*., fn. 16, *supra*, p.1121
[28] GAO, "High-Risk Series Update", GAO-05-207 (January 2005)
[29] *FAR* 16.501-2(a)

common-use products and services in a longer timescale; and (ii) to respond to emergency acquisitions as prearrangement.[30]

Multiple awards IDIQs should be the "default" option, due to the statutory preference established by the *FASA*, as explained earlier. The decision of whether multiple awards are appropriate must be part of the procurement planning.[31] The *FAR* further outlines the factors the contracting officer should consider when determining the appropriate number of contract to be awarded, including: the scope and complexity of the requirement, the expected duration and frequency of future orders, the mix of resources an awardee must have to perform expected requirement, and the ability to maintain competition between awardees throughout the duration.[32] The circumstances where multiple awards must not be used are also dictated.[33] The decision on whether a multi-award or single-award IDIQ is selected and the relevant justification should be recorded. All the above requirements call for careful planning of acquisition and design before embarking on the award procedures.

After the planning phase, the contracting officer starts the first stage of an IDIQ by soliciting tenders, following the

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[30] There are many literatures analysing the value of IDIQs in responding to emergency procurement. See J. I. Schwartz, "Katrina's Lessons for Ongoing US Procurement Reform Efforts", (2006) 6 *P.P.L.R*, pp. 363-373; K. J. Wilkinson, fn. 6, *supra*, pp. 231-286; U.S. Office of Federal Procurement Office, *Emergency Acquisition Guide* (May 31, 2007)

[31] *FAR* 16.504(c)

[32] *FAR* 16.504(c)(ii)(A).

[33] *FAR* 16.504(c)(ii)(B).

selected award procedures, i.e. sealed bids or competitive negotiation. The main contents of a solicitation include: the duration of the contract(including any options); total minimum and maximum quantity of the goods and services to be acquired; a statement of work, describing the general scope, nature, complexity, and purpose of the subject matter to be purchased under the contract, so as to allow a supplier to determine whether he has interest and how to submit an offer.

Apart from the above, the solicitation should also include the procedures to be used for issuing subsequent orders.[34] In the case of multiple awards, the procedures and selection criteria must "provide awardees with a fair opportunity to be considered for each order".[35] The information would be repeated in the IDIQ contract itself. The IDIQ may be awarded based on either lowest price or "best value".

4.3.2 *The second stage procedures*

Once an IDIQ is in place, user agencies may directly place orders from the awardees within the scope of the contract. All awardees should be given a "fair opportunity" for being considered for each order valued above USD 3,500 (micro purchase) unless exceptional circumstances are met.[36]

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[34] *FAR* 16.504(a)(4)
[35] *FAR* 16.504(c)
[36] *FAR* 16.504(b)(1)(i), (2)

Where the order is below the simplified acquisition threshold (SAT), the contracting authority is not required to invite all the awardees and may use the information available to determine the best offer.[37] If the order exceeds the SAT, it should be awarded "on a competitive basis". The contracting officer should issue "fair notice of the intent" to all the awardees to invite tenders, which includes a description of the subject matter and the selection criteria used for the award.[38] All offers received should be fairly considered.

Additional competition requirements should be followed in orders exceeding USD 5.5 million. Apart from the fair notices of intent issued, the contracting officer should (i) provide a reasonable period for awardees to respond; (ii) specify the evaluation factors, and their relevant importance that may be used; and (iii) provide post-award notices and debriefing to unsuccessful awardees regarding the result.[39]

Yukins submitted that the second stage of IDIQ often lacks transparency and competition.[40] For the awards based on IDIQs, there is no obligation to publish award notices, as required in other procurements. [41] Although additional procedural

[37] *FAR* 16.504(b)(1)(ii)
[38] *FAR* 16.504(b)(1)(iii)
[39] *FAR* 16.504(b)(1)(iv)
[40] C. R. Yukins, "Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting", 37 *Public Contract Law Journal* (Spring 2008) 3, p.562
[41] *FAR* 5.301(b)(3)

requirements apply to large (high value) orders, contracting authorities are still given broad discretion/ flexibility in developing procedures for placing orders.[42]

Furthermore, a large part of task orders under IDIQs are "protest-proof", as explained below. Thus, the "fair opportunity" requirement, which was intended to ensure competition at the second stage, may be softened and become meaningless, as aggrieved awardees cannot protest and seek remedies.[43]

As Yukins argued, the awards of task orders against IDIQ contracts may be "below the radar", and the second stage may become a "black hole" of oversight and review.[44] It is gratifying the problems have been recognised, and incremental efforts have been devoted to enhancing transparency and competition in IDIQ contracts.[45]

4.4 Centralised Purchasing Vehicle: the GSA Schedules

The GSA Schedules administered by the GSA represent one of the largest and most preferred programs to date for commercial items. GSA Schedules are essentially IDIQ contracts but also differ from the "standard" IDIQs in many ways. For instance, the GSA Schedules are open arrangements and involve a fully

[42] *FAR* 16.505(b)(1)(ii)
[43] K. J. Wilkinson, fn. 6, *supra*, pp.231-286
[44] See C. R. Yukins, fn. 40, *supra*, pp.545-568
[45] *Ibid.*, pp.545-568

electronic/automatic process, in contrast to the closed "standard" IDIQ contracts. They also differ in the extent of transparency and competition applicable at the second stage and in the availability of protests as explained below. The GSA Schedules are governed by *FAR* Subpart 8.4.

4.4.1 *Awarding schedule contracts*

The first stage of the GSA Schedules is much analogous to open framework agreements under the *Model Law* and dynamic purchasing systems in the EU.[46] The Schedule contracts are established before actual requirements, based on the assumption that certain commercial items will always and commonly be needed by federal agencies.

All solicitations for the Schedule contracts should be publicised electronically on the Federal Business Opportunities (FBO), the portal for all federal procurement opportunities.[47] New suppliers can request to join at any time within the validity. To that end, solicitations are standing, subject to continuous refreshments and updates to reflect the latest terms and conditions.[48] Suppliers should identify the solicitations against

[46] As outlined in section 3 of this chapter, framework agreements in the EU are presumed to be closed and an open and online contracting vehicle- dynamic purchasing system- was introduced by the 2004 EU Directives.
[47] https://www.fbo.gov/
[48] GSA, *Multiple Award Schedules Desk Reference 2016* (Version 7, Fall 2016), p.121

which they wish to offer items, and electronically submit offers, in compliance with the relevant instructions.

Because the Schedules are open-ended, there is no head-to-head competition between the tenders, which are evaluated on their merit. Both the suitability of suppliers and their offers will be reviewed for admission. Contracts are awarded to the "responsible" suppliers that submit "responsive" offers within the Schedule scope, and whose prices are determined "fair and reasonable".[49]

To determine whether the prices are "fair and reasonable", the GSA contracting officers use several tools, which mainly include: (i) price analysis based on market research, sale histories and invoices; (ii) pre-award audits, to verify the submitted information and avoid overpricing[50]; (iii) in particular, the "Most Favoured Customer" clause (MFC); and (iv) the new Transactional Data Reporting Clause (TDRC)[51].

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[49] GSA provides the following criteria for evaluation: responsibility, responsiveness, scope, subcontracting plan if any, and price analysis and review of terms. See GSA, "Responding to a Solicitation" (Lastly reviewed May 26, 2016), available at https://www.gsa.gov/portal/content/202577 (accessed Sep 24, 2018)

[50] Although the value of pre-awarded audits is recognized, this tool has been underused in practice. See GAO, "Contract Management: Opportunities to Improve Pricing of GSA Multiple Award", GAO-05-229 (Feb. 2005); See also Nicholas M. Economou, "MAS Schedule Policy Advisory Panel Discussion on Fair and Reasonable Price Determinations", (Aug. 4 2008), available at https://www.gsa.gov/graphics/staffoffices/EconomouLtrs-Aug4and13_R2-g-a1Q_0Z5RDZ-i34K-pR.pdf (accessed Sep 24, 2018)

[51] See *Federal Register Volume* 81, Number 121 (June 23, 2016), at 41104, available at https://www.gpo.gov/fdsys/pkg/FR-2016-06-23/html/2016-14728.htm (accessed Sep 24, 2018)

Since there is no meaningful competition at the first stage establishing the price, the MFC clause was intended to obtain the best price through benchmarking the price under Schedules against the price in the commercial marketplace. [52] The MFC clause mandates a supplier to offer the price under the Schedules at least as favourable as that it offers to any of its commercial customers.

The TDRC is a newly introduced tool that replaces the previous "Price Reduction Clause" (PRC). Under the earlier PRC, suppliers were asked to reduce the price offered to the government whenever lowering prices for the similarly situated customers.[53] The clause was removed in 2016. The new pilot scheme-TDRC obligates the suppliers to submit monthly reports, including details of orders awarded under the GSA Schedules, GWACs, and other IDIQ contracts. The focus of the price-tracking and comparison shifts from the "vertical-level" (benchmarking the price under Schedules against that in the

[52] It is submitted by Yukins that "how to control prices" is perhaps the most important difference between "standard" IDIQ contracts and the GSA Schedules. In the former case, competitive prices are established through the first-stage competition. In the GSA Schedules, the "competitive forces" are in the commercial marketplace, instead of the government marketplace. Notably, Yukins further submits that the MFC clause "creates onerous fraud risks" for suppliers. See C. R. Yukins, "The U.S. Federal Procurement System: An Introduction", GW Law Faculty Publications and Other Works (2017)

[53] GSA, "Final Plan for Retrospective Analysis of Existing Rules" (August 18, 2011), available at https://obamawhitehouse.archives.gov/sites/default/files/other/2011-regulatory-action-plans/departmentofstateregulatoryreformplanaugust2011.pdf (accessed Sep 14, 2018)

commercial marketplace) to "horizontal-level" (between similar prices paid by other agencies). The TDRC is expected to improve the GSA's ability to conduct more effective price analysis and to validate "fair and reasonable" prices. The impact of the new clause remains to be seen.[54]

Despite these tools, in practice, they are not always effectively implemented, thus less likely to help achieve the best price. For instance, the GSA Inspector General reported that contracting officers had not been consistently negotiating MFC or conducting price analysis.[55] It is not surprising to find that the Schedules do not necessarily provide the best value and agencies may overpay for their orders.[56]

A contractor, upon the award, is required to publish a price list for its contract.[57] The information of all Schedules is available on GSA *eLibrary*.[58] Each Schedule contract is valid for a base of five years, with renewable options for up to three additional five-year periods.[59] Such a long duration makes sense as the "open" nature of Schedules can reduce the risks to

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[54] J. S. Aronie, "Price Reductions Are Dead; Long Live Price Reduces-Transactional Data Reporting Rule" (July 25, 2006), available at www.sheppardmullin.com (accessed Sep 16, 2018)
[55] Office of Audits, Office of Inspector General of U.S. GSA. See "Major Issues from Multiple Award Schedule Preaward Audits", Audit Memorandum Number A120050-3, A 120050-5, A 120050-6 dated Sep. 26, 2011; Mar. 13, 2015 and Sep. 19, 2016.
[56] *Ibid.*
[57] GSA Schedule contracts shall be articulated in compliance with *FAR* Subpart 12 and the *GSAR*.
[58] See https://www.gsa.gov/portal/content/100020 (accessed Sep 24, 2018)
[59] *FAR* 2.101

competition, as is the case with dynamic purchasing systems in the EU and open framework agreements under the *Model Law*.

4.4.2 *Ordering under Schedule contracts*

At the second stage, orders can be awarded directly from the awardees in compliance with the prescribed procedures.[60] An agency, wishing to place an order, can search and browse all items available via GSA *Advantage!*®, the electronic shopping system for federal government,[61] or via *GSA eLibrary*.

The specific procedures may vary between orders, depending on two factors: (1) whether a Statement of Work (SOW)[62] is involved; and (2) the amount of the given order. Two value thresholds are in place, dividing orders into three sub-types: orders at or below the micro-purchase threshold of USD 3,500 (Micro), orders exceeding the micro-purchase threshold but not exceeding the simplified acquisition threshold of USD

[60] *FAR* 6.102(d)(3). An ordering activity against a Schedule contract is considered as to have complied with the full and open competition requirement, pursuant to the *Competition in Contracting Act 1984,* codified in *10 U.S. Code § 2304*

[61] See https://www.gsaadvantage.gov/advantage/main/home.do (accessed Aug 24, 2018)

[62] According to *FAR* 8.405-2(b), a SOW "shall include a description of work to be performed; location of work; period of performance; deliverable schedule; applicable performance standards; and any special requirements (e.g., security clearances, travel, special knowledge) …".

150,000 (SAT), and orders exceeding the SAT.[63] Acquisition planning is needed in any order.[64]

- Ordering Procedures Not Requiring Statement of Work (SOW)

A SOW is a document that describes the requirement and defines the procurement in detail. It is not required for orders for products and fixed-price services under the Schedules. The procedures are structured in *FAR* 8.405(1). GSA has produced a figure to visually display the ordering procedures not requiring a SOW, which is reproduced below as Figure 3.1 for clarity.

As the figure shows, no procedural requirements are imposed for micro-purchases. For orders above the micro-purchase threshold but below SAT, agencies should survey or request for quotations from at least three contractors and make the "best value" determination.[65] Where orders exceed the SAT, agencies, following the "simplified acquisition procedures", should issue Request-for-Quotation (RFQ), consider more than three awardees and seek an additional price reduction.[66]

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[63] Primarily governed by 41 U.S.C. 1908, micro-purchase and simplified acquisition thresholds should be subject to mandatory review and adjustment, and the adjustments are calculated and updated in *FAR* in every fifth year that is evenly divisible by five. The current thresholds were adjusted on July 2, 2015.
[64] *FAR* 8.404(c). This highlights the acquisition planning phase in the US federal procurement. By contrast, in China as depicted in Chapter V, such phase is often either omitted or conducted improperly.
[65] *FAR* 8.405-1(c)
[66] *FAR* 8.405-1(d)

- Ordering Procedures Requiring Statement of Work

A SOW is required when ordering services at hourly rates under Schedules, the requirements of which cannot be specified in advance and may vary among different agencies, such as consultancy service. The ordering procedures requiring SOW are governed under the *FAR* 8.405-2.

Where a SOW is required, the user agency is always required to "solicit head-to-head competition by issuing RFQ" before placing an order. The ordering procedures, in this case, are more complex and challenging than awards without SOW being involved.[67] User agencies should issue an RFQ containing a SOW in orders exceeding the micro-purchase threshold. The Figure 3.2 below, generated by GSA, provides the ordering procedures that require a SOW.

[67] R. J. Sherry, G. M. Koehl and S. A. Armstrong, "Competition Requirements in General Services Administration Schedule Contracts", (2008) 37 *Public Contract Law Journal* 3, pp.467-487

Figure 3.1 Ordering Procedures Without a SOW

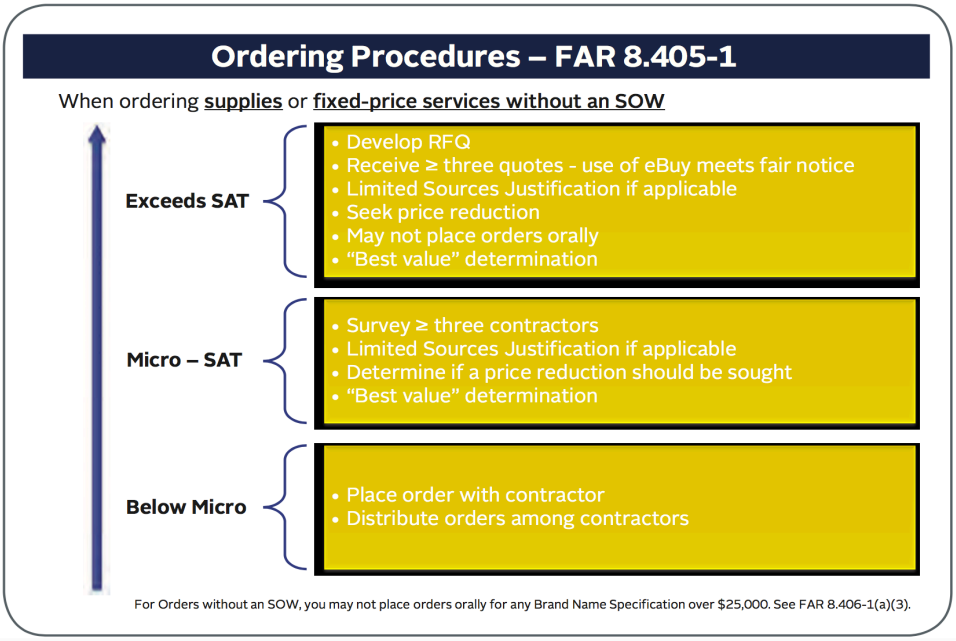
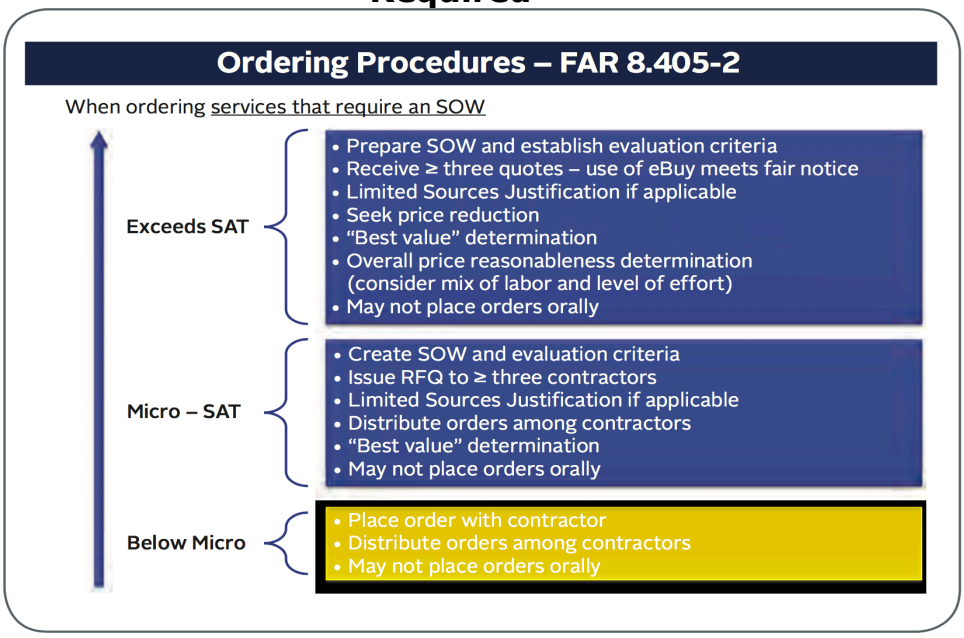


Figure 3.2 Ordering Procedures When a SOW Is Required



Source: GSA, *Multiple Award Schedules Desk Reference 2016*, (Version 7, Fall 2016)

Agencies must request a price reduction where the order is valued above the SAT and are encouraged to voluntarily do so in all cases, to reflect the quantities ordered and/or the current

conditions of the market.[68] However, GAO reported that user agencies often opted not to haggle over as envisaged, which may be a contributor to overpricing problem.[69]

Suppliers do not have to reduce the price as requested. To "induce" them to offer discounts, the *FAR* provides that a supplier providing an agency with a discount not be obliged to provide the same offer to other agencies.[70]

Apart from direct ordering, user agencies may establish Blanket Purchase Agreements (BPAs) with one or more than one contractor against any Schedule contract to fulfil repetitive needs.[71] Once a BPA is put in place with a selected supplier, the agency can place direct awards without further competition. To some extent, a BPA is close to a mini-IDIQ within an IDIQ.

Similar to the "standard" IDIQs, there are limited information obligations in orders under Schedules. User agencies are not required to notify ("synopsize") their intention to order.[72] Award notices regarding the task orders are exempted here either.[73] The lack of communication may provide perfect opportunities for potential irregularities.

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[68] *FAR* 8.405-4
[69] GAO, "Contracting Strategies: Data and Oversight Problems Hamper Opportunities to Leverage Value of Interagency and Enterprise wide Contracts", GAO-10-367 (April 2010) p.50
[70] *Ibid.*
[71] The procedures to establish BPAs are provided under the *FAR* 8. 405-1 and 8.405(2).
[72] *FAR* 8.404(a)
[73] *FAR* 5.301(b)(3)

Ordering under GSA Schedules appears to be administratively complex as it involves too many overlapping options, which may offset the envisaged simplicity and efficiency of the programme.

4.5 Protests

The bid protest mechanism, known as the remedies in the EU and challenge proceedings under the *Model Law*, has always been a critical safeguard to enforce the laws in the US federal procurement.[74] To date, an aggrieved protester may select to file a protest of the award of an IDIQ contract at one of three primary fora: procuring agency (agency protest), [75] the Government Accountability Office (protest at GAO),[76] or the US Court of Federal Claims (COFC)[77]. Agency protest is not the pre-requisite for other fora. However, a protestor is encouraged to seek initial resolution at the agency level.[78]

In the context of IDIQs, the first stage of awarding IDIQs is fully subject to "bid protests", as other procurement contracts. With regard to task orders based on IDIQs, a distinction is made

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[74] J. Cibinic *et al*., fn. 16, *supra*, p.1673.
[75] *FAR* 33.103. The legal base of agency protest is the *Executive Order* 12979.
[76] 31 U.S.C. § 3551. Protests at GAO are governed by the *GAO Bid Protest Regulations*, codified at 4 C.F.R. subpart 21
[77] 28 U.S.C. § 1491(b).
[78] *FAR* 33.102-(e). For more analysis about the protest forum, see M. J. Schaengold, T. M. Guiffre and E. M. Gill, "Choice of Forum for Federal Government Contract Bid Protests", (2009) 18 Fed. Cir. B. J. 2, p. 84.

between orders under "standard" IDIQ contracts and those based on the GSA Schedules.

In the cases of "standard" IDIQs, protests in connection with the awards of task orders are authorised on one of the two grounds: (1) an order increases the scope, period, or maximum value of the underlying contract; or (2) an order is valued in excess of USD 10 million.[79] The CGFC, by statute, can only hear protests on the first ground, while GAO has the exclusive jurisdiction over protests based on the second ground.[80]

A GAO protest of an order exceeding USD 10 million may be brought on any issues arising at the ordering stage.[81] Protests against small task orders are not allowed before GAO. However, a difficulty is present regarding how to determine whether or not the order at issue is valued above USD 10 million. This issue is critical and should be clarified as it determines the scope of GAO's jurisdiction over order protests. Although GAO clarified some aspects in its decisions on several cases, for instance, explaining that the price proposed by an offeror does not

[79] As explained in section 4(1) above, the US gradually opened the gate of protests to task orders based on IDIQ contracts after the 1994 *FASA* "protest ban".
[80] *FAR* 16.505(10)
[81] 41 U.S.C. § 4106(f)(1)(B). As mentioned earlier, GAO reinstated its jurisdiction over protests of civilian task order awards by the end of 2016 by *GAO Civilian Task and Delivery Order Protest Authority Act of 2016*.

necessarily represent the value of the order, more and objective guidance is needed on this issue.[82]

Notably, the above protest restriction on task orders under the "standard" IDIQ contracts does not apply to that under GSA Schedules. It means the task orders within the Schedules at any value can be protested, which may remedy the lack of transparency at the second stage of the Schedules.

5 Conclusions: Experience and Lessons from the Selected Systems

Framework agreements are used and regulated under the three systems in different manners, grounded on their legal and institutional frameworks, and based on the objectives and reflecting procurement capacity of each procurement system.[83]

Among the three systems, the *Model Law* provides the most comprehensive regulatory approach, with detailed procedural safeguards, supported by extensive guidance (through the

[82] M. Alinger, "Recent Developments in Task and Delivery Order Contracting" (Summer 2009) 39 *Public Contract Law Journal* 4, pp.839-852; *ESCO Marine, Inc.*, Comp. Gen. B-401438 (September 4) 2009, 09 CPD ¶ 234

[83] For different scopes and effects of public procurement rules in the EU, US and UNCITRAL Model Law, see L. Ș. Filipon, *Non-Traditional Regular Purchasing Arrangements in Public Procurement- A Doctrinal and Comparative Analysis of Regulation and Implementation Systems*, PhD Thesis, University of Nottingham, School of Law (March 2018); D. I. Gordon and G. M. Racca, fn. 22 *supra*, "Integrity Challenges in the EU and U.S. Procurement Systems", Ch. 1 Part II in C. R. Yukins and G. M. Racca (eds.), *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (Bruylant, 2014), pp. 117-118

Guide to Enactment). This is because the *Model Law,* as a "framework" law, is intended to provide all essential procedures for conducting framework agreements and to assist the enacting States, especially the developing states, to strike a proper balance between the procurement objectives, especially between efficiency and integrity. In contrast, the US federal system, relying heavily on streamlined arrangements in the acquisition of commercial items, tends to tip the scale in favour of efficiency and convenience over integrity, and arguably adopts the most flexible approach to governing IDIQs, such as imposing protests restriction on task orders.

The EU procurement system is *sui generis* because the top priority of the EU Directives is to achieve single market. Therefore, other procurement objectives including value for money, efficiency and integrity, are less concerned at the EU level, which are left to the Member States. Another particularity of the EU system is that there are separate rules on public procurement in the public and utilities sectors. This is mainly on account of the different nature of the procuring entities and the need for greater flexibility in the utilities sector.[84] For instance,

[84] Arrowsmith proposed to have only a single procurement directive that regulates all procurement to achieve true simplification. See S. Arrowsmith, "Modernising the EU's Public Procurement Regime: A Blueprint for Real Simplicity and Flexibility" (2012) 21 *P.P.L.R.* 71–82. As suggested later in Chapter VIII, the EU's approach provides a way forward to improving the Chinese public procurement framework.

negotiations in call-offs are allowed in framework agreements in the utilities sector but not allowed in the public sector.[85] Qualification systems are only permitted in the utilities sector.

Generally speaking, all three selected systems provide relatively comprehensive regulation on framework agreements. Different types of framework agreements, as classified in Ch. II, are allowed in all systems, i.e. closed frameworks, with or without second stage competition, and open framework agreements (DPS in the EU and GSA Schedules in the US). Notably, to promote and ensure on-going competition in the second stage, the US system establishes a statutory preference for multi-award IDIQs.

Concerning operational procedures, the first stage of concluding closed frameworks, is similar to awarding contracts in "traditional" procurements. Notably, the *Model Law* makes open tendering as the default option and should be preferred over other award procedures. In the EU and US systems, procuring entities are free to choose the award procedures.

In all the selected systems, nearly full transparency safeguards apply to the first stage, for instance, including the requirement on the information to be included in procurement

[85] The provisions on framework agreements under the *2014 Utilities Sector Directive* are more prescriptive than those in the earlier Directive. The new rules aim to increase transparency in the procedures for concluding of frameworks. This is in line with the trend of enhancing transparency argued in this chapter. However, the provisions regarding the call-off stage are still less detailed than those in the public sector.

documents. Procuring entities are required to disclose information as much as possible at this stage to maximise competition and to ensure stage consistency. However, the risk of collusion, which is closely related to and interacted with information disclosure, seems being less considered.[86]

Careful planning and preparation before launching award procedures is always good practice, being accentuated in all systems. This can be reflected by the level of details required in the solicitation and master agreements, for instance, the estimated total quantity or value of expected awards under framework agreements, and in multi-supplier frameworks, the estimated number of admitted suppliers. The *Model Law* further obligates procuring entities to record the decision to use framework agreements and the selected type with reasons. In the US, the decision on whether a single award or multiple awards are selected, and the justifications need to be documented as well. *FAR,* furthermore, lists the elements to be factored in determining the appropriate number of suppliers.

With regard to the second stage, the normal transparency and competition requirements are to different extent "relaxed" to ensure simplicity and expedience in call-offs. Due to that, the

[86] A paradox of detailed information is the risk to collision. For discussion on the information dynamics, see G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press, 2016) chapter 9.

ordering stage tends to be more vulnerable to improper use and abuse. Arrowsmith describes the call-off stage as an "inherent transparency gap".

The *Model Law* provides the highest level of transparency and competition safeguards on call-offs among the three systems. The high standard can be exemplified from, for instance, the compulsory notification of any upcoming second-stage competition to all supplier parties and the application of award notices regarding call-offs.

In contrast, in the EU and US federal systems, the second stage of framework agreements and IDIQs tends to be often saddled with lack of transparency, uncertain competition and inadequate oversight.[87] At the EU law level, there is neither *ex-ante* notification for upcoming call-offs nor *ex-post* notices after awards under frameworks. Particularly noteworthy is that the UK, at the national level, takes a step towards enhanced transparency in requiring publication of contracts awarded based on framework agreements at the national level, irrespective of the value. In the US, procuring entities are granted broad discretion in awarding task orders, despite the "fair opportunity" requirement and additional procedural safeguards in large orders. Moreover, the US rules allow much

[87] See C. R. Yukins, fn. 40, *supra*, at p.553

more “relaxed” limit on the duration of IDIQs, which can be as long as 20 years.

In the context of open framework agreements, they are operated and maintained on a fully electronic basis. In all the selected systems, the solicitation should be “standing”, and new suppliers can request to join at any time within the validity. No substantial competition is envisaged at the first stage.

At the ordering stage, the *Model Law* and EU system require all supplier parties to be invited to any call-offs. Contract award notices are required for orders awarded under DPS, either in the form of separate notices for each award or through grouped notices. In contrast, in the US, transparency and competition are largely diluted in awarding task orders under GSA Schedules. For instance, for large orders, procuring entities may restrict the notice of an intended task order to three supplier parties, provided that they are envisaged to respond. There are limited information obligations regarding the awards of orders.

The supplier review measures/ challenge proceedings/ bid protests vary among the three selected systems, grounded on their own underlying judicial traditions. The first stage of framework agreements is subject to full review in all systems reviewed, just like the “traditional” procurements.

However, the second stage seems to be in limbo, being less monitored and reviewable, which can be attributed to various

reasons. For instance, challenges against call-offs may be restricted with a view to avoiding excessive disruptions to the procurement process, which may jeopardise administrative efficiency. Alternatively, the lack of transparency at the ordering stage, as is the case in the EU, makes timely challenges and pre-award remedies meaningless.

Among the three systems examined, the *Model Law* provides the most thorough coverage of supplier review for call-offs, recalling the fact that it seeks to help the enacting states to properly balance integrity and efficiency in the use of framework agreements. While it allows challenges against all acts and decisions, the robust transparency safeguards imposed to the call-off stage (mainly those with second-stage competition) make the supplier review implementable.

From the historical evolvement, the US and EU experiences suggest that enhanced transparency and competition are needed to deter and prevent any improper use of frameworks. The continuous fine-tuning of the regulations and policies on IDIQs in the US provides a perfect example of this. There will always be concerns and doubts that more safeguards may impede administrative efficiency, which is generally considered the core benefit of framework agreements. However, in light of the availability and development of IT in public procurement, the above concerns tend to be unfounded. For instance, the

additional information obligations, i.e. notices of any ordering opportunity, can be issued at negligible cost and time. Moreover, as highlighted by Albano and Nicholas, sophisticated planning and design can assist procuring entities in ensuring ease of use in call-offs while securing integrity and competition.

There is also a tendency of "liberalising" protests against call-offs based on framework agreements to improve integrity and accountability, which can be demonstrated by the historical evolvement on this issue on both sides of Atlantic. More frequent and apparent efforts in this respect can be observed in the US federal system, as explained in section 4. Currently, protests against large task orders are explicitly allowed.

The consistent issues and reorientation efforts in the three systems arguably suggest a need of enhancing transparency and oversight at the second stage of framework agreements, especially in less-developed procurement systems, which can be demonstrated by the comprehensive regulatory approach that the *Model Law* adopts. The international experiences also reveal the need for continually tuning up the trade-offs between different objective to promote the beneficial use of frameworks.

It is equally important to note that not all problems related to framework agreements are legal issues, and they cannot be adequately addressed by regulation alone. As Yukins observed, in the US, although there is significant public support for reform

and on-going efforts devoted at the policy level, the reform was perceived fragmented and "tortuous", moving upon compromises. The main reason for that is the resistance from the stakeholders with vested interest in the less-transparent and anti-competitive procurement marketplace.[88] One lesson from the US is that understanding and coordinating the interests of various stakeholders need to be considered in proposing reform in any procurement systems. To have in place practical and institutional measures is critical to implementing well-intended and designed rules and policies.[89] The availability of well-trained and experienced procurement personnel is undoubtedly a key to ensure proper use of framework agreements in any system.

[88] See Yukins, fn. 40, *supra*, at p.553

[89] See G. L. Albano and C. Nicholas, fn. 86, *supra*, pp.122-123. As explained in Chapter IV, fragmentation features the institutional framework for public procurement in China, where the political pressures and compromise have stunted the evolvement. There is a need, therefore, to have a full picture of public procurement and to find an acceptable approach to development.

Chapter IV. Overview of Chinese Public Procurement

Over the past three decades, China has built up its unique dual regulatory framework for public procurement. Public procurement activities in China are primarily governed under two national laws: *The Government Procurement Law (GPL)* and the *Tendering and Bidding Law (TL)*.[1] It needs to be noted from the outset that "government procurement" and "public procurement" are distinguished in China. The *GPL* adopts a narrow definition of "government procurement", which refers only to procurement by government agencies, institutions and public organisations at all levels with fiscal funds.[2] Therefore, other activities of what may often be considered as "public procurement" are not "government procurement" in China, such as the procurement by state-owned enterprises (SOEs), which is, to a limited extent, subject to the *TL*.

Both the *GPL* and *TL* are implemented by numerous regulations and rules that form a rather complex regulatory "net", which may perplex the outsiders. This chapter seeks to

[1] For more information about the history of China's public procurement, see P. Wang and X. Zhang, *Chinese Public Procurement Law: An Introductory Textbook*, (Nottingham: The EU Asia Inter University Network for Teaching and Research in Public Procurement Regulation, 2010); F. Cao and P. Wang, "The New Chinese Government Procurement Law" (2002) 6 *P.P.L.R.*, NA133–9; R. Rothery, "China's Legal Framework for Public Procurement" (2003) 3 *Journal of Public Procurement* (3), p.370

[2] *The GPL*, Art. 2

illustrate the legal and institutional frameworks for public procurement in China, against which context the evolvement of framework agreements will be explored. It serves to usher in the further analysis of how framework agreements are used and regulated in China in the following chapter.

1 The Legal Framework for Chinese Public Procurement: A Dual System

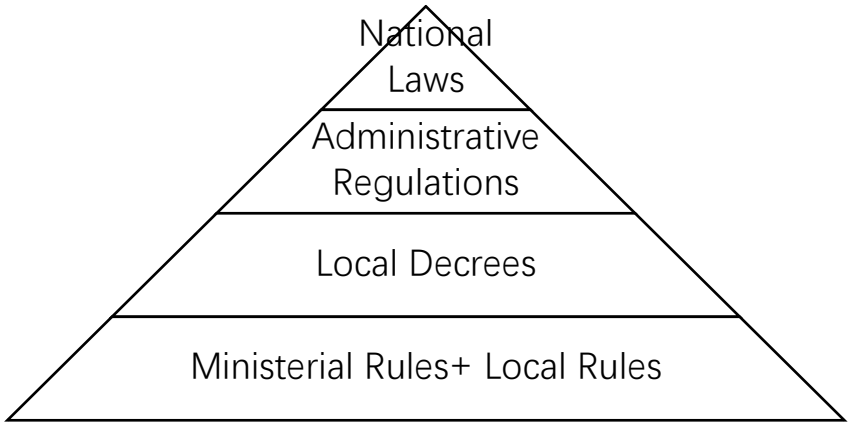
1.1 Hierarchy of Chinese Legislation

The hierarchical structure of all regulatory norms in China is established under the *Legislation Law*.[3] Broadly, Chinese legislation comprises: the Constitution at the top level; the national laws promulgated by the National People's Congress and its standing committee at the first level; administrative regulations enacted by the State Council at the second level; local decrees issued by Provincial People's Congress at the third level; and at the fourth level, ministerial rules adopted by central ministries and local rules issued by local governments. All laws and regulations should follow the hierarchy and must not overstep their authority or contravene the higher-order.[4]

[3] *The Legislation Law of the People's Republic of China* was promulgated on 15 March 2000, and amended in 2015, available at http://www.spp.gov.cn/zdgz/201503/t20150316_93168.shtml (accessed Sep 30, 2018)
[4] *The Legislation Law*, Art 96

The national laws and State Council regulations, as well as the ministerial rules apply nationally, while local decrees and local rules are enforceable in their specific geographic regimes. One caveat is that ministerial rules and local rules have the same legal authority and should be implemented within their respective jurisdiction.[5] Where there is any inconsistency between the rules adopted by different ministries, or between the ministerial rules and local rules regarding the same issue, it is up to the State Council to determine which rules prevail.[6]

Figure 4.1 The Legislative Hierarchy of China



1.2 A Dual Legal System: The *Tendering Law* and the *Government Procurement Law*

According to Wang, the development of China's public procurement framework could be broadly divided into two

[5] *Ibid.* Art 91
[6] *Ibid.* Art. 95

phases: i) the evolvement of the tendering system since the mid-1980s, spearheaded by the National Commission of Development and Reform (NDRC, then State Planning Commission), culminating in the promulgation of the *TL* in 1999; and ii) the establishment of the government procurement system led by the Ministry of Finance (MOF), earning its pattern with the enactment of *the GPL* in 2002.[7]

In 1979, China initiated its market economic reform and started to transform from a centrally planned economy to a market economy. With the opening of the competitive market, tendering activities were introduced in the mid-1980s mainly to promote competition among SOEs and to reduce corruption in construction projects. Since then, hundreds of regulations and rules governing tendering activities were adopted by different government agencies. However, they were fragmented and often contradictory. In the 1990s, there was a push to set up a national law to give an end to the regulatory chaos, ultimately resulting in the promulgation of the *TL* in 1999.[8]

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[7] P. Wang, "China's Evolving Legal Framework on Public Procurement" (2004) 6 *P.P.L.R.* p.286

[8] *Tendering and Bidding Law of the People's Republic of China* (the TL) was promulgated on August 30, 1999 and came into effect on Jan. 1, 2000, available at http://www.npc.gov.cn/wxzl/gongbao/2000-12/05/content_5004749.htm (accessed Sep 24, 2018). For more information about the evolvement of tendering system in China, see J. Tian, "Public Procurement in China: The Way Forward" (2001) 4 *P.P.L.R.* p.207; F. Cao, "From Tendering Law to the Public Procurement Law", in S. Arrowsmith and M. Tybus (eds.), *Public Procurement: The Continuing Revolution* (Kluwer Law International, London, 2003); P. Wang, "China's Evolving Legal Framework on Public Procurement" (2004) 6 *P.P.L.R.* p.287; Q. Kong,

The *TL* is the first national law on public procurement in China, reflecting a significant movement towards a modern procurement regime. However, since the *TL* still maintains a focus on tendering activities mainly in construction projects, regardless whether the purchaser is a government agency, a private company or an SOE. It prohibits any negotiations or other flexible procurement methods. The potential coverage of both the public and private sectors and the availability of tendering procedures only all preclude the *TL* from being comprehensive public procurement legislation.[9]

The *GPL* developed separately as a result of "a new wave of government procurement reform" in the mid-1990s, which was part of the national fiscal and tax reforms, the purpose of which was to strengthen control of the public expenditure.[10] The governments at all levels actively conducted pilot projects and adopted their rules on government procurement. By 2000, the MOF had published a series of ministerial rules in this respect.

From the global view, public procurement has been increasingly bound up with international trades and foreign investment. Leading international and regional organisations

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"Chinese Law and Practice on Government Procurement in the Context of China's WTO Accession" (2002) 11 *P.P.L.R*. pp.61-84

[9] P. Wang, fn. 7 *supra,* at p.292; P. Wang and X. Zhang, fn. 1 *supra,* at p.11

[10] P. Wang, C. H. Bovis and X. Tu, "A Comparative Analysis of Utilities Procurement in EU and China", component 5 of *A Report Prepared for EU-China Trade Project* (II) (August 2013), p.87

such as WTO have set up agendas to liberalise public procurement market.[11] Upon the WTO's accession, China committed to joining the Agreement on Government Procurement (GPA) and started the negotiation soon.[12] To have a public procurement framework in conformity with the international norms had become a *sine qua non* for China to march into international organisations and trade.[13]

Against such context, in 1999, a legislative programme for a national government procurement law was initiated, just when the *TL* was about to be enacted. In 2002, the *GPL* was promulgated and came into effect on Jan 1st, 2003. The *GPL* represents the formation of the dual-track regulatory system of public procurement in China.[14]

The *GPL* defines "government procurement" in a modern but narrow manner, as explained earlier. In addition to open and restricted tendering, it allows competitive negotiations, request

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[11] R. Rothery, fn. 1, *supra,* p.374

[12] "The Report of the WTO Working Party on the Accession of China" (1 Oct. 2001), WT/ACC/CHN/49, available at https://www.wto.org/english/tratop_e/gproc_e/gp_gpa_e.htm (assessed Aug 14, 2018).

[13] See Rothery, fn. 1 *supra,* at p.375.

[14] X. Tong, "Chinese Procurement Law: Current Legal Framework and A Transition to the World Trade Organization's Government Procurement Agreement" (2003) Spring, *Temp. Int'l & Comp. L. J.* p.140; I. Gebhardt and M. Mueller, "China's New Government Procurement Law: A Major Step Towards Establishing a Comprehensive System?" (July/Aug. 2002) *China Law and Practice*

for quotations and single-source procurement, and provides the circumstances for their use.[15]

The *GPL* divides government procurement into centralised and decentralised procurement.[16] The scope of centralised procurement is determined by the relevant centralised procurement catalogues. The catalogues list the type of items that must be centrally purchased, which are determined and updated by MOF (at the central level) and the local governments (at the local level).[17] Therefore, the scope of centralised procurement between central and local governments and that between different localities varies. Moreover, there are several line ministries, such as Taxation Administration and Customs Administration that establish their own departmental procurement catalogues for the items that they have special requirements.[18] A supplier review and remedy system is established under the *GPL*, which is absent in the *TL*.

The *GPL* made significant breakthroughs in improving the Chinese public procurement regime in several aspects, i.e. the availability of different procurement methods and the existence of supplier review. However, it yet failed to harmonise the fractured legal framework. Such "failure" may be attributed to

[15] *The GPL,* Arts.29-32
[16] P. Wang and X. Zhang, fn. 1 *supra,* at p. 31
[17] *The GPL,* Art.7
[18] *Ibid.* Art.18

the complicated institutional framework behind. That is, different central ministries, mainly between the NDRC and MOF, strive mightily for guarding their power while coveting others'. Drafting and enforcing laws and regulations have become one of the ways to "codify" their vested jurisdiction.[19] The "turf battle" amongst the different government agencies not only led to the formation of the dual-law system on public procurement, as now it stands, but has also become one major impediment to the development of Chinese public procurement.

Both the *TL* and *GPL* are based more on principles than on detailed rules, and their provisions are too general in certain aspects, in need of further elaboration and clarification. Therefore, they are respectively implemented by one State Council regulation-the *Implementing Regulation of the Tendering Law (IRTL)* and the *Implementing Regulation of the Government Procurement Law (IRGPL)*.[20] Numerous ministerial

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[19] There was at a certain point during the TL drafting process when the legislators considered tendering should be an integral part of the overall public procurement, especially with the help of international procurement expertise. However, the *TL* failed to fulfil this aim for several reasons, one of which could be the fear of the precedent NDRC and relevant ministries that the *TL* may be "swallowed" by the newly drafting *GPL*. The root cause was the "battle of power" between NDRC and MOF for the leading position in regulating public procurement. See P. Wang, fn. 7 *supra,* at p.292

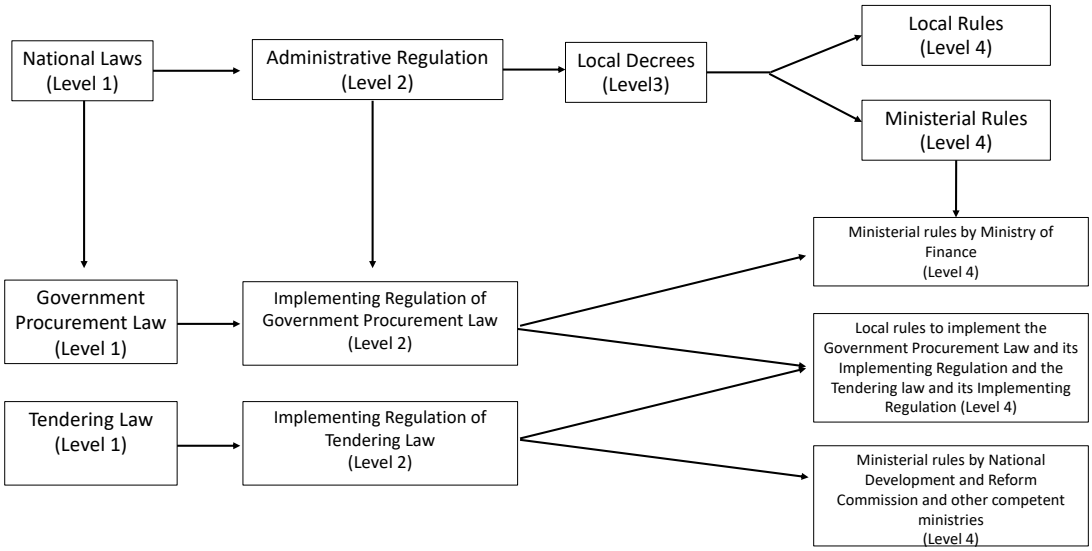
[20] *The Implementing Regulation of the Tendering Law*, enacted by the State Council on Dec. 20, 2011 and came into effect on Feb. 1st, 2012, available at http://www.gov.cn/zwgk/2011-12/29/content_2033184.htm (accessed Sep 20, 2018); *Implementing Regulation of the Government Procurement Law*, enacted by the State Council on Jan. 30, 2015 and came into effect on March 1st, 2015, available at enacted by the State Council on Dec. 20, 2011 and came into effect on Feb. 1st, 2012, available at http://www.gov.cn/zhengce/content/2015-02/27/content_9504.htm (accessed Sep 20, 2018)

rules and local rules are further issued to implement the national laws and State Council regulations. The hierarchical structure of public procurement laws and regulations in China is shown in figure 4.2.

In fact, there is a third stream of regulations separately governing the import of machinery and electrical products via international tendering in China- the *Implementing Measures for International Tendering for Machinery and Electrical Products (for Trial Implementation)* (IMIT).[21] Following the established practice, Ministry of Commerce is the regulatory authority on international tendering in this respect. Currently, there is a fourth stream of regulations separately governing public-private partnership projects.

[21] Hereinafter referred to as the IMIT. *The IMIT*, Order No.1 [2014] of the MOFCOM, was enacted on February 21st, 2014, available at http://www.chinabidding.com/infoDetail/224466622-News.html (accessed Sep 22, 2018)

Figure 4.2 Public Procurement Laws and Regulations under China's Legislative System



1.3 The Coverage of the *Government Procurement Law* and *Tendering Law*

China has two sets of national laws on public procurement: the *TL* and *GPL*. Rather than synergism, there are often overlaps and conflicts between the two laws, i.e. regarding their coverage.[22]

There is no clear division of the scope of coverage of the two laws. Basically, the *TL* applies to all tendering activities (open and restricted tendering) conducted within the territory of China, either public or private.[23] It has a mandatory coverage, whereby three types of works (and the incidental goods and

[22] P. Wang, "China's Government Procurement Policy at a Crossroad", December 2008 (Policy Paper)
[23] The *TL,* Art.2

services) must be procured based on tendering procedures in accordance with the *TL*. These works projects are: (i) large infrastructure and utility projects that concern the public interest or public security including projects in transportation, energy, post, telecommunication, water and other utilities sectors; and (ii) works that are totally or partly funded by the State; and (iii) works using loans from international organisations or foreign governments. [24] The mandatory coverage is the effective coverage of the *TL* in practice, which is essentially restricted to the works procurement based on tendering procedures.

The *GPL* applies to all government procurements in China. Procurement activities are defined as "government procurement" only when three elements are fulfilled. Firstly, government procurement activities are conducted by government agencies, public institutions and public organisations. Secondly, the procurement shall be paid with fiscal funds. Thirdly, the goods, services and works to be procured shall be either within the centralised procurement catalogue or their value exceeds the prescribed thresholds in accordance with the law.[25] Failure to meet any of the three requirements will make a procurement not regarded as "government procurement" and be excluded

[24] The *TL,* Art.3
[25] *The GPL,* Art.2

from the *GPL* application. Thus, the procurement of Chinese SOEs is outside the *GPL* coverage because they are not within the entity coverage. The table 4.1 below outlines the fundamental differences between the *TL* and *GPL.*

Given the above, the scope of coverage of the two laws is primarily defined by the type of the subject matter in procurement (works or goods and services) and the involvement of tendering procedures, instead of the nature of the procuring entities. Such demarcation not only leads to the tensions and overlaps between the two laws but also results in the regulatory gap regarding procurement by Chinese SOEs.[26]

Article 4 of the *GPL* was intended to coordinate the *GPL* with the *TL* by stating that, "the *TL* shall apply where works are procured through tendering proceedings". The *IRGPL* made further efforts to reconcile the coverage overlaps. According to Article 7 of the *IRGPL,* the *TL* and its implementing regulations apply in government procurement of works based on tendering

[26] From the EU experience, in the early phase, the original EU public procurement regulations comprised three Directives that applied to works, services and goods separately. In the later 1990s, the need for modernisation and simplicity was recognised, leading to the consolidation of the existing separate Directives into a single Public Sector Directive. The evolvement of the EU Directives can to some extent reveal the tendency towards coordination and harmonisation, and China is suggested to draw on the EU's experience. See M.K. Larsen, "The New EU Public Procurement Directives", in R. Nielsen and S. Treumer (eds.), The New EU Public Procurement Directives (Djøf Publishing, 2005) p.10. However, it should be noted that from the outset, the rules in the public sector and utilities sectors have not been consolidated into one comprehensive rules.

proceedings, and the *GPL* and its implementing rules are observed in the works procured via non-tendering procedures.

Although the article clarifies the overlap in government procurement of works, it leaves a range of uncertainties unanswered yet. For instance, it remains unclear to what extent the *TL* should govern government procurement of works. Whether the *TL* only applies to the tendering procedures or the whole procurement project in all aspects, including the supplier review rules. It is also unclarified who is the supreme regulator on government procurement of works, the MOF or the NDRC.[27] It is further questionable whether the *GPL* or *TL* should apply where a new procurement method that involves both tendering procedures and other procurement methods emerges, such as framework agreements.

Table 4.1 Differences and similarities between the *Government Procurement Law* and the *Tendering Law*

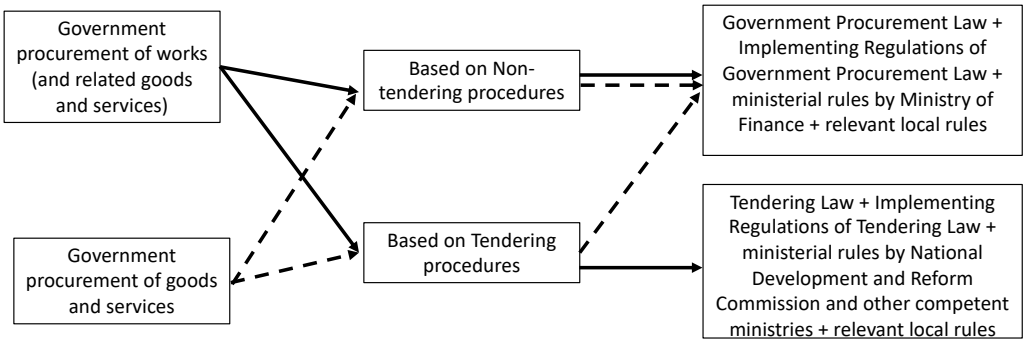
	Government Procurement Law	Tendering Law
Level of legal authority	National law (2nd level) Implementing Regulations of Government Procurement Law (3rd level)	National law (2nd level) Implementing Regulation of Tendering Law (3rd level)
Legal branch	Administrative law	Civil law
Regulatory Authority	MOF and its local branches	NDRC and other Nine Central Ministries

[27] P. Wang, fn. 7 *supra*, at p.306; See also Wang, fn. 22 *supra*, at p.15

End-users	1. Government agencies; 2. Public institutions; 3. Social organisations under budget control including schools, universities, hospitals, research institutions and etc	Government agencies, public institutions, social organisations, SOEs as well as private purchasers
Coverage	Procurement of goods, services and goods when three key factors are satisfied: 1 Procuring subjects are the above users; and 2. The procurement has to use fiscal funds; and 3. the procurement objects are goods, services and works that either within the centralised procurement catalogue or the amount of which exceeds the prescribed thresholds	1. Mandatory coverage: major works concerning public interests or public security and their related goods and services; 2. Voluntary coverage: all tendering proceedings
Typical projects covered	Construction and maintenance of government buildings; office equipment and facility purchases; procurement of government-use vehicles; procurement of services for conferences, etc.	Key construction projects and infraction projects, such as renewable energy projects; electricity generation and supply; water supply; sewage projects; public transportation projects and etc; procurement projects of SOEs, particularly those centrally-administered ones

Methods available	Open tendering, restricted tendering, request for quotation, competitive negotiation and single-source procurement and other methods authorised by MOF	Open tendering and restricted tendering
Intermediate agencies involved and their nature	Central procurement agencies established in accordance with the Government Procurement Law.	Tendering agencies. They are social intermediary cooperates established according to the *Tendering Law*.
Whether SOEs shall apply	No	Yes
Review procedures	Yes	No

Figure 4.3 Application of Rules in Chinese Government Procurement



1.4 The Procurement of Chinese State-owned Enterprises (SOEs)

1.4.1 Overview of Chinese SOEs

Chinese SOEs have a long history and are still the backbone of the national economy, although their relative economic weight has fallen as the result of the successive reforms and transformation.[28] While it is acknowledged that they operate a substantial procurement market, the size of such market is unknown and there is no reliable statistics provided by as the Chinese government on this issue.

There is no legal definition of SOEs in current Chinese laws and regulations, which is more used as a common term. As Wang submitted, a more encompassing term "state-owned and state-holding enterprises" seems more appropriate and accurate to denote SOEs, instead of merely "state-owned enterprises".[29] SOEs, in this case, include (i) state-owned

[28] G. Fan and N. C. Hope, "The Role of State-Owned Enterprises in the Chinese Economy", Ch.16 of the *US-China Economic Relationship in the Next 10 Years*, the China-United States Exchange Foundation (2013)

[29] See Wang, Bovis and Tu, fn. 10 *supra*; See also OECD, "State Owned Enterprises in China: Reviewing The Evidence" (January 26 2009); The U.S.-China Economic and Security Review Commission, *An Analysis of State-owned Enterprises and State Capitalism in China,* (Oct. 26, 2011) Prepared for the USCC by Andrew Szamosszegi and Cole Kyle, Capital Trade, Incorporated, available at https://www.uscc.gov/Research/analysis-state-owned-enterprises-and-state-capitalism-china (accessed May 24, 2018)

enterprises; and (ii) the firms whose majority of shares and holding right belong to the government or other SOEs.[30]

Chinese law lacks unified governance for SOEs. Chinese SOEs comprise central SOEs (yangqi) and local SOEs (difang guoqi). Central SOEs are usually large SOEs, owned by the central government. Majority of the central SOEs are managed by the State-owned Assets Supervision and Administration Commission of the State Council (SASAC), who exercises the investor's right on behalf of the state.[31] Apart from those directly managed by the SASAC, there are two more types of central SOEs: (i) state-owned financial SOEs supervised by the MOF[32]; (ii) other SOEs owned by other central ministries.

Local SOEs are supervised by the SASAC branches established at the local level.[33] SASAC and the local branches exercise broad supervision over the SOEs but do not directly

[30] The regulation of SOEs is scattered in several laws and regulations. Firstly, the wholly state-owned companies are defined under *the Company Law of the People's Republic of China.* Secondly, the *Law of State-owned Assets in Enterprises* defines state-invested enterprises, which includes wholly state-owned enterprises and companies, state-holding companies and state-invest joint stock companies. However, the National Bureau of Statistics in 2006 provides that only state-invested companies with holding right are within the SOEs coverage, as a result of which the state-invest joint stock companies were excluded from the broad concept of SOEs.

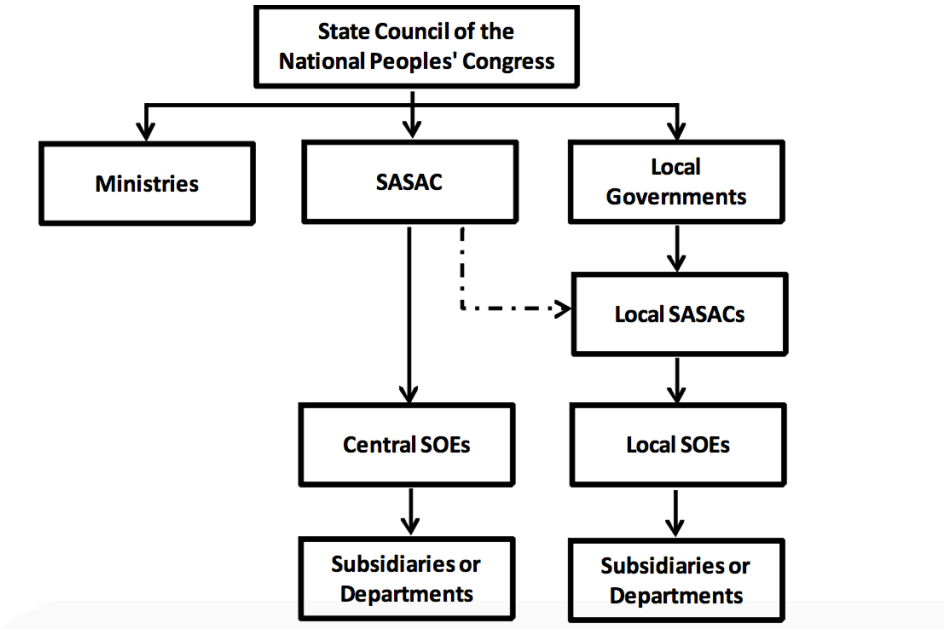
[31] Till the end of 2016, the central SASAC oversees 102 central SOEs, http://www.sasac.gov.cn/n86114/n86137/index.html (accessed May 24, 2018)

[32] State-owned financial enterprises are supervised by the MOF, Central Huijin Ltd., the China Banking Regulatory Commission, China Insurance Regulatory Commission and China Securities Regulatory Commission.

[33] "Notice of the State Council on the Setup of Institutions (annulled)" No. 8 [2003] of the State Council; "Interim Measures for the Supervision and Administration of State-owned Assets of Enterprises", No.378 [2003] of the State Council.

engage in their day-to-day business operation and management. Thus, they are barely involved in specific procurement activities of SOEs.

Figure 4.4: Structure of Relationships Between SOEs and Chinese Governments



Source: Yongheng Deng *et al.*, "Monetary and Fiscal Stimuli, Ownership Structure, and China's Housing Market" NBER Working Paper *No. 16871* (March 2011)

Chinese SOEs can be found in nearly all sectors of the economy, especially in the utilities sector, such as energy, electricity, communication, civil aviation and transport, which are considered as "strategically important industries" in China. They also have considerable power in fully competitive industries such as construction and manufacturing.

Currently, China is undergoing a new reform initiative under which SOEs are classified into two categories by function: publicly-oriented SOEs (gongyilei) and commercially-oriented

SOEs (shangyelei), with the former mainly operating in the utilities sector and dedicated to the public welfare and the later fully engaging in competitions for profit-seeking.[34] With the new classification system, the future regulations and guidelines on SOEs are envisaged to be following a dual-track approach.

1.4.2 The procurement of SOEs under Chinese Public Procurement Rules

There is a lack of unified regulation or guidance on the procurement of Chinese SOEs in general in China, especially under the Chinese fragmented regulatory system. The special characteristics of SOEs per se do not necessarily lead to the regulation of their procurement. As explained in section 1.3 of this chapter, the procurement by SOEs is outside the scope of the *GPL*, irrespective of whether SOEs use fiscal funds or not.

Regarding the *TL,* its application to SOEs is based on the type of the procurement projects and the involvement of tendering procedures. As Wang submitted, covering part of the procurement of SOEs appears to be a "by-product" of the *TL*.[35]

The *TL* **may** be applicable to any tendering procedures under Article 2. At the same time, it **must** apply in the procurement

[34] "Guiding Opinions of the Communist Party of China Central Committee and the State Council on Deepening the Reform of State-Owned Enterprises" (Sep. 13, 2015), http://www.gov.cn/zhengce/2015-09/13/content_2930377.htm (accessed June 10, 2018)
[35] P. Wang, *State Enterprises and Public Procurement in China*, PhD thesis, University of Nottingham (2004)

of works that fall within its mandatory coverage under Article 3. In reality, most of the works projects by SOEs are related to infrastructure projects and are in the utilities sectors and therefore are subject to the *TL* regulation.[36]

On the other hand, whether to apply the *TL* in the procurement of goods and services is more of a choice of Chinese SOEs. This is because first, these procurements are outside the mandatory scope of the *TL* and secondly, SOEs may simply use non-tendering procedures to opt out.[37]

In reality, Chinese SOEs, especially those controlled by the central government (central SOEs), tend to conduct procurements following their internal rules that are more flexible than the public procurement rules, especially the tendering rules, in many aspects. This may be explained by the fact that SOEs, as market players, need greater flexibility than the ordinary government purchasers in procurements, on account of the competitive circumstances where they operate. Nevertheless, such flexibility is hardly allowed under the current tendering rules, the priority objective of which tends to be anti-corruption and integrity. For instance, negotiation procedures of any kind are not permitted at all under the *TL*.

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[36] The coverage of the *TL* is defined in articles 2 and 3 of the *TL*. See section 1.3 of this chapter above.

[37] For more discussion about the application of the TL to the procurement of SOEs, see Wang, Bovis and Tu, fn. 10 *supra*, pp. 116-118

SOEs, in this context, seem entitled to procure in a flexible manner where appropriate. However, it does not mean that they are at full discretion. At present, most of the internal rules by SOEs are not accessible to the public. They are not subject to any auditing or other public oversight in the context of procurement. As explained in Chapters VII and VIII, on account of the nature of SOEs and the problems that arise due to lack of regulation, it is necessary to subject the procurement of SOEs to a certain extent of transparency and oversight.

Besides, the *MOFCOM Tendering Measures* should apply when SOEs are involved in purchasing mechanical and electrical products from abroad. Financial SOEs should observe the *Several Rules on Strengthening the Administration of Centralised Procurement of Financial SOEs* in conducting procurements, further complicating the regulatory framework.[38]

1.4.3 Policies and regulations by SASACs

The SASAC and the local branches, on behalf of the State, supervise most of the Chinese SOEs. According to the *Law of State-owned Assets in Enterprises*, procurement is not among the major issues on which the investor has rights in participation

[38] "Several Rules on Strengthening the Administration of Centralised Procurement of Financial SOEs", No. 209 [2001] of MOF, http://www.mofcom.gov.cn/aarticle/bh/200301/20030100063820.html (accessed May 15, 2018)

in policy decisions.[39] Thus, the SASAC and local branches do not directly engage in the procurement of SOEs. On the other hand, on account of the vast amount of expenditure by SOEs in procurements, and especially in light of the extensive incidents of abuse of power by SOEs officials and corruption being investigated, as will be discussed in Chapter VII, the SASAC arguably has interest and rights in regulating and supervising the procurement of SOEs to safeguard the state-assets.

In fact, the SASAC has been increasingly proactive in issuing policy documents to encourage normalising procurement by SOEs since 2010. Notably, in 2010 it issued a "Guiding Opinion on Addressing Major Problems in Procurement of Construction Works by Central SOEs", where it identified several irregularities that were commonly encountered in the procurement of SOEs. To resolve the identified problems, it further encouraged the central SOEs to establish internal rules governing the works tendering and procurement of supplies in line with legal norms. The SASAC seemingly has claimed the authority over regulating

[39] *Law of the People's Republic of China on State-owned Assets in Enterprises*, adopted on Oct. 28, 2008 and came into force on May 1st, 2009. According to Article 12, SASAC "…enjoy the return on assets, participation in policy decisions on major issues…", available at http://www.npc.gov.cn/englishnpc/Law/2011-02/15/content_1620615.htm (accessed July 19, 2018)

central SOEs' procurement through the "Guiding Opinions" and other policy documents.[40]

At the local level, most of the local governments do not regulate the procurement of SOEs in their jurisdictions directly. However, there are very a few localities where the governments empowered the local SASAC branches to adopt specific rules governing the procurement of their controlled SOEs. For instance, Wenzhou City adopted a series of local rules with the aim to comprehensively regulate the procurement of the local SOEs. [41] Fuzhou Municipal SASAC in 2018 adopted "Implementing Measures for Centralised Purchases of Bulk Supplies by Municipality-Invested SOEs (Trial)", with a view to regulating centralised purchases of the local SOEs to fight against corruption and to achieve value for money.[42]

Given the above, there are no unified guidance or regulatory rules adopted by the SASAC on the procurement of all SOEs at the moment. However, the recent moves arguably demonstrate

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[40] For instance, see "Opinion on the Decision-Making Mechanism of SOEs regarding Four Important Issues", No. 17 [2010] of the Chinese Communist Party Secretariat

[41] See the *Measures on Managing Procurement Agencies Database of Wenzhou City-owned or Handling Enterprises* (Trial), *Measures on Managing Procurement Evaluation Experts Database of Wenzhou City-owned or Handling Enterprises* (Trial) and specially *Measures on Handling Complaints Arising from Procurement of Wenzhou City-owned or Handling Enterprises* (Trial). The Chinese text is available at http://www.wzgqcgzs.cn/gzw/gqcg/gqcg_l.jsp?fid=20&page=1 (accessed July 19, 2018)

[42] Adopted on April 16th, 2018, available at http://www.fuzhou.gov.cn/zgfzzt/srsj/zfxxgkzl/gkml_31841/xzfggzhgfxwj/201804/t20180417_2182365.htm (accessed June 30, 2018)

the SASAC's incentive in adopting policies and consistent rules for SOEs to address the endemic irregularities in this respect. Moreover, as further suggested in Chapter VIII, China is undergoing a new round of SOEs reform and the SASAC is in the driving seat, which puts it at an advantageous position in playing a leading role in regulating the procurement of SOEs.

2 The Institutional Framework for Chinese Public Procurement: Complication and Fragmentation

As explained in section 1.1 above, China has two sets of laws governing public procurement. The parallel operation and even the "duel" between the *GPL* and *TL* (as well as their implementing regulations and rules) can be mainly boiled down to the underlying fragmented public procurement governance.

There are a number of central and local government agencies that are involved in supervising and regulating public procurement in China. The "major players" are the NDRC and the MOF. Historically, the NDRC drafted the *TL* and is the "guardian" of the *TL.* It coordinates the relevant ministries in issuing policies for tendering and supervises large scale infrastructure projects.[43] The MOF, as the "guardian" of the *GPL,*

[43] The State Council delegates the NDRC to play the leading role, as the general coordinator, in drafting policies and regulations on tendering. In

is the supreme regulator of government procurement activities. [44] Inconsistencies are further found among the government agencies within the tendering and the government procurement system, which particularly exacerbate the fragmented and complicated institutional framework in this area.

It is observed that various ministries and government agencies make strenuous and continuous efforts to build up their regulatory territory on public procurement while coveting others.[45] The "turf battle"[46] between NDRC and MOF for the leading position of regulating Chinese public procurement not only resulted in the co-existence of the *TL* and *GPL* but also led to the conflicts of implementing rules at various levels.[47] NDRC and MOF are often competitive in adopting rules on many issues, for instance, the bid evaluation committee, designated media for disclosure and publicity, challenge and review proceedings, public-private partnership regulation, etc. Developing rules

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reality, it has the authority to determine the scope of compulsory tendering projects, thresholds for tendering, the designated media to publish solicitations and award notices, etc.

[44] Besides, MOFCOM has been until now managing and regulating the procurement of imported mechanical and electrical products by government agencies and Chinese SOEs.

[45] P. Wang, C. H. Bovis and X. Tu, fn. 10 *supra*, pp.103-104. For more analysis about the fragmented institutional framework for public procurement in China, see D. J. Mitterhoff, "The Four into One Platform: New Reform Initiatives Compound China's Dissected Public Procurement Governance" (2012) *University of Maryland Legal Studies Research Paper* No. 2012-43; P. Wang, fn. 7 *supra,* at p.301

[46] D. J. Mitterhoff, "China - Waiting for Leviathan: A Note on Modern Wo- Er Trading Co Ltd v Ministry of Finance of the People's Republic of China" (2013) 3 *P.P.L.R.* NA47

[47] For more information about the evolvement and adoption of the two national laws, see D. J. Mitterhoff, fn. 45 *supra*; P. Wang, fn. 7 *supra*, at p.301

have arguably become a method for them to guard the regulatory fortress and further to expand their power. The inconsistencies and tensions impose high compliance burdens on the practitioners.

The deeply fragmented institutional framework, derived from the "turf battle" between the relevant government agencies, mainly between the NDRC and MOF, has arguably become one of the most significant obstacles that debilitate China to improve and harmonise the public procurement regulation. The governance segmentation has also impeded the negotiation for China's accession to the WTO GPA.[48]

However, it would be unfair to say the Chinese government has neglected the "dysfunction". In fact, successive attempts have been made to address the fragmentation, which however failed. In 2005, an inter-ministerial coordination mechanism was set up covering the then eleventh ministries, including the MOF and MOFCOM, with the NDRC taking the lead. The coordination mechanism was intended to address the conflicts regarding administrative supervision on tendering activities between different government ministries, thus promoting the

[48] P. Wang, "China's Accession to the WTO Government Procurement Agreement- Challenges and the Way Forward", (2009) 12 *Journal of International Economic Law*, pp.663-706

consistency in implementing and enforcing tendering rules.[49] Despite the inspiring goal, the actual work of the coordination mechanism was nothing more than two scheduled liaison meetings and an annual summit every year.[50] Undoubtedly, the coordination mechanism did not make much difference to the fragmented framework.

Enacting the State Council regulations for implementing the *TL* and *GPL* was considered another opportunity to harmonise the two laws, thus diffusing the tensions amongst different government agencies. With the promulgation of the *IRTL* and *IRGPL*, albeit the efforts made in addressing the coverage of the national laws, the hope of "harmonisation" failed short again.

More recently, a new reform-public resources trading platform reform- has swept across the country. Spearheaded by the NDRC, the reform was intended to regroup the splintered regulatory regimes on public procurement into a centralised administrative structure. The basic idea is to integrate construction tendering, government procurement, transfer of land-use rights and mining rights into one single management platform, called the "Public Resources Trading Platform".[51] The

[49] See "Interim Measure on Inter-Ministerial Coordination Mechanism on Tendering Proceedings" NDRC Document [2005] No.1282
[50] *Ibid.* Articles 6 and 10. See also Wang, Bovis and Tu, fn. 10 *supra,* pp.103-104
[51] See "Plan for the Institutional Restructuring of the State Council and Transformation of Functions Thereof", State Council (March 10, 2013) http://www.lawinfochina.com/display.aspx?lib=law&id=13554&CGid= (accessed July 30, 2018)

public resources trading centres were set up at various levels to carry out the reform and administer these Platforms.

In 2015, NDRC, as the initiator, coordinating other 15 relevant ministries promulgated the *Interim Measures for the Administration of Public Resources Trading Platforms* to regulate the Platforms operation specifically.[52] As of October 2018, as many as 623 trading platforms are established at various levels in China, and a national Platform is also in place that shares information with and provides access to all local Platforms.[53] It is plausible to see that the fragmented institutional framework for public procurement has been taken into serious consideration and substantive efforts have continuously been devoted to this.

The reform is still underway, and the results remain to be seen. However, the author argues that the outcome is less likely to be fruitful for several reasons. Firstly, the legality of the platform reform remains in question. As aforementioned, "public resources trading centres" were set up to administer the platforms, becoming the actual regulator and supervisor of the "centralised" activities. To that end, many local centralised

[52] *Interim Measures on Management of Public Resources Exchange Platform*, enacted on June 24, 2016 and effectuated on August 1st, 2016, http://www.sdpc.gov.cn/zcfb/zcfbl/201606/W020160630390343326928.pdf (accessed July 30, 2018)
[53] The access to the national platform is http://www.ggzy.gov.cn/ (accessed Sep 23, 2018)

purchasing agencies (CPAs) have lost their independent legal status and have been merged into the new centres, which is the case of new centres in Hangzhou and Guangzhou municipalities.[54]

Nevertheless, such a merger is in breach of the *GPL* in that CPAs must be independent legal entities.[55] Besides, the new centres being the supervisor may violate the *GPL* which explicitly designates the MOF and its branches as the supreme supervisor on all government procurement.[56] Since the *Interim Measures for the Administration of Public Resources Trading Platforms* are ministerial rules enacted by NDRC, sitting at the fourth level of Chinese legislation, its provisions must not contradict those under the *GPL*.

More importantly, the reform cannot resolve the "turf battle" among different ministries. While NDRC plays the leading role in the reform, other ministries with vested interests, especially MOF, who are less willing to "hand in" their regulatory territory, tend to quietly resist implementing the reform.[57]

After years of inputs, there is still no sign of harmonising the two sets of procurement laws. From the author's perspective,

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[54] See http://www.hzctc.cn/NewsShow/Home?id=6197&ModuleID=8&AreadID=72; http://www.gzggzy.cn/cms/wz/view/index/layout2/zxwz.jsp?siteId=1&channelId=3 (accessed Sep 23, 2018)

[55] *The IRGPL*, Art. 17

[56] The *GPL*, Art.13

[57] For more analysis, see D. J. Mitterhoff, fn. 45 *supra*, p.43

the Platform reform may end as another failed attempt to integrate Chinese public procurement regulatory system, as the institutional tensions remains unsolved, and the experience from the earlier Coordination Mechanism suggests that NDRC is unable to address the segmentation on its own.

2.1 The Tendering System: Decentralised Administration

Within the tendering system, while NDRC is the "guardian" of the *TL*, the enforcement of the rules and supervision on tendering activities are further dissected and bestowed to other several competent ministries within their respective functions.[58] The ministries mainly include: Ministry of Housing and Urban and Rural Construction (MOHURD, for the supervision on general construction procurements), the Ministry of Transportation (MOT, for the supervision on procurement of national roads and highways), Ministry of Industry and Information Technology (MIIT, for the supervision on procurement of communication and IT infrastructure projects),

[58] The *TL* itself does not address the issue of the supervisory authority over tendering activities under the Law, which was left to the State Council. Arguably based on the compromises between NDRC and other ministries, the State Council endorsed a decentralised regulatory structure. In 2000, the State Council issued the "The Opinion on the Division of Administrative Supervision on Tendering Activities by Relevant Ministries under the State Council" (May 4, 2000, available at http://www.gov.cn/gongbao/content/2000/content_60239.htm (accessed Sep 27, 2018). According to the "Opinions", the supervision and enforcement of tendering activities are divided amongst the competent ministries and for Water Resources, Transportation, National Rails, Civil Aviation Administration, Industry and Information Technology and Construction.

Ministry of Water Resources (for the waterworks projects), National Railways (for the supervision on construction and maintenance of the national rail system), and Civil Aviation Administration (for the management of the airports).

They are allowed to formulate ministerial rules to implement the *TL* and the *IRTL* in specific aspects. For instance, MIIT in 2014 enacted *the Measures for the Administration of Tendering in Communications Construction Projects.*[59] It is not surprising that the "fortress mentality" also takes place under the tendering system amongst the relevant ministries in self-regulating tendering activities within their fields.[60]

2.2 The Government Procurement System: Separation of Supervision and Procurement Functions

The MOF is the "guardian" of the *GPL*. It and its local branches are tasked with supervising government procurement at the central and local level respectively.[61] The duties of the finance departments mainly include: (i) reviewing and approving of

[59] No. 27 [2014] of MIIT, Chinese text available at http://www.miit.gov.cn/n1146295/n1146557/n1146624/c3554792/content.html (accessed June 20, 2018)

[60] It was said that during the drafting process of the *TL*, efforts were made in setting up a higher-level office to supervise all tendering activities but failed in the end due to the conflicts among the relevant government ministries. For the history, see F. Cao, "From Tendering Law to the Public Procurement Law" in S. Arrowsmith and M. Trybus (eds.) *Public Procurement: The Continuing Revolution* (Kluwer Law International, London, 2003)

[61] *The GPL,* Art.13

procurement budgets; (ii) drafting the centralised procurement catalogues and determining the thresholds for open tendering; (iii) designating official media for information publication; (iv); supervising government procurement activities and the operation of centralised purchasing agencies (CPAs); (v) hearing and reviewing complaints by suppliers; (vi) issuing government procurement policies and rules, and etc.[62] MOF has the exclusive authority to approve new methods other than those prescribed under the *GPL.*

Article 60 of the *GPL* establishes the principle that supervision and procurement functions must be separate by stating that supervision authorities (MOF and its local branches) shall not set up CPAs or engage in procurement activities. It follows that in centralised procurements, the roles of supervisor and purchaser should be separated and the involvement of purchaser, namely the CPAs is necessary.[63] In practice, however, as pointed out later, it is not uncommon that the local finance branches often "trespass on" the duties of the CPAs and intervene centralised purchases as discussed in Chapter V.

[62] *The GPL,* Arts 7, 11, 13, 26, 33, 55-58, 59, 65; "Notice of the State Council Office on Issuing the Implementation Plan to Fully Promote the Government Procurement System Amongst the Central Government Agencies", No. 53 [2002]

[63] As explained in section 1.2 of this chapter, centralised purchases of the items listed on centralised procurement catalogues must be carried out be CPAs under Article 7 of the *GPL.*

CPAs are non-profitable public institutions with the independent legal personality, set up in accordance with the *GPL*. [64] They are designated to executing centralised procurement, i.e. operating framework agreements, on behalf of the same-level government agencies. Most if not all the CPAs are financed directly from the fiscal budget and are staffed by ordinary civil servants who need not have procurement qualifications.[65] As discussed in Chapter V below, procurement officers in CPAs are more concerned about procedural compliance, rather than achieving the best value of procurement for government agencies.

There is often a CPA at and above the municipal level of government in each administrative area, following the fiscal system.[66] Therefore, within a province, the provincial-level CPA

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[64] *The GPL* Art.16, 18; *the IRGPL* Art. 12

[65] There are several cases where the CPAs are self-supporting, with their expenses paid by their earnings. C. Li, "Talking About Advantages and Disadvantages of the Setup of Centralised Procurement Agencies", *China Finance*, (Oct 17, 2007), available at http://finance.sina.com.cn/review/yjfx/20071017/10094069746.shtml (accessed May 27 2018). Regarding the organisational forms of CPAs, according to an OECD report, the most common organisational forms in the EU are non-profit limited companies and independent agencies that are owned and controlled by the state and public bodies with legal personality. See OECD (2011), "Centralised Purchasing Systems in the European Union", SIGMA Papers, No. 47, OECD Publishing, Paris.

[66] The *GPL* does not prescribe whether governments below the municipal level, i.e. county governments, should establish CPAs. One main reason may be that the scale of procurement at such level is often small and the procurement capacity tends to be limited. Therefore, centralised procurement is not necessarily needed. However, no rules exist to prevent the governments below the municipal level from forming CPAs according to their needs. See http://www.ccgp.gov.cn/zcfg/zswd/zfcgdsr/201310/t20131029_3587728.htm (accessed Dec. 12, 2018)

often co-exists with the CPAs established by different municipal governments.

At the central level, Central Government Procurement Centre (CGPC) is the central CPA, which is tasked with centralised purchases on behalf of general central government agencies. Apart from it, there are additional five CPAs established by the competent central ministries and departments to conduct their respective departmental centralised procurement.[67] It is argued that the co-existence of as many as six CPAs at the same level, who are all based in Beijing, may artificially dissect the procurement market and thus dilute the benefits of centralised procurement. Figure 4.5 provides the structure of CPAs in Chinese government procurement.

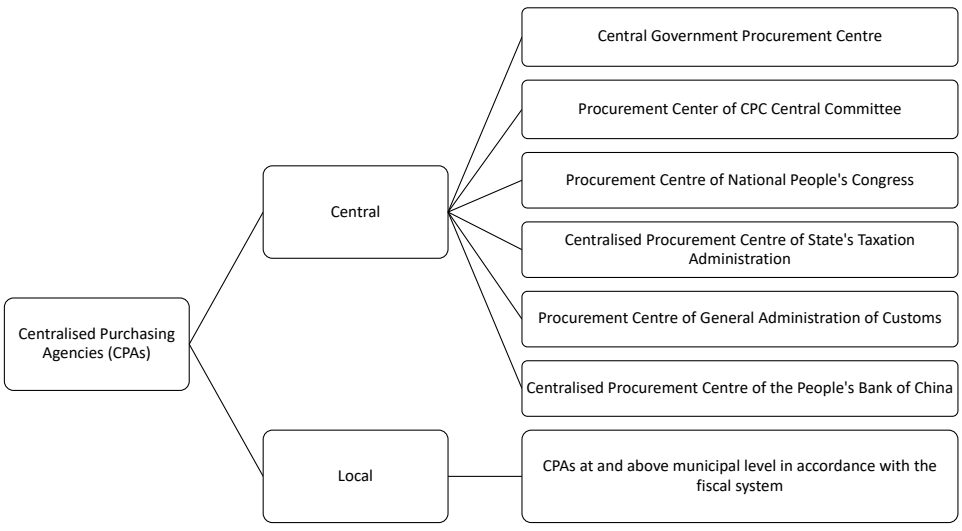
There is a lack of consistency and coherence in administrating CPAs. It is observed that CPAs in different areas and at different levels are operated in various models and are subordinate to different leading authorities.[68] Their leading

[67] The CGPC undertakes centralised procurement for general central government agencies, available at http://www.zycg.gov.cn/english.html (accessed May 27, 2018) The other five CPAs at the central level are the PCCPC established by the CPC, PCNPC conducting procurement for the NPC Standing Committee, CPCSAT established by the State Administration of Taxation, PCGAC set up by the General Administration of Customs, and CPCPBC established by the People's Bank of China.

[68] C. Li, "Talking About Advantages and Disadvantages of the Setup of Centralised Procurement Agencies", (Oct. 17, 2007), *China Finance*, available at http://finance.sina.com.cn/review/yjfx/20071017/10094069746.shtml (accessed Aug 20, 2018)

authorities could be the local Bureau of Government Offices Administration, the local finance department, the local commerce department and the local SASAC branch, and etc.[69] As will be analysed in Chapter , such management morass has created barriers for information sharing, talents exchange, standardisation of procurement language and inconsistent implementation of rules. More importantly, having the local finance departments as the "manager" of the CPAs particularly violates the principle of separation under the *GPL.* There is, therefore, a need to rationalise the management of CPAs to improve centralised government procurement, including framework agreements.

Figure 4.5 Centralised Procurement Agencies in Chinese Government Procurement



[69] For instance, the Tianjin municipal CPA and Gansu provincial CPA are not independent from the finance department, which is in breach of the *GPL*. In Hubei and Neimenggu, the provincial CPAs are led by the Office of Provincial Government. In Beijing, the municipal CPA is affiliated to the SASAC.

3 Brief View on Framework Agreements in Chinese Public Procurement

Framework agreements have been widely used by government agencies, public institutions as well as SOEs in China. In the absence of a uniform definition, a number of terms are used to refer to framework agreements and the similar arrangements, including framework agreements (kuangjia Xieyi), designated-provider procurement (Dingdian Caigou), agreement procurement (Xieyi Gonghuo), agreement and designated-provider procurement (Xieyi Gonghuo) and framework tendering (Kuangjia Zhaobiao). Framework agreements will be used as a generic term in this research.

3.1 The Evolvement of Framework Agreements in Chinese Government Procurement

Framework agreements have been part of government procurement in China for around two decades and are still widely used today. The evolvement of their use and regulation reflects the difficult government procurement reform embarked on by the Chinese government.

In the mid-1990s, China launched the government procurement reform, culminating in the enactment of the *GPL*

in 2002. Prior to the reform, government agencies had full discretion in procurement. One of the main goals of the government procurement reform was to strengthen control over government expenditure and combat corruption through centralising procurement. The initial centralised purchasing agencies were created then for purchasing common-use items. The centralisation caused push-back by government agencies, who had been deprived of the procurement discretion and also led to the excessive workload for the then CPAs, who had little experience and skills. The inefficiency and burden in strictly applying tendering procedures, which were the norm methods at that time, further added to the resistance to the reform.

On the other hand, with the spread of computers, purchases of IT items became a significant part of government procurement, like the rest of the world. In light of the increasing demands governmentwide for IT products and given the rapid updates of these items, more expedient procurement process and shorter lead-time were required, which posed particular challenges to the then CPAs. The long procurement cycle of the "traditional" methods, especially tendering procedures, had been unable to meet the above needs.

Against this context, the finance departments informally introduced framework agreements for several purposes.[70] They were, first, intended to confer certain extent of discretion/flexibility for government agencies, thus to ease their resistance to the centralisation reform. Secondly, framework agreements were envisaged to improve administrative efficiency, thus to satisfy the extensive requirements for IT purchases and to liberalise the then CPAs.

It is argued that framework agreements played an important role in balancing the interest of stakeholders and helped pave the way for the reform.[71] They provided government agencies with a particular gateway to convenient and efficient purchases of the common-use items, therefore being rapidly accepted by all levels of governments.

In 2002, MOF issued the "Notice on Procurement of Computers and Printers by Central Government Agencies" and "Government Procurement Plan of Central Government Agencies in 2002", whereby three pilot framework agreements projects were initiated to procure computers and printers for

[70] For details about the historical evolvement of framework agreements in Chinese government procurement, see X. Yan and X. Wu (ed.), *Framework Agreement and Its Price Mechanism Research* (in Chinese), (China Financial and Economic Publishing House, 2010); A. Hao and J. Feng, "The Dialectical Analysis of the History and Future of Framework Agreements", *Chinese Government Procurement Newspaper* (Jan. 15, 2013)

[71] Three participants in the interview have confirmed this.

central government agencies.[72] The success of the projects was based mainly on the positive attempts made by many local governments on framework agreements.[73] For instance, early in 1996, Changsha had issued local rules instructing the use of framework agreements.[74] Also, Hebei Province and Nanjing Municipality in Jiangsu Province also adopted measures to guide the use of framework agreements.[75]

The enactment of *GPL* in 2002 is a turning point for the development of framework agreements in Chinese government procurement. On the one hand, the use of framework agreements has seen a remarkable increase at both central and local levels. Their popularity can be demonstrated by the expanding coverage and increasing amount of purchases of framework agreements. For instance, framework agreements at the central level in 2002 covered only two categories of products, including computers and printers. In 2008, the products

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[72] No. 13 and No. 17 [2002] of the MOF, available at http://law.lawtime.cn/d640221645315.html; http://www.mof.gov.cn/zhengwuxinxi/caizhengwengao/caizhengbuwengao2002/caizhengbuwengao200211/200805/t20080519_21161.html (accessed Sep 20, 2018)

[73] X. Yan and X. Wu (ed.), fn. 70 *supra*, at p.14

[74] For instance, see "Interim Measures on Designated Procurement of Printing Services for Changsha Municipal Government Organs and Institutions" [1999] of Changsha Finance Bureau

[75] For instance, see *Interim Measures on Designated Procurement of Office Supplies for Provincial Government Organs and Institutions*, No. 1 [2001] of Hebei Provincial Finance Department; "Notice on Issuing the Interim Measures for Administration in Government Procurement of Conference Services for Nanjing Municipal Government Agencies and Institutions in 2002" No.284 [2002] of Nanjing Finance Bureau (in Chinese)

covered by the framework agreements increased to 49 categories, comprising 189 sub-categories.[76] At the local level, the use of frameworks can be found in almost all provinces at various levels.

At present, framework agreements are still prevalently used by the Chinese governments nationwide. However, there are no relevant official statistics, such as the size of the procurements subject to framework agreements and their proportion out of the total government procurement expenditure.[77] The scant information, in turn, may reflect the transparency flaw regarding Chinese government procurement.

On the other hand, however, the regulation has been far behind of the practice. To date, the national law and the secondary regulation- the *GPL* and *IRGPL*-do not mention framework agreements at all. In reality, nevertheless, several line ministries (at the central level) and a number of local governments have adopted rules governing the use of frameworks in their own jurisdictions, which are at the fourth level of Chinese legislation. Regarding the ministerial rules, for instance, the State Administration of Taxation issued *Measures*

[76] X. Yan and X. Wu, fn. 70 *supra*, at p.14

[77] Albano and Nicholas highlight that the lack of information and data on framework agreements is a common issue in many jurisdictions in G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement*, (Cambridge University Press, 2016), p.124.

on Managing Government Procurement Through Framework Agreements in State Administration of Taxation System in 2007.[78]

In terms of the local rules, there is no database that includes all local rules on government procurement, *a fortiori* those concerning framework agreements. After an extensive search, it is observed that among 31 provincial-level administrative divisions that are within Chinese government procurement system, 27 provinces/municipalities have adopted rules at the provincial level, to a different extent, governing the use of framework agreements. It is interesting to note that Sichuan, Henan and Hainan provinces, in light of the practical problems in using frameworks, have decided to withdraw their use at the provincial level, whilst their use are still allowed below the provincial level.[79] The other four provinces have issued informal guidance instructing the use of framework agreements, instead of formal local rules. The figure 4.6 below illustrates the status

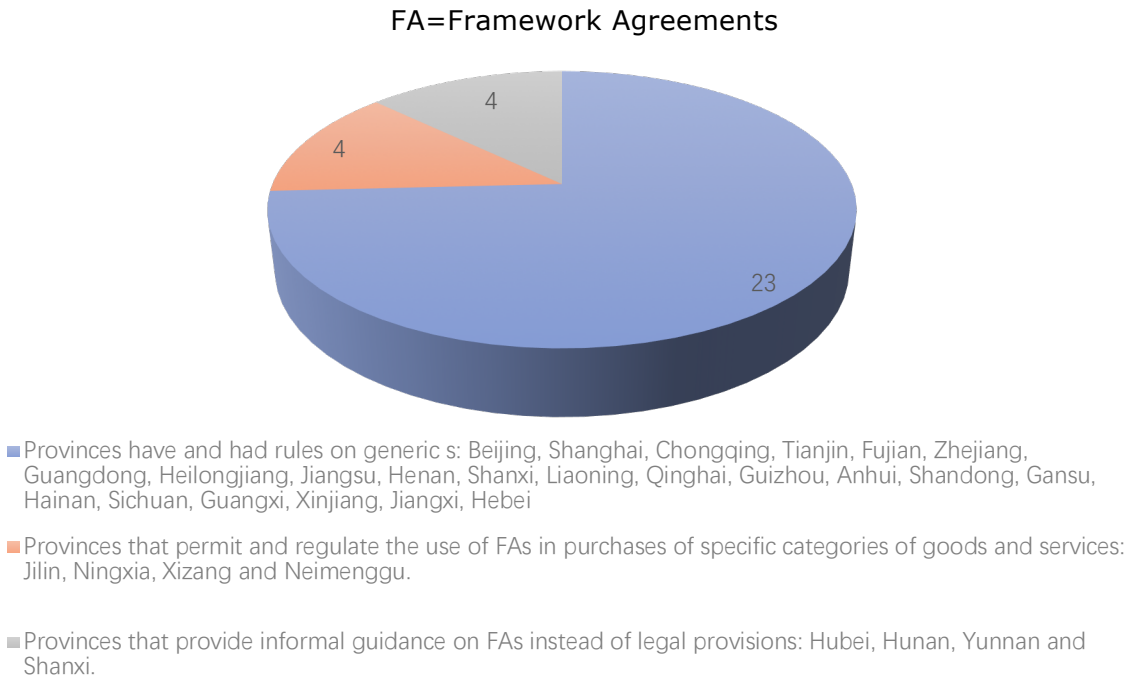
[78] No.73 [2007] of the State Administration of Taxation, available at http://www.ccgp.gov.cn/zcfg/bwfile/201310/t20131029_3587701.htm (accessed May 12, 2018)

[79] Sichuan, Henan and Hainan provinces decided to withdraw the use of framework agreements in government procurement at their provincial level in 2014, 2016 and 2018 respectively and to use electronic marketplaces to purchase those covered by framework agreements. See http://www.scpcfe.cn/jcsjc/tabid/1485/ctl/InfoDetail/InfoID/24433/mid/2706/Default.aspx?ContainerSrc=[G]Containers%2f_default%2fNo+Container; http://www.xinhuanet.com/fortune/2017-03/21/c_1120664376.htm; http://news.sina.com.cn/c/2018-08-05/doc-ihhhczfa6593413.shtml (accessed May 12, 2018)

of regulating framework agreements by Chinese provincial governments.[80]

[80] It is reiterated that there are no official statistics regarding the practice and regulation of Framework agreements in China. The chart is based on the data collected by the author after extensive research. As illustrated in the chart, 23 provinces/municipalities, i.e. Beijing and Shanghai municipalities have or used to have rules on generic Framework agreements. For instance, see "Notices on Issuing Interim Measures on Administrating Beijing Municipal Framework Agreements and Designated Procurement of Services" No.362 [2010], available at http://www.bgpc.gov.cn/news/news/news_id/118 (in Chinese); "Notices on Issuing Measures on Administrating Electronic Framework Agreements in Shanghai Municipality" No. 4 [2017], available at https://www.czj.sh.gov.cn/zys_8908/zcfg_8983/zcfb_8985/zfcg_9033/201706/t20170605_175448.shtml (in Chinese, accessed May 13, 2018)); "Notices of Municipal Bureau of Finance on Issuing Interim Measures of Administrating Chongqing Municipal Framework Agreements Electronic Transactions Platforms" No. 38 [2012], available at http://www.gec123.com/providerList.action (in Chinese, accessed May 12, 2018); *Measures on Framework Agreements and Designated Procurement of Tianjin Municipal Budget Units*, No. 3 [2008], available at http://www.tjgpc.gov.cn/webInfo/getWebInfoByPkWebInfoId.do?pkWebInfoId=23AA77FB-4EE2-444A-B003-C98222BF7ACB (in Chinese, accessed May 13, 2018); *Interim Measures of Fujian Provincial Department of Finance on Administrating Framework and Designated Procurement in Fujian Provincial Government Procurement*, No.3 [2005], available at http://law892.infoeach.com/view-ODkyfDc2NjE1.html (in Chinese, accessed May 13, 2018); "Notices of Zhejiang Provincial Department of Finance on Issuing Measures of Implementing Framework Agreement in Government Procurement (Trial)" No.32 [2003], available at http://www.zjzfcg.gov.cn/detailPage?type=2&ID=250185 (in Chinese, accessed May 13, 2018); "Notices of Provincial Finance Department on Issuing Measures of Administrating Framework Agreements in Heilongjiang Provincial Government Procurement" No.12 [2015], available at http://218.8.25.229:8003/xwzs!queryOneXwxxqx.action?xwbh=AAAHa1AABAAG3XSAAT_525law (in Chinese, accessed May 12, 2018), and etc. Four provinces chose to permit and regulate framework agreements in purchases of specific goods and services. For instance, Jilin Province provides rules on framework agreements specifically for official vehicles services and office automation equipment rather than generic framework agreements. See "Notices on Issues Concerning Designated Procurement of Jilin Provincial Office Vehicles" No. 1042 [2014], available at http://zcc.jlart.edu.cn/View.Asp?Class_Id=6&id=59 (in Chinese, accessed May 12, 2018). Ningxia also adopted "Notice on Implementing Framework Agreements in Government Procurement of Partial Office Automation Equipment and Furniture" No. 105 [2006]. In the other provinces, including Hubei, Hunan, Yunnan and Shanxi, the local governments tend to issue informal guidance/ plans/ manuals, instead of formal legal rules to govern framework agreements. For instance, see Hubei provincial finance department published the "Practical Manual of Using Framework Agreements in Government Procurement" (2014) http://www.hbdofcom.gov.cn/CMShbsw/201409/201409021051049.pdf (accessed May 12, 2018). Hunan Province will issue guidance through annual

Figure 4.6 Status of Regulation on Framewok Agreements by the 31 Local Governments at Provincial Level in China



The existence of numerous local rules can arguably demonstrate the nationwide take-up of framework agreements in practice. Despite that, however, due to the silence of the national law and regulation on this issue, these rules may be considered to have overstepped their legislative mandate and thus be invalid. Apart from the laws and regulations, in reality, MOF also adopted various policy circulars that mentioned framework agreements. Although these documents are well respected in practice, they do not form the legal basis for the use of framework agreements. As discussed in Chapter V,

"Notices" instructing the use of framework agreements. See "Notices of Hunan Provincial Department of Finance on Issues Concerning Framework Agreement in 2010 for the Use of Provincial Administrative Agencies and Institutions" No. 3 [2010].

frameworks lack an adequate legal basis in Chinese government procurement and their legality remains at question.

Table 4.2 Regulatory Status of Framework Agreements in Chinese Public Procurement Regime

	1st level: national law	2nd level: State Council Regulations	4th level: ministerial rules	4th Level: local Rules adopted by the local governments
Government Procurement System	*GPL*: No	*IRGPL*: NO	Yes	Numerous
Tendering System	*TL*: No	*IRTL*: NO	Yes	

3.2 Practice and Regulations of Framework Agreements in the Chinese Tendering System

There are no rules regulating framework agreements under the *TL* and *IRTL*. The absence makes sense because framework agreements are considered more appropriate for repeated purchases of standard goods and straight services that are commonly used, whereas the *TL*, as earlier explained, mainly applies in works procurements. The tendering rules may apply where tendering procedures are used to conclude framework agreements. This also means they will be excluded if non-tendering procedures are deployed at the first stage.

Regarding the ministerial rules, a similar term of framework agreements- "centralised tendering" (jizhong zhaobiao)-is seen

in the *Measures on Administrating Communication Construction Projects Through Tendering Proceedings,* adopted by MIIT.[81] The "Measures" allow procuring entities to use "centralised tendering" in the procurement of communication works and related goods and services. According to the practitioners, centralised tendering is commonly used in the procurement of certain works in the communication sector for improved efficiency, the requirement on which tends to be consistent and stable, such as laying cables and maintenance of communication base stations. The "Measures" recognises such benefits and reflects the practice.[82]

3.2.1 Regulating framework agreements by Chinese SOEs

It is observed that Chinese SOEs have been using framework agreements for long, mainly in purchasing goods and services that are frequently needed.[83] As explained in section 1.2 of this chapter, most procurement of works by Chinese SOEs is subject to the *TL*, whereas their procurement of supplies and services remains a regulatory gap, beyond the scope of the current

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[81] *Measures on Administrating Communication Construction Projects Through Tendering Proceedings,* No.27 [2014] of MIIT, Arts. 22-24, 35, 38, 42 and 47, available at http://www.miitcntc.org.cn/news_detail9/newsId=7ef293ab-4128-45b6-8e89-3cea24e2d2f2.html (accessed May 16, 2018)

[82] "Understanding Measures on Administrating Communication Construction Projects Through Tendering Proceedings" (2014) China Bidding 18, pp11-12

[83] P. Wang, C. Bovis and X. Tu, fn. 10 *supra.*

public procurement rules.[84] SOEs, especially those central ones, tend to adopt their own rules to self-regulate their supplies and services acquisitions.

Similarly, many large SOEs are observed to have adopted internal rules to govern their use of framework agreements. For instance, China Petrochemical Corporation (Sinopec), set up the "Sinopec Rules Administrating Framework Agreements Procurement".[85] However, most of the internal rules are not assessible to the public. Due to the regulatory gap regarding SOEs' procurement of goods and services, as explained above in section 1.4.2 of this chapter, transparency requirements and oversight are generally absent in framework agreements by SOEs, which may facilitate corruption and other irregularities.

Though uncommon, there are also cases where SOEs may use framework agreements to procure works. Where they engage in communication works as identified above, they may need to comply with the *Measures on Administrating Communication Construction Projects Through Tendering Proceedings*.[86]

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[84] As explained, the *GPL* does not apply because the procurement of SOEs is not considered "government procurement" under the *GPL*.

[85] The Chinese text is available at http://wenku.baidu.com/view/97c45e92bb4cf7ec4bfed04b.html?re=view (accessed May 15, 2018). The rules are claimed to have been modified, whereas the new version is not available to the public.

[86] *Measures on Administrating Communication Construction Projects Through Tendering Proceedings*, No.27 [2014] of MIIT

4 Summary

Over the last three decades, China has made significant progress in establishing a modern and structured public procurement system, which however remains fragmented and inconsistent. Unlike most of the procurement systems that have a unified framework to regulate all public procurement activities, China has two parallel sets of laws that govern public procurement: the *GPL* and *TL*. Rather than synergism, the two laws co-exist uneasily with overlaps and clashes in many aspects, such as the coverage. The scope of coverage of the two laws is mainly defined on the basis of the type of the subject matter (works or goods and services) and the procurement method employed (tendering or non-tendering). One side-effect of the two-dimensional laws is that the procurement of goods and services by Chinese SOEs and their works projects based on non-tendering procedures is not regulated at all.

The root cause of the inconsistent legal framework is the fragmented institutional framework for public procurement behind. There is a myriad of ministries and government agencies involved in regulating public procurement, who are all contending for power. According to Wang *et al*, the current fractured system is "the result of compromises among powerful central government ministries reluctant to give up their jurisdiction accompanied by the argument that the line

ministries know their business better", especially between NDRC and MOF for the leading regulatory of public procurement.[87]

The fragmented regulatory framework also inherited in the context of framework agreements. They made debut early in Chinese public procurement and continue being widely used by government agencies as well as Chinese SOEs. In government procurement, nearly all provinces in China have or have had adopted local rules governing the use of frameworks in their own jurisdictions. In the procurement of SOEs, framework agreements are considered as an efficient and flexible procurement tool and thus are frequently employed by SOEs.

However, the regulation is far behind the practice. Until today, framework agreements are not mentioned at all in the Chinese primary or secondary public procurement laws and regulations-the *GPL*, *TL*, *IRGPL*, or *IRTL*-that are the legal base for all other rules implementing them. As discussed in Chapter V, in the absence of an adequate legal basis, the legal status of framework agreements in Chinese government procurement remains in question. Doubts are raised regarding the legality of the numerous local rules and ministerial rules relating to framework agreements remains in question.

Regarding framework agreements used by Chinese SOEs, since they are mainly used in procuring supplies and services,

[87] See Wang, Bovis and Tu, fn. 10 *supra*, at p.10

their use is currently outside the public procurement regulation. Large SOEs tend to conduct framework agreements following with their own internal rules, which, however, are mostly inaccessible to the public. As discussed in Chapters V and VI, a number of problems and challenges arise due to lack of regulation in the use of framework agreements, which caused a significant amount of public criticism.

Chapter V. The Use and Regulation of Framework Agreements in Chinese Government Procurement

1. Introduction

Framework agreements are prevalently used in Chinese government procurement and by SOEs, mainly in purchasing goods and services that are commonly needed. In the absence of unified guidance or regulation, as Chapter IV explained, the *modus operandi* of framework agreements in the two areas vary to some extent.[1]

Chapter V and VI will provide an insight into how framework agreements are taking place in the government procurement and by SOEs in China. The survey starts with examining how framework agreements are operated and then moves to analyse the legal issues and practical problems that may undermine the beneficial use of framework agreements. Given the paucity of relevant data in the public domain, especially in the procurement of SOEs, the author conducted semi-structured interviews, as explained in Chapter I, and the information obtained becomes part of the sources for the analysis.

[1] As explained in Ch. IV, "government procurement" and "public procurement" are distinguished in China, since the *Government Procurement Law* (GPL) adopts a narrow definition of "government procurement".

2. The Definition and Coverage of Framework Agreements

There is no uniform definition of framework agreements in Chinese government procurement. Various terms are used to refer to framework agreements (and similar arrangements), as provided above in Chapter VI. The term "framework agreements" is more commonly seen in practice.

In 2013, Ministry of Finance (MOF), the supreme regulator of Chinese government procurement, issued "Government Procurement Basic Operation Data Specification", where it for the first time expressly described framework agreements.[2] According to the "Specification", framework agreements refer to:

> "An implementing form to centrally select multiple suppliers and to determine the terms and conditions of future contracts, in respect of price, services, etc. through open tendering and other methods, which will be consolidated in the form of agreement. Within the validity of the agreement, procuring entities are free to choose from the suppliers admitted and the products they offer. It mainly applies to procurements of common-use and relatively standard products, which are readily available in the market and are expected to be frequently needed."[3]

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[2] For the regulatory status of framework agreements in Chinese government procurement, see Chapter IV above and section 6.1 of this chapter.

[3] See MOF "The Master Plan on Establishing National Government Procurement Management and Transaction System" and "Government

It should be noted that the purpose of the description is for data collection, not for providing a legal definition of framework agreements, let alone authorising their use. Although the "Specification" is a policy circular only, which, in principle, has no legal force, it in reality is well respected, at least among the local finance branches. Therefore, the description is arguably able to reflect the practice of framework agreements in government procurement.

Based on the description and the practice, framework agreements in Chinese government procurement operate close to what are known as "framework agreements" in the EU and UNCITRAL *Model Law*. [4] A framework agreement is a procurement mechanism with two stages of operations: A first stage used to select more than one supplier to award a master agreement that sets out the main terms and conditions for future contracts and a second stage used to order under the agreement when a specific requirement arises.

In Chinese government procurement, framework agreements are used for centralised procurements, as explained

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Procurement Basic Operation Data Specifications"', No. 18 [2013]. The Chinese text is "指通过招标采购等方式，统一确定采购项目中标供应商范围及中标产品的价格和服务条件，并以协议书形式固定，由采购人在协议有效期内自主选择供应商及中标产品的一种实施形式。主要适用于规格及标准相对统一，品牌较多，日常采购频繁的通用类产品", available at http://www.ccgp.gov.cn/zcfg/mof/201310/t20131029_3587691.htm (accessed Aug 1, 2018)

[4] See Ch. III above.

below,[5] and are therefore multi-supplier and multi-user type, as per the classifications in Chapter II. They, in most cases if not all, are closed, which means new suppliers are not allowed to join the frameworks after they are concluded. Most framework agreements are binding on both demand and supply sides. Therefore, once a framework agreement is in place, the procuring entities are bound to purchase within the frameworks and the suppliers are obligatory to supply as requested.

2.1. Differentiating Framework Agreements with Related Notions in Chinese Government Procurement

In Chinese government procurement, several procurement techniques are also frequently used for centralised purchases, apart from framework agreements, which mainly include Bulk Centralised Procurement and Electronic Marketplace. This section attempts to clarify their connection and differences with frameworks.

[5] Albano and Nicholas use centralised framework agreements to refer to framework agreements that are established by centralised purchasing bodies and used in centralised procurements. See G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (2016 Cambridge University Press), p.124

- **Framework Agreements vs. Bulk Centralised Procurements**

Bulk centralised procurement (Piliang Jizhong Caigou)[6] is a technique used for centralised purchases of common-use and standard goods. Article 24 of the *IRGPL* provides the legal basis for the use of BCPs by stating that, "Items that are listed on the centralised procurement catalogue shall be procured through BCPs where appropriate, except for urgent purchases of low-value goods that are not frequently needed or for purchases of services and works with special requirements".

It is interesting to note that in the original draft *IRGPL*, there was a provision that authorised the use of framework agreements, but it was removed from the final version. In the meantime, a new article was added permitting and encouraging the use of BCPs.[7] Such changes may reflect the intention of MOF to replace framework agreements with BCPs in centralised purchases, given the significant criticism on the improper use of framework agreements in practice. This assumption may be supported by another MOF circular which states that the initial idea of introducing BCPs was to address the problems caused

[6] Hereinafter referred to as BCP.
[7] See the *Draft Implementation Regulation of the Government Procurement Law (Inviting Public Opinions) 11/01/2010,* Article 32, http://www.china.com.cn/policy/txt/2010-01/11/content_19215879.htm (accessed Aug 3, 2018)

by the abuse and overuse of frameworks, i.e. overpricing.[8] In terms of wording, it seems to indicate that BCP is superior to framework agreements.

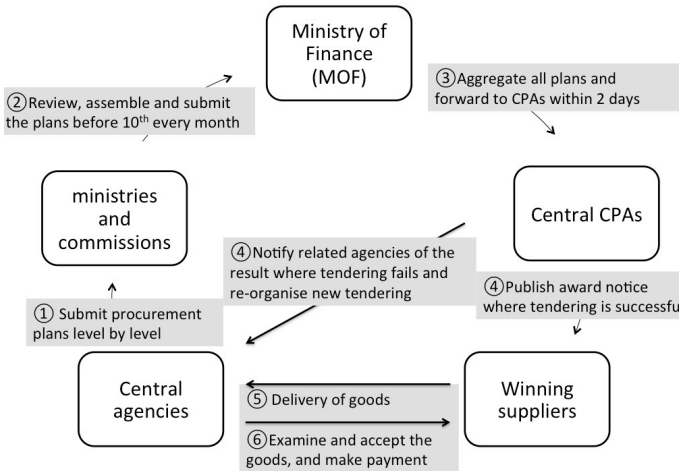
A BCP also includes two stages of operations. At the first stage, the centralised purchasing agency (CPA) selects the "best" supplier or suppliers to reach a master agreement on the aggregated demands of the procuring entities. The master agreement should include almost all the terms and conditions for future orders, including the price, the overall (aggregated) quantity of expected needs and the duration. Flexibility is only allowed regarding the delivery schedules at this stage, i.e. the exact time and precise location for individual orders. With the competition entirely focused at the first stage, the second stage is for the procuring entities to issue orders and schedule deliveries from the supplier.

BCPs are different from the "traditional" one-off procurements in that they are established before any actual requirement on the basis of estimates. They differ framework agreements as described above because they provide a high level of certainty regarding future orders, with particular regard to the terms of price and quantity, and no second-stage

[8] See MOF, "Notices on Issues of Further Carrying Out Government Centralised Procurement by Central Agencies" No. 101 [2009], http://gks.mof.gov.cn/mofhome/guokusi/redianzhuanti/zhengfucaigouguanli/200908/t20090807_191031.html (accessed Aug 3, 2018)

competition are involved in BCPs. Therefore, BCPs locate somewhere between framework agreements and the "traditional" procurements. To some extent, BCPs operate closer to "definite-quantity contracts" in the US[9] and "framework contract" in the EU.[10]

Figure 5.1 Operational Procedures of Bulk Centralised Procurement at the Central Level[11]



MOF and its local branches (the supervising authorities of government procurement) are supportive of BCPs mainly due to their benefits of expenditure savings and improved transparency.

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[9] *Federal Acquisition Regulation*, 16.502 (a) provides that "A definite-quantity contract provides for delivery of a definite quantity of specific supplies or services for a fixed period, with deliveries or performance to be scheduled at a designated location upon order".

[10] European Commission, *Explanatory Note: Framework Agreements – Classic Directive*, CC/2005/03 rev. 1, (July 2005, Brussels). According to the *Note*, framework contracts are "framework agreements that establish all the terms".

[11] The figure is based on the *Interim Measures for Administration of Centralized Procurement in Bulk by Central Budgetary Departments*, No. 109 [2013], Chinese text available at http://www.ccgp.gov.cn/zycg/plcgzs/201310/t20131028_3346073.htm (accessed Aug 4, 2018)

BCPs may allow the government agencies to better deploy the potentials of centralised procurements with better economies of scale, enhanced competition and process streamlining.[12]

As explained above, under a BCP, all aspects of the future requirements, including the total quantities are known to the suppliers from the very outset. The certainty about the future tasks, *ceteris paribus,* can elicit more favourable offers, especially lower prices, because uncertainty, i.e. in the volume or specification, is likely to raise the submitted prices.[13] Moreover, a BCP is awarded a single supplier. The winner-takes-all situation can boost competition among participants, leading to reduced prices. There is less risk of collusion as there is no further chance to "share the pie". Furthermore, with the competition entirely focused at the first stage, the ordering process in BCPs is simple, fast and easy to use.

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[12] The analysis concerning "framework contracts" in the EU can be relevant here. See G. L. Albano, A. Ballarin and M. Sparro, "Framework Agreements and Repeated Purchases: The Basic Economics and A Case Study On the Acquisition Of IT Services", Quaderni Consip, IV, available at http://www.ippa.org/IPPC4/Proceedings/04EconomicsofProcurement/Paper4-1.pdf (accessed Sep 12, 2018)

[13] *Ibid.* For example, when the total volume is uncertain, the suppliers need to bear the discrepancy between the estimated demands and the actual purchases. Such uncertainty may lead to the price premium and add to the submitted price. BCPs are commonly believed to provide lower prices than framework agreements. See Legislative Affairs Office of the State Council, China, "Answering Questions on Issues Concerning *Implementing Regulation of Government Procurement Law*" (Feb 27, 2015), http://www.chinalaw.gov.cn/article/xwzx/fzxw/201502/20150200398282.shtml (accessed Sep 12, 2018); Centralised Procurement Centre of the People's Bank of China, "Critically Viewing the History and Future of Framework Agreements" (Jan 14 2013), http://news.hexun.com/2013-01-14/150153962.html (accessed Sep 3, 2018); G. Luo, "Thoughts on Improving Framework Agreements and Bulk Centralised Procurement" 2 (2012) *China Government Procurement* 60, p.60

On the other hand, BCPs may be overused and their potential benefits may be overweighed by the risk of not meeting the actual needs of procuring entities. The key to achieving most benefits of BCPS is to standardise and aggregate contracts through setting out all terms in advance. Hence, BCPs are not suitable where the requirements vary between different users and when there is supply diversification. The lower the homogeneity of the requirement, the lower the standardisation of contracts and the less effective of using BCPs.

In the meantime, the estimates cannot always be accurate, and it is often that the expected quantity exceeds the actual needs. According to two participants in the interview, sometimes they ordered and paid for the products under BCPs in excessive of the actual requirement and left them unused.[14] In these circumstances, framework agreements are more appropriate to fulfil the flexible demands.

While BCPs can help the government purchasers to reap the benefits of centralisation, especially the fiercer competition and improved purchasing power, thus generating considerable savings "today", over-emphasising these benefits may adversely impact the participation and competition "tomorrow".

[14] The extent of satisfaction of procuring entities about BCPs varies between provinces. For instance, as one participant provides, under BCPs at the provincial level in Guangdong, the majority of procuring entities at the provincial level are satisfied with the products purchased through BCPs.

There is always a risk that the centralised purchasing power may be abused.[15] In China where the government is one of the major buyers in the market, centralisation and aggregation can neutralise the market power of fewer and large suppliers. As the size of purchases gets larger, SMEs may find it more difficult to participate in the procurement market due to the more demanding economic and financial qualifications required. Also, given the winner-takes-all situation, large suppliers will strive hard to be the winner of the competitive tendering- thus leading to a lower number of participants in the long term.[16]

Incumbency suppliers is a good example of this. Taking the monthly BCPs for laptops and desktops at the central level as an example, the winners in July 2017 continued to win the competitive procedures for the BCP in August. The winning suppliers were Lenovo, Tsinghua Tongfang, Acer, Asus and Haier, who are all large suppliers in the Chinese PC industry.[17] The

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[15] I. H. Anchustegui, "Division into Lots and Demand Aggregation- Extremes Looking for the Correct Balance?", Ch. 5 in G. S. Ølykke and A. S. Graells (eds.), *Reformation or Deformation of the EU Public Procurement Rules* (Edward Elgar, 2016), pp. 140-141

[16] The EU Directives emphasise the costs and benefits of demand aggregation. According to Recital 59 of the *2014 EU Public Sector Directive*, "There is a strong trend…towards the aggregation of demand by public purchasers, with a view to obtaining economies of scale, including lower prices and transaction costs, and to improving and professionalising procurement management…However, the aggregation and centralisation of purchases should be carefully monitored to avoid excessive concentration of purchasing power and collusion, and to preserve transparency and competition, as well as market access opportunities for SMEs".

[17] See the award notices of the BCP for desktops in July and August, Chinese text available at http://oa.zycg.cn/article/show/471629 and http://oa.zycg.cn/article/show/469618 (accessed Sep 23, 2018)

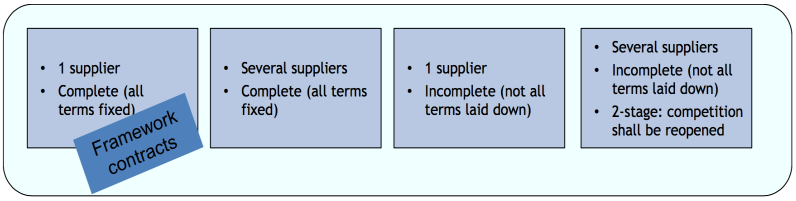
sizeable contracts close the procurement markets for SMEs. Though some tools, i.e. set-asides for SMEs, may be used to encourage their participation, it is submitted that excessive demand aggregation and the policy focus on cost saving "could run contrary to SMEs' access".[18] The concerns about excessive aggregation exist in the use of framework agreements as well.

Given the above analysis, BCPs can allow the government agencies to benefit from tighter competition and a streamlined process when the demands of various agencies are homogeneous and can be standardised. In contrast, when the procuring entities have heterogeneous requirements, customisation is needed in subsequent orders. In this context, framework agreements can provide necessary flexibility. Both BCPs and frameworks are options for centralised purchases, and it is pointless or possible to single out which should dominate.[19]

Also, there is no clear-cut distinction between the two arrangements. Where a framework is concluded with a single supplier based on realistic estimates, with full terms established, it may function as a BCP. It is all about the trade-off between administrative efficiency on one hand and flexibility on the other.

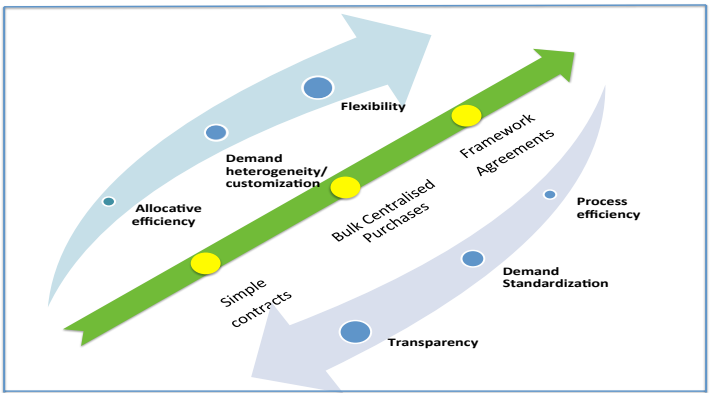
[18] See I. H. Anchustegui, fn. 15 *supra*, at p.144. According to Anchustegui, in the EU, the concern has been expressed about the negative impact of demand aggregation on the division into lots and on SMEs' access.
[19] Three participants said BCP would not be the only form of centralised government procurement.

Figure 5.2 Types of Framework Agreements in the EU



Source: OECD (2011), "Centralised Purchasing Systems in the European Union", SIGMA Papers, No. 47

Figure 5.3 Framework Agreements and Bulk Centralised Procurement



- **Framework agreements vs Electronic Marketplace**

An Electronic Marketplace (Dianzi maichang), or Online Mall (Wangshang shangcheng)[20] is an online virtue market that provides procuring entities with a simple, fast and transparent access to commonly used items at centrally negotiated prices from the registered suppliers.[21] EMs are analogous to the *Public*

[20] Hereinafter referred to as EM.
[21] Article 10 of the *IRGPL* provides the legal basis for using EM by stating that "The state shall apply unified construction standards for electronic trading platforms for government procurement and promote the utilisation of information networks for carrying out electronic government procurement activities".

Administration E-Marketplace in Italy [22], the *Government eMarketplace* in the UK[23], and the *Acquisition Advantage!* in the US.[24]

EM is also a procurement tool/ mechanism for centrally purchasing. The CPA firstly identifies the categories of goods/services that will be commonly needed and registers the qualified suppliers. The procuring entity, when a requirement arises, browses or searches what they need. The results will be presented as a list of options that can be compared. The entity selects the one that best suits the needs and adds to the shopping basket. The ordering experience is comparable to private online shopping, i.e. from Amazon. Many of the existing EMs also support online competition functions, including the electronic request for quotations and electronic reverse auctions, which allow procuring entities to seek more favourable offers.[25] EMs can significantly streamline the ordering process, enable

[22] Available at https://www.acquistinretepa.it/opencms/opencms/menu_livello_I/header/Inglese/TOOLS/Electronic_Marketplace.html(accessed Sep 13, 2018)

[23] Available at https://www.gov.uk/government/publications/government-emarketplace (accessed Sep 13, 2018)

[24] Available at https://www.gsaadvantage.gov/advantage/main/start_page.do (accessed Sep 13, 2018)

[25] For examples about how EM operates, see the EM established by CGPC at the central level or the Zhejiang Provincial EM, available at http://zzds.gpmart.cn/gs4/index.html and https://www.zcy.gov.cn/ (accessed Sep 13, 2018)

on-going transparency and monitoring, and encourage the participation of SMEs.[26]

Since their debut, EMs have often been considered as a separate procurement method/ arrangement which is distinguished from and is more effective than framework agreements.[27] However, the author holds that EMs originate from framework agreements and there is no clear or absolute demarcation between the two arrangements.[28]

The essential rationale behind both frameworks and EMs is to provide an efficient way for repetitive purchases of relatively standard goods and services. In fact, the majority of items that are currently purchased through EMs used to be covered by framework agreements. Regarding procedures, both EMs and framework agreements operate in two stages, and the procurement contracts will only be awarded at the second stage. When frameworks operate on the electronic basis, with e-Commerce capacity, they may function as EMs. As one participant stated, "…EM tends to be considered as the 2.0

[26] CCS, "Government eMarketplace: Changing the Landscape of Public Sector Purchasing" (Feb. 28, 2014), available at https://www.gov.uk/government/publications/government-emarketplace (accessed Aug 27, 2018)

[27] Y. Xu, "Analysing Five Organisational Form of Centralised Government Procurement by Ronghui Xie" (in Chinese June 29, 2015) available at http://caozuoshiwu.caigou2003.com/caozuoshiwu/267483.html (accessed Sep 12, 2018)

[28] Nine participants agreed with this view. Three participants held the opposite viewpoint and stated that EMs and framework agreements are different procurement methods.

version of framework agreements, the digital and advanced version (author's translation)."

The "kinsmanship" between EMs and framework agreements can be supported by the "Government Procurement Basic Operation Data Specifications", issued by MOF. In this circular, EMs are provided as the supplementary information of framework agreements.[29] Moreover, the EMs at the central government level is named "Framework Agreements Marketplace" (Xieyi gonghuo shangcheng), which indicates the connection between framework agreements and EMs.[30]

3. Organisational Set-up of Framework Agreements

In Chinese government procurement, framework agreements are used in centralised procurements, at the central and local levels. Four parties are mainly involved in operating and using a framework agreement: (1) procuring entities as the end users; (2) suppliers; (3) centralised purchasing agencies (CPAs),[31] and (4) finance departments, the supervisory authorities.

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[29] MOF, "Government Procurement Basic Operation Data Specifications"', No. 18 [2013]. According to the document, a national government procurement management system comprises 8 sub-systems, one of which is framework agreements with EM mentioned as the bracketed material, Chinese text available at http://www.ccgp.gov.cn/zcfg/mof/201310/t20131029_3587691.htm (accessed Sep 12, 2018)

[30] See http://zzds.gpmart.cn/gs4/index.html (accessed Sep 11, 2018)

[31] *The GPL*, Art. 16; *the IRGPL*, Art. 12.

As explained in section 2.2 of Chapter IV, since the involvement of CPAs is compulsory in all centralised procurements, CPAs have the exclusive authority to implement and manage framework agreements.[32] The purchaser and end user in frameworks are separate. It follows that procuring entities cannot establish framework agreements either in its own right or jointly with others. In contrast, in the EU and US, procuring entities are allowed to establish framework agreements *per se* or join those established by others.[33]

There is often a CPA at and above municipal level of governments in each administrative area following the fiscal system. They establish and maintain framework agreements for the use of government agencies and public institutions at their corresponding level. Therefore, in a province, multiple framework agreements let by different CPAs, such as that those at the provincial and municipal levels often co-exist; they may cover similar items but are used by different users. The existence of multi-layer of frameworks but with possibly overlapping coverages may not only cause waste of resources

[32] *Ibid.,* Art. 18. Implementing aggregated purchases through CPAs is also one hallmark of many public procurement systems in OECD countries. See OECD, *Government at A Glance 2015*, (OECD Publishing, Paris, 2015). The separation between purchaser and user, as submitted by Schooner, is the norm in government procurement. See S. Schooner, D. Gordon and J. Clark, "Public Procurement Systems: Unpacking Stakeholder Aspirations and Expectations" (2008) *GW Law Faculty Publications & Other Works.* Paper 111

[33] For details about framework agreements in the EU and IDIQ contracts in the US federal government, see Ch. III above.

but can also artificially segment the procurement market, diminishing the benefits of centralised purchases.

The use of framework agreements is made mandatory for the procuring entities. Even though in some cases, they *de jure* may opt to buy outside, where the terms in the market are better than those under frameworks, in reality, such an option has been rarely used.

Procuring entities can only use the frameworks established by the same-level CPA and are prohibited from turning to others, even if the terms therein turn out to be favourable. In another word, for procuring entities, a framework agreement being used not because it leads to value for money but because it is the only choice. One concern of such designated frameworks and mandatory use is that CPAs may have little incentive to optimise or improve the procurement results of framework agreements.

4. Conditions for the Use of Framework Agreements in Government Procurement

Framework agreements are not suitable for all procurements. In Chinese government procurement, there are no uniform or express conditions for the use of framework agreements. As explained in Chapter IV section 2.2 above, the prerequisite for using framework agreements, like in other centralised

purchases, is that the subject matter to be procured should fall within the scope of the centralised procurement catalogues.[34]

In general, the circumstances where framework agreements are primarily employed in China are similar to that in the EU and US. By reviewing the local rules and ministerial rules related to framework agreements, it can be observed that framework agreements are mainly used to purchase the relatively standard goods and services that are readily available in the market, which are expected to be frequently needed.[35] The typical subject matter of framework agreements are office supplies and IT products.

Chinese public procurement has been learning in practice. The above circumstances, concluded by the author, are more

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[34] *The GPL*, art.7. The scope of centralised procurement catalogues may vary from one to another province, as different provincial governments define their own catalogues. The focus of the catalogues is to a large extent limited to the off-the-shelf goods/services, based on the practice. The centralised procurement catalogues are normally updated on a yearly basis.

[35] Fifteen participants in the interviews mentioned this condition. Thirteen provinces provide this condition for use of framework agreements in their local rules, but in different expressions, including Shandong, Jiangsu, Jiangxi, Xinjiang, Hainan, Guangxi, Beijing, Fujian, Guangdong, Shanxi, Heilongjiang, Hebei and Zhejiang. For instance, Article 5 of the Measures on Administrating Shandong Provincial Framework Agreement Government Procurement No. 13 [2008] in Article 5 provides that "实行协议供货的项目，一般为规格或标准相对统一、产品品牌较多且市场货源充足的通用类产品". According to the Interim Measures on Administrating Framework Agreement in Jiangsu Provincial Government Procurement, framework agreements may be used to procure common use and standardised goods or services, where there will be repeated requirements, which are largely available in the market and the purchases of which are from one source. The Chinese text is "政府集中采购目录中，规格或标准相对统一、品牌较多、日常采购频繁且市场货源充足的通用类产品，或者通用服务类项目可以采用协议供货形式开展采购活动". The similar expression is found in the ministerial rule- *Measures on Managing Government Procurement via Framework Agreements in State Administration of Taxation System* (Trial), No.73 [2007], Article 5.

like a rule of thumb that provides some hints on using frameworks, rather than accurately articulating provisions that are enforceable. Despite that, however, doubts may still arise concerning how the CPAs in practice determine whether the condition for use has fulfilled or not, especially regarding how to assess the "likelihood" and "frequency" of future requirements.[36]

CPAs are not required to justify or record their decisions on using framework agreements. There is no guidance or supervision on this issue. Therefore, CPAs are less likely to be held accountable for any inappropriateness in such decision-making. As a participant stated, "…it is more a subjective assessment based on their long-term experience" (author's translation). It is argued that the lack of accountability and vagueness in the description may provide shelters for procurement officials to the improper use of framework agreements, for example to circumvent normal transparency and competition requirements. The risk can be particularly exacerbated where effective planning and adequate oversight are absent, which is often the case in the current use of framework agreements in China, as discussed below.

[36] This difficulty of assessing "expectation" of future needs has also been raised under the *UNCITRAL Model Law*. See Ch. III above.

The circumstances where framework agreements may be used, as described above, preclude their use in urgent procurements. This exclusion arguably makes sense, because the prerequisite for using frameworks is that the subject matter should be within the scope of "catalogues", which is mainly limited to the off-the-shelf goods and services. On the other hand, however, as explained earlier in Ch. III, the international experience has proved the efficacy and efficiency of framework agreements in responding to emergency procurements. The Chinese government is suggested to consider the possibility of using frameworks in urgency.

4.1. The First Stage: Concluding a framework agreement

It is reiterated that all framework agreements in Chinese government procurement are used for centrally purchasing and CPAs are the purchaser, separate from the users. All frameworks are of closed nature, involving multiple suppliers and multiple purchasers, with or without the second-stage competition.

At the first stage, it is up to the CPAs to determine whether to use framework agreements and how to structure them based on careful procurement planning and design. While the international experience highlights the significance of effective planning in ensuring the success of framework agreements, as demonstrated in Ch. III, Chinese CPAs are observed to often

"skip" the planning stage but "rush into" the tendering procedures. In very few cases thorough demand and market analysis have been conducted in practice.[37]

The decision to use framework agreements is part of procurement planning, which essentially involves the application of the condition for use. As pinpointed earlier, the decision tends to be more based on assumptions and experience, rather than on a reasonable cost-effective analysis.[38] Where this happens, discrepancies are highly likely between the "assumed" and actual requirements. It is also possible that the terms established cannot reflect the market practice. For instance, given the lack of proper market and demand analysis, a CPA may not objectively define the scope of requirements with precision. The problem of bespoke and exclusive supplies (Zhuangong Tegong), as explained later, is a typical example of the too-broad specification.[39] On the other

[37] That framework agreements are not a substitution to procurement planning is highlighted under the UNCITRAL Model Law, in the EU and US systems.

[38] According to an official from a provincial finance department, the decision-making process may draw on the experiences and references from framework agreements in other localities. "You can tell that they will be repeatedly required in scattered lots by almost all procuring entities. Also, the procurement data will also be taken for use. Unfortunately, because of the current 'sketchy' budget, we cannot get the accurate or sophisticated data."

[39] Six participants mentioned the problem of exclusive supplies. They also mentioned suppliers' perverted intention to circumvent supervision on price reductions and consider it a reason for the problem. By providing bespoke products, there are counterparts in the commercial market, and the pricing under framework agreements is incomparable with the market price. On the other hand, however, as one participant pointed out that, there are cases

hand, the lack of procurement expertise and skills may also lead to unsound decision-making, as discussed later.

Open tendering has been the primary award procedure to conclude framework agreements and has generally been considered as a *sine qua non* of frameworks.[40] This, however, does not prevent other methods from being used in appropriate circumstances. The CPA should prepare and issue an advertisement to solicit tenders on the designated media in accordance with the solicitation procedures in open tendering.[41] There is an official portal designated by MOF which provides access to all the existing media on government procurement at various levels.[42]

There is no general requirement about what information a solicitation should include. Usually, a call for competition

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where bespoke and exclusive products could be justified, for instance, requiring energy-efficient laptops for the environmental objective of government procurement. In the US, there was a time when the government used to make bespoke purchases of goods. To harness this problem, in the 1990 reform the approach to buying "commercial items" was adopted to secure full and effective competition. See G. L. Albano and C. Nicholas, fn. 5 *supra*, at pp.103-104

[40] Nine participants highlighted the use of open tendering. In some documents, the use of open tendering is expressly stated, for instance, see Article 3 of the *Measures on Administrating Shandong Provincial Framework Agreement Government Procurement* No. 13 [2008] of Shandong Provincial Finance Department. From the international experience, open tendering is also often made the primary method to conclude framework agreements, as the case of Hungary. See OECD, "Centralised Purchasing Systems in the European Union", *SIGMA Papers*, No. 47 (OECD Publishing, Paris, 2011).

[41] *Administrative Measures for Government Procurement Information Publicity*, No.19 [2004] of the MOF. There is a national portal designated by MOF through which one can access to all provincial and ministerial government procurement websites, available at http://www.ccgp.gov.cn/index.shtml (accessed Aug 12, 2018)

[42] Available at http://www.ccgp.gov.cn/index.shtml (accessed Aug 12, 2018)

includes the description of the subject matter to be procured, technical specification of the requirements, the qualification criteria, division into lots if any and other information necessary to submit tenders.[43]

It is observed that the volume/size of the aggregated demands, in terms of both quantity and value, under a framework agreement is scarcely included in the solicitation or the master agreement itself. [44] In the absence of such information, the suppliers are unable to understand the scope of the procurement, and thus are unlikely to decide whether they have interest to participate and how to prepare tenders.

Upon receipt of the tenders, the CPA evaluates the qualification and their offers, following the evaluation procedures in open tendering, and selects more than one supplier to conclude the framework/master framework, based on either "comprehensive evaluation" or lowest price. The "comprehensive evaluation" is the award criteria similar to "most economically advantageous tender" in the EU and "best

[43] Usually, the solicitation documents are provided as an attachment to the notice. However, only the registered suppliers or the procuring entities can download and access to the documents, which are inaccessible to the public. For instance, see the "Notice of Inviting Tenders for 2017-2018 Framework Agreement on Information Products by Central Government Agencies", available at http://oa.zycg.cn/article/show/456058 (accessed Aug 12, 2018)

[44] Two participants stated that the terms of quantity and amount are not required in practice. In the EU, US and *Model Law*, the information included in the advertising notice for a framework agreement is required to be as complete as possible. See Chapter III above.

value" in the US system, which enables the CPAs to consider factors other than price only.[45] The award criteria should be specified in the solicitation.

Regardless of the criteria selected, price must be considered and is normally the decisive factor. However, as discussed later, it is questionable whether suppliers can and how to prepare and submit reasonable prices when they are not fully aware of the scope of future tasks to be performed, such as the quantity. As a participant stated, "…we often submit tenders based on the null hypothesis at the first stage of framework agreements …".

There is no general requirement restricting the number of suppliers admitted to a framework agreement, either maximum or minimum. In reality, frameworks awarded with very a few (e.g. less than three) are rarely seen. It is more often that the number of the supplier parties is higher than actually necessary or reasonable. In an extreme case, all qualified suppliers that have submitted responsive tenders may be accepted, in which case the framework actually functions no more than supplier list. The first-stage competition, in this case, may become meaningless. A large and excessive number of supplier parties may lead to lengthy and complex second-stage, which means each call-off has to go through a competitive selection process.

[45] *The 2014 Public Procurement Directive*, Art. 67; *Federal Acquisition Regulation* Subpart 2.1.

This may jeopardise administrative efficiency, which is the "core" of framework agreements.

The inappropriate number of the awardees can be mainly attributed to the lack of effective procurement planning. For instance, it may be difficult to effectively reduce the number of suppliers when the specification is too broad and vague and when the requirements are unclearly defined.[46] What may be worse, the importance of determining the right number of the supplier parties has not been fully recognised, thus being neglected by the procurement officials in the planning process.[47] For the government purchasers, allowing suppliers to enter the framework does not require them to order from each supplier party. Therefore, having a large number of suppliers does not generate more obligations or cause any losses, but instead provides more freedom to choose. However, as discussed soon, an unreasonable number of awardees does have the adverse impact on the competition and the overall effectiveness of frameworks.

The CPA needs to publish an award notice regarding the conclusion of a framework agreement. The notice often includes

[46] See Albano and Nicholas, fn. 5 *supra*, at p.131

[47] As provided in Chapter III, the right number of suppliers to be admitted to a framework is important because it impacts the dynamics of the competition and may shape the mini procurement market within the framework.

the identities of the suppliers entering the framework and their respective bids.[48] Price is a must-have term in the notice and in the master agreement. Rather than an exact figure, the price established at this stage tends to be a pricing mechanism to be applied to determine the price of a specific order.

In practice, the two most common-use price mechanisms are (a) Ceiling price, also known as reserve price or cap price (Zuigaoxianjia); and (b) Discount (Zhekoulv).[49]

A ceiling price is a price that is pre-set by the CPA for volume purchases, which is the procuring entities' maximum willingness to pay for the goods or services under framework agreement. It is disappointing that no information is available showing how CPAs in practice determines the ceiling price under frameworks. With a ceiling price established, it applies to all the awards under the framework, and any orders above this price will not be accepted.[50] It is not only a determinant factor for admitting the suppliers to a framework agreement, but also serves as a

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[48] For instance, see "Award Notice Concerning the 2014 Framework Agreement of Software by the Central Government Agencies" (published on Oct. 31, 2017), Chinese text available at http://oa.zycg.cn/article/show/482680 (accessed Aug 14, 2018)

[49] In the interview, two participants provided the use of the ceiling price in framework agreements, and six participants stated the availability of discount rate in their practice. One participant confirmed the combined use of both. See also X. Yan and X. Wu, *Framework Agreement and Its Price Mechanism Research* (2010, China Financial and Economic Publishing House) p.42

[50] For instance, see "Notices on Issuing the Implementing Measures on Centralised Procurement of IT Products Through Framework Agreements for Central Government Agencies (Trial)" No. 25 [2006] of the CGPC, Art. 12. The practice of ceiling price can be found in other procurement systems, i.e. in Brazil, see Albano and Nicholas, fn. 5 *supra*, p.136

safeguard to avoid discretionary price rise in call-offs, preventing overpricing and ensuring consistency between two stages.

The "discount" mechanism is also commonly employed to denote price in framework agreements. It means the minimum discount margin that supplier parties are bound to offer in the call-offs. To determine the price of a specific order, procuring entities apply the following algorithm:

Award price = the market price (benchmark) × (1-discount)[51]

This "discount" mechanism is analogous to the "Most Favoured Customer" clause in the US GSA Schedules, as mentioned in Chapter III. It seeks to ensure the government enjoys an equally or more favourable price from the supplier than any other customers. It is also intended to allow frameworks to reflect the market practice within the duration.

However, it is argued that the price benchmark presents a challenge in the implementation, mainly because it is unclear what the "market price" means and how to objectively determine it. In reality, a product can be priced in a variety of forms, such as retail price, wholesale price, manufacturer's price and e-commerce prices. In the absence of a unified standard

[51] See *Measures on Managing Government Procurement via Framework Agreements in State Administration of Taxation System* (Trial) No.73 [2007] of the State Administration of Taxation, Art. 8.

and objective method to define the "market price", the comparability between the price under framework agreements (subject) and the market price (object) is questionable.[52] It is further noted that there is a lack of means of gathering and collating price data about all the call-offs under framework agreements. Therefore, no empirical evidence is in place to demonstrate whether framework agreements have always offered the best value as expected.

A framework agreement, in Chinese government procurement, usually lasts from three months to one year.[53] There are cases where the CPAs may extend the duration of an existing framework without justification, discretionally or inadvertently. Such extension may harm the equal treatment for any new suppliers that may wish to participate. More importantly, the extension may exacerbate the walled-off effect in the relevant market of closed frameworks.

Once a framework agreement is in place, procuring entities are obliged to fulfil all their requirements from the framework agreement. In most cases if not all, they, as end users, are excluded from the first stage and have little voice in concluding

[52] The vagueness in implementing the "market price" is a problem of the government procurement in general.
[53] For instance, a framework agreement established by the CGPC is usually valid for a year and the duration of that at the provincial level in Shandong and Hebei is 6 months and 4 months respectively.

frameworks. In practice, ex-ante communications with user entities and ex-post feedback from them are usually absent.[54] It is not surprising therefore that complaints may emerge that framework agreements cannot meet the real needs of users.

4.2. The Second Stage: Call-offs

At the second stage, procuring entities can place orders from the supplier parties. There are no uniform rules as to how call-offs should be made in Chinese government procurement. Practice suggests that call-offs can be made directly ("direct awards") or after a further round of competition. Whether or not a second-stage competition is involved is arguably hinged on two interacting factors: (1) the extent of the completeness of the master agreement; and (2) the value/amount of the order. In reality, the second factor often plays a decisive role, maybe due to its straightforward and objective implementation.

(a) Direct award

Direct award usually applies in small-value purchases where all the terms and conditions for future orders are established in the framework agreement itself. In this case, the procuring entity is

[54] Although pre-communication between the CPA and user entities is required in a very few localities, such as Beijing, the absence of such communication and dialogues is more commonly seen in framework agreements in Chinese government procurement. "Notices on Issuing Interim Measures on Administrating Beijing Municipal Framework Agreements and Designated Procurement of Services" No.362 [2010], Art. 11.

free to order from any supplier that is considered appropriate, without the need to go through any further competition, provided the price is not above the ceiling price.

In light of the simplicity and convenience, procuring entities may discretionally split a large purchase into smaller ones to apply direct awards, avoiding any competition that should have taken place. Given the lack of adequate oversight, direct awards may pose significant risks to transparency and competition, creating opportunities for the improper use of frameworks, such as favouritism.

(b) Second-stage competitions

Procuring entities may reopen a second-stage competition among the supplier parties to award a call-off, the core element of which tends to be price in most if not all cases. Practice suggests that this competition is usually carried out in two forms: request for quotations and electronic reverse auctions.[55]

- **Request for Quotations**

For purchases valued exceeding a prescribed threshold (large orders), procuring entities may need to request for quotations

[55] These are two forms that are most commonly used. In practice, there are other methods to award a contract under framework agreements. Regular Price Competition (Xieyi jingjia) is a method highlighted by one participant. With this method, price competition is to be held (a) for the first order placed under the framework agreement; and (b) on a monthly basis, the result of which would be updated and applied to the orders thereafter.

from at least three supplier parties to obtain the best price.[56] The one offering the lowest price is usually the successful supplier of the order. There is no objective method established to identify and determine whom to be surveyed among the supplier parties, which means procuring entities are granted the full discretion in this respect, as is the case of IDIQs in the US and framework agreements in the EU.[57] This discretion, in conjunction with the limited transparency, may shelter for improprieties without being noticed.

The UNICITRAL *Model Law* may provide a solution for China (as well as for the EU and US systems) on the issue by requiring that either all suppliers within a framework agreement or only the capable ones must be invited, in the latter case of which all supplier parties should be notified about the competition.[58] This two-fold approach could firstly help to circumvent unfettered discretion in the ordering stage, and secondly to allow restricting the competition to the "capable" suppliers for efficiency.[59] The key to this approach is the notification of

[56] For example, this award method is available in the use of framework agreements established by the CGPC for the use of general central procuring entities and in departmental framework agreements of State Administration Taxation. See "Notices on Issuing the Implementing Measures on Centralised Procurement of IT Products Through Framework Agreements for Central Government Agencies (Trial)", No. 25 [2006] of the CGPC, Art. 14.
[57] See Albano and Nicholas, fn. 5 *supra*, at 120
[58] The *Model Law*, Art.61(4). Where the second method is used to issue invitations, a procuring entity should interpret "capable" objectively and narrowly and should explain why other suppliers are excluded.
[59] The *UNCITRAL Model Law*, Art. 62. See Ch. III section 2 above.

competition opportunities, and China is strongly suggested to apply such measure, as proposed in Chapter VIII.

- **Electronic Reverse Auction[60]**

Procuring entities may use an electronic reverse auction, also known as the second-stage price competition to place an order under frameworks.[61] It usually applies where the price of the item to be required to volatile, such as IT products. The electronic purchasing techniques enable the government to obtain better pricing through on-gong competition with minimum burden and cost, and to benefit from enhanced transparency.

Generally, electronic reverse auction in China operates close to that in many procurement systems. Procuring entities should first solicit participation through the electronic systems and specify all the information necessary. During the auction, the suppliers present their bids and can successively underbid vis-à-vis other bids back-to-back. The auction result will be generated automatically, and the lowest price bid is to be selected after the specified time.[62]

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[60] Seven participants used the term "second stage price competitions" and another two used the term "electronic reverse auctions".
[61] For instance, electronic reverse auctions are frequently used in the second stage of framework agreements in Shanghai and Guangdong, available at http://www.shzfcg.gov.cn:8090/shzfcg/index and http://www.gdgpo.gov.cn/ (accessed Aug 17, 2018)
[62] For instance, see *Measures on Administrating Shandong Provincial Government Procurement through Framework Agreements Government Procurement*, No. 13 [2008], Arts 23-24; *Measures on Administrating Online Framework Agreements in Shanghai Municipality* No. 4 [2017], Art. 26

The primary objective of reopening the second-stage competition is to ensure the government agencies obtain a competitive price that reflects the requirement and the market practice. To that end, many other tools are also employed, one of which is the "price update" requirement, by which the suppliers are requested to regularly reduce the price they offer to the government, whenever they reduce the price in the commercial market.[63] This requirement is similar to the Price Reduction Clause under the US GSA Schedules.[64] In reality, it is inevitable that suppliers may be reluctant to drop the price as requested, which means reduced profits.[65] Despite the efforts to ensure the compliance of suppliers, CPAs often claimed to be shorthanded and incapable of consistently tracking market changes and conducting market benchmark.[66] On the other

[63] For instance, see *Measures on Administrating Shandong Provincial Framework Agreement Government Procurement*, No. 13 [2008], Art.21.
[64] See Chapter III, section 4 above.
[65] "Notice of Zhejiang Provincial Finance Department and Centralised Purchasing Agency on Sampling Survey of Procurement Prices under Framework Agreements and the Relevant Handling Results" (March 2012). The suppliers' incompliance is also a problem present in the US. See U.S. Office of Audits. Office of Inspector General. GSA, "Major Issues from Multiple Award Schedule Pre-award Audits", Audit Memorandum Number A120050-6, (Sept.19, 2016)
[66] Eleven participants in the interview provided monitoring and comparing the market price is critical to the success of a framework agreement, whereas in the framework agreements practice it is an intractable problem. The lack of consistent market benchmark is also a problem that emerges in the UK. The National Audit Office reported that CSS does not consistently compare its framework agreements against other deals in the market, which leads to the doubt regarding whether framework agreements by CSS has necessarily achieved the best value for the users. See National Audit Office, "Cabinet Office-Crown Commercial Service: Report by the Comptroller and Auditor General" (HC786, Session 2016-17, Jan. 2017), p.39. Albano and Nicholas

hand, as pinpointed earlier, how the price comparisons should be objectively undertaken remains be clarified.

Some CPAs often resort to relevant market indices as a benchmark to determine whether the prices offered under frameworks are competitive. To place an order, the entity refers to the data of third-party organisations that have expertise in capturing real-time market price and uses their data to determine the basis for the price.[67] "Zhongguancun Index for Electronic Information Products" (Zhongguancun dianzixinxi chanpin zhishu) is the most commonly used indicator for IT products in practice.[68] While the government can access to the real-time data collected by the professionals, there is a risk of over-reliance on the third parties, which is not conducive to developing its own capabilities and may lead to conflicts of interests.[69]

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identified this issue in other systems. See Albano and Nicholas, fn. 5 *supra*, at p.283

[67] Three participants referred to this measure.

[68] The purpose of the Index, issued by Ministry of Commerce, is to collect and analyse the prices of electronic information products from 450 dealers from four IT malls, available at http://www.zgcindex.org/%E9%A6%96%E9%A1%B5/tabid/36/Default.aspx (accessed Aug 17, 2018)

[69] It is argued that the third party may compromise their neutrality to satisfy certain suppliers for personal gain or interest. As one participant submits, "Where there is power, there is rent-seeking", which is particularly true when those third-party organisations are market players. So, we can only use third party monitoring for reference, and can never rely on them". Another participant contends that they thought about bringing in two or more third parties to avoid excessively relying on one. However, this idea was withdrawn finally since they could not deal with the situation where different providers present different and even contradictory information.

At the ordering stage of frameworks, there are few information obligations in Chinese government procurement, as is the case in the EU and US systems.[70] The procuring entities do not have to advertise an upcoming call-off within the frameworks. The call-off stage becomes a closed system, posting significant risks to competition and transparency, not only to the public but also amongst the supplier parties within frameworks, as will be discussed in section 6.

Not long ago, orders awarded under framework agreements were not subject to the award notice requirement. This may be because the conclusion of a framework agreement is often regarded as the end of the whole procurement process, with the ordering stage being merely the execution of the agreement. Given that, although the *IRGPL* requires procuring entities to publish all public contracts[71], it hardly applies to awards made under framework agreements.

However, in September 2017, the MOF issued a policy circular where it for the first time expressly requires awards

[70] Eight participants talked about the limited publicity problem in call-offs in the interview. For more information about the issue of the lack of transparency in the EU context and under the *Model Law*, see S. Arrowsmith, *The Law of Public and Utilities Procurement Volume 1* (2014), chapter 13. In the US, Government Accountability Office ("GAO") identified that the lack of public notice might be among the reasons that contributed to the overpricing problem, in the *Contract Management: Benefits of Simplified Acquisition Test Procedures Not Clearly Demonstrated,* Report GAO-01-517 (April 2001)
[71] *The IRGPL*, Art. 32 and 43

made under framework agreements being made public.[72] The obligation of making call-offs public is a very recent move and how it is implemented in practice remains to be seen. Nevertheless, the impact of this new requirement cannot be underestimated since it indicates that MOF, the supreme regulator has recognised the transparency loophole and made efforts to remedy the concern.

The post-award management is generally missing in the context of framework agreements in Chinese government procurement. There is little evidence showing that CPAs or finance departments have evaluated whether and to what extent framework agreements have been successful in meeting procuring entities' needs or in analysing the problems encountered in practice. In the absence of *ex-post* management as well as the *ex-ante* planning, it is difficult-if not possible- to know whether framework agreements are the most appropriate method in the procurement.

[72] See "Notice of Ministry of Finance on Further Implementing Information Publicity of Government Procurement Activities", No. 86 [2017]. It also provides the information to be included in the notice, including the names of the parties involved, unit price, quantity and the total value of the order.

5. Supplier Review

A supplier review mechanism is provided under the *GPL* and its implementing rules, mainly *IRGPL* and the *Measures on the Handling Complaints of the Government Procurement Suppliers* (the MOF Review Measures)[73], whereby an aggrieved supplier can complain and seek remedies. Under the system, an aggrieved supplier may lodge an objection (zhiyi) to the procuring entity or its procurement agencies, (including CPAs, i.e. in cases of framework agreements) against any impropriety that arise in the procurement solicitation, procurement process, the selection of successful supplier and the contract awards.[74]

Where the aggrieved supplier is not satisfied with the review result, or when the response is not given timely, the supplier may file a complaint (tousu) to the competent finance department.[75] If the decision is still considered unsatisfactory or is not made timely, the supplier may apply for administrative review (xingzheng fuyi) before the finance department at the next higher level.[76] It also has the right to raise administrative

[73] The *MOF Review Measures*, No.94 [2017]
[74] *The GPL*, Art. 52
[75] *The GPL*, *Art. 55.* Article 13 of the *GPL* and Article 17 of the *MOF Review Measures* expressly state that the finance departments at all levels as the authority to handle government procurement complaints.
[76] Article 58 of *the GPL. Administrative Reconsideration Law of the People's Republic of China* was adopted at the Ninth Meeting of the Standing Committee of the Ninth National People's Congress on April 29, 1999, promulgated by Order No.16 of the President of the People's Republic of China on April 29, 1999, and effective as of October 1, 1999.

litigation before the administrative court where it disagrees with the review results.[77] Apart from the above formal challenge proceedings, a supplier may make inquiries (xunwen) when it has doubts about the procurement process and should obtain responses from the relevant procuring entities.[78]

Currently, there are no express rules about the application of the review mechanism in the context of framework agreements. Since the first stage is based on the standard award procedures, mainly open tendering, the challenge proceedings should apply, *mutatis mutandis*, to the conclusion of framework agreements.

One caveat is that in cases of framework agreements, CPAs act as the first-instance review body, not the procuring entities, hearing complaints and handling disputes that arise in concluding frameworks, recalling the fact that all frameworks are established and maintained by the CPAs.[79] In fact, when government agencies or suppliers have any doubts about frameworks, in most cases, they may choose to first reach the CPAs for resolution.

As for the second stage, to date, it is unclear whether challenges against the call-offs under framework agreements

[77] *The GPL*, Art. 58. In China, there are no special administrative courts, and administrative lawsuits are dealt with by the administrative divisions of various courts.
[78] *The GPL*, Art. 51
[79] *The GPL*, *Art.* 52 provides that the procurement agency may also be the review body.

are allowed. A question closely relevant to this issue is whether a framework agreement is itself a procurement contract. If the answer is affirmative, it means call-offs are the execution of contracts, and all the procedural safeguards, including the supplier review, may cease to apply to the post-award activities. There is no consensus reached on the legal status of the master agreements, and the applicability of the review mechanism at the call-off stage remains in question.[80]

On the other hand, even if complaints against call-offs are allowed, the lack of transparency at this stage, as explained earlier, may make the review mechanism meaningless and ineffective. For instance, a disappointed supplier is highly likely to miss the deadline for making complaints because it was unaware of the breach and thus unable to provide evidence timely. The newly introduced requirement of award notices is expected to remedy the transparency deficiency.

Furthermore, the lack of proper division of roles and responsibilities between procuring entities and CPAs may pose challenges for suppliers that wish to protest against the call-offs under framework agreements. As discussed later, it is generally unclear whether CPAs act as the principal or as an agent on behalf of the procuring entities. A supplier may find it difficult

[80] In the interviews, six participants suggested that master agreements were procurement contracts and four considered they were not.

to identify the right party to file a challenge and be held back from acting so. There is, therefore, a need to rationalise the responsibilities between the parties involved to enable the potential disputes settlement and remedies in framework agreements.

6. Analysis of the Problems and Challenges in the Use of Framework Agreements in China's Government Procurement

The above sections have elucidated how framework agreements are operated in Chinese government procurement. Based on that, this section proceeds to pinpoint and examine the major problems that may detract from the achievement of benefits of framework agreements.

6.1. The Use of Framework Agreements: *Ultra Vires*?

The widespread practice of framework agreements in Chinese government procurement points out an assumption that their use has been *ab initio* permitted under the current government procurement rules. However, it is argued that the use of framework agreements lacks an adequate legal basis and may, therefore, be *ultra vires*.

6.1.1. Framework agreements as a distinctive procurement method

It is unclear whether framework agreements are regarded as a separate procurement method or a procurement technique, the answer of which may impact their legality. However, under the current government procurement rules, framework agreements are argued to lack an adequate legal basis for being treated as a separate procurement method.

Framework agreements are not mentioned in the national law or the State Council regulation on government procurement, namely the *Government Procurement Law* (GPL) or the *Implementing Regulations of Government Procurement Law* (IRGPL), which are the legal base for all government procurement rules. Article 26 of the *GPL* specifies the methods available for government procurement, including open tendering, restricted tendering, competitive negotiations, single-source procurement, request for quotations, and any other methods authorised by the competent authority under the State Council, namely the MOF.[81] The non-exhaustive list is flexible in coping with future possibilities, whereas the flexibility may jeopardise the legal certainty of the *GPL*. The exclusive authority of MOF to approve new methods, subject to no

[81] According to Article 13 of the *GPL*, MOF is the competent authority under the State Council.

supervision, may become unconstrained discretion. For example, the attitude of the MOF to a particular method may be the decisive factor in the availability of such a method.

Regarding framework agreements, MOF has not mentioned framework agreements as a separate procurement method in its ministerial rules that are currently in full effect. It is suspected that MOF may deliberately choose not to authorise framework agreements to avoid the related disputes, especially in light of the public criticism on the improper use of the arrangement, such as overpricing as explained in section 6.4. The fact that MOF quickly accepted competitive dialogue (Jingzhengxing cuoshang) as the sixth procurement method[82] however remains silent on framework agreements may indicate the MOF's "ostrich syndrome" regarding framework agreements. However, "burying the head in the sand" cannot address the problems.

The *Measures for the Administration of Government Procurement Through Non-Tendering Methods* is a relatively recent ministerial instrument adopted by MOF dedicated to regulating non-tendering procurement methods.[83] Given the

[82] In 2014, MOF for the first time expressly mentioned competitive dialogue in PPP projects and very soon issued the *Interim Measures for the Administration on Government Procurement Through Competitive Dialogue*, No.214 [2014]. The "Interim Measures" is, in theory, a set of normal rules and does not have the legal force as the ministerial regulation.
[83] *Measures for the Administration of Government Procurement Through Non-Tendering Methods,* No.74 [2013] of MOF, Chinese text available at

prevalence of framework agreements, the fact that they are not mentioned at all in the *Measures* seems disappointing. Such silence arguably implies that: (i) framework agreements are not regarded as a separate method; or (ii) MOF deliberately avoids mentioning framework agreements.

For the above, framework agreements lack an adequate legal basis being a distinctive procurement method under the existing government procurement rules. In that case, the hundreds of local rules and ministerial rules related to framework agreements, as mentioned in Ch. IV might be in breach of the *GPL*, simply because their lawmakers have no right to authorise the use of new methods.

6.1.2. Framework agreements as a part/stage of open tendering procedure

In practice, framework agreements are more considered as a procurement technique, as part of other methods, especially open tendering, because open tendering is usually made the default procedures to conclude frameworks, as explained above.[84] No approval from the MOF is required for employing a new procurement technique. Despite that, however, the

http://www.gov.cn/flfg/2014-01/03/content_2559194.htm (accessed Aug 18, 2018)

[84] Five participants firmly believed that framework agreements were part of open tendering.

viewpoint of considering framework agreements as part of tendering is arguably untenable for several reasons.

Firstly, the tendering proceedings, in Chinese government procurement, are regulated by the *Measures for the Administration of Tendering Proceedings in Government Procurement* (MOF Tendering Measures).[85] The fact that the *Measures* do not mention frameworks in any kind may reject the viewpoint that framework agreements are part of tendering procedures. It is particularly interesting to note that the former *MOF Tendering Measures* adopted in 2004 briefly mentioned framework agreements in the then Article 85, which was removed in the modification process.[86] The then-existing frameworks-related provision may support the view that frameworks tended to be considered as part of open tendering, as a technique/tool. The removal of such provision arguably reflects the MOF's "deliberate" negligence to authorise framework agreements, maybe in order to avoid the problems arising in their improper use.

[85] The current *Measures for the Administration of Tendering Proceedings in Government Procurement* No. 87 [2017] of MOF. As explained in Chapter IV, the *Tendering Law* in reality mainly applies to procurement of works based on tendering procedures, and the *Government Procurement Law* mainly applies to the procurement of goods and services and the procurement of works based on non-tendering procedures. Therefore, tendering procedures in the procurement of goods and services and those in works projects are subject to different regulations.

[86] The previous *MOF Tendering Measures,* No.18 [2004] of MOF. It was amended in 2017, and the final version removed the relevant provision.

Secondly, whilst open tendering can be, and indeed has been mainly, used in practice to conclude framework agreements, it is also possible to use other procurement methods, such as restricted tendering especially in purchases of services.

More importantly, operating framework agreements may be inconsistent with the existing government procurement rules in many aspects, at the risk of violating the *GPL* and the *IRGPL*. For instance, to conduct more than one round of tendering or competition during a procurement procedure is not permitted under the current rules. This is because China follows the traditional sealed-bid approach, by which one and the only one winning bidder will be determined upon the bid opening and evaluation.[87] A further round of submission and competition was not envisaged in drafting the laws, and the procedural rules, especially those on acceptable of the successful submission cannot be tailored to apply to frameworks involving a second-stage competition.

Moreover, the existing requirements for information to be included in solicitation and that in contracts do not allow the necessary flexibility in framework agreements. According to the *Measures on Administrating the Government Procurement Information Publicity*, the technical specifications, the identity of the purchaser(s), and particularly a precise quantity should

[87] See *MOF Tendering Measures*, article 3

be articulated in solicitation documents. However, in the context of framework agreements, these terms may not be finalised until a specific need arises.[88] Similarly, the rules on contract notices, which requires accurate information on a fixed quantity, delivery schedule, identity of the procuring entity, cannot properly apply to framework agreements either.[89] In light of the prevalent use of frameworks, these inconsistencies not only "hurt" the legal certainty of the government procurement rules as a whole but also create an obstacle to the development of frameworks.

On account of the above, framework agreements lack the adequate legal basis as a separate method. When they are considered as part of open tendering, their operation may be in breach of the current government procurement rules in many aspects. MOF is argued to be inextricably relevant to the uncertain legal status of frameworks. As mentioned earlier, it is suspected of choosing not to authorise or regulate frameworks to escape from the related disputes and criticism. On the other hand, it recognises the potentials of frameworks and may wish to continue benefiting from the cost savings associated with volume purchasing and administrative efficiency. To aver the risks of framework agreements, it promotes the use of other

[88] *Measures on Administrating the Government Procurement Information Publicity*, No. 19 [2004] of MOF, articles 10, 11
[89] *Ibid,* article 12

centralised procurement techniques, such as Bulk Centralised Purchases and Electronic Marketplace, but "quietly" allowing the use of frameworks in reality.

6.2. Defective Organisation and Management of Framework Agreements

The inconsistent organisation and management of framework agreements have become one critical obstacle to achieving their potentials in Chinese government procurement. This problem primarily derives from the underlying fragmented administrative system of China's government procurement and can be mainly manifested in three aspects.[90]

6.2.1. Unclear role-separation between finance departments and CPAs

As explained in Chapter IV, the *GPL* requires the separation of roles between the user (government agencies and public institutions) and purchaser (CPAs), and that between the purchaser and the supervisor (finance departments) in centralised procurement. Such role separation is intended to provide check-and-balance and for efficient implementation. Given that, CPAs should have independent legal personality in

[90] See Ch. IV section 3 above.

carrying out centralised purchases, supervised by but not subordinate to the finance departments.[91] The role separation between purchaser and supervisor appears to have few problems at the central level. At the local level, however, CPAs are under budgetary control and many of them are set up by or attached to the local finance departments, spelling doubts about their independence. The finance departments are found to have often intervened in the operation of framework agreements. For instance, it is common that the local finance branches, not the CPAs, determine the products and services to be procured through framework agreements-the coverage of frameworks.

The intervention of the finance departments, firstly, is in breach of the *GPL* which expressly prohibits the supervision authorities from undertaking procurement activities. Furthermore, the local finance departments arguably lack sufficient procurement expertise and competence in making sound procurement decisions.

Determining the coverage of frameworks is more challenging than expected, as the process involves many tasks, such as sub-categorising the subject matter and defining the minimum technical requirements. In practice, however, relevant officials in the finance departments are observed to rely on past

[91] According to article 16 of the *GPL* and article 12 of the *IRGPL,* CPAs are defined as public bodies with independent legal personalities.

practices rather than effective demand and market analysis and assume that the items that are likely to be frequently needed and, therefore, can be appropriately procured through framework agreements.[92]

The problematic check-and-balance on the roles between CPAs and finance departments mainly derives from their uneven institutional status. At the local level, finance departments hold control of the budget and are considered one of the most powerful government agencies, whereas CPAs tend to have little voice.[93] According to an official from a local CPA, "We mostly follow the decisions of the provincial finance department. For example, when they decided to extend the duration of the existing framework agreements for one more year, we will do as they request and won't set up a new framework agreement."

6.2.2. Inconsistent management of CPAs

Inconsistent management of CPAs is another problem that adversely impact the beneficial use of framework agreements. There is no unified system that manages all CPAs nationwide, as a result of which CPAs in different localities operate

[92] Three participants expressed the identical view that local finance branches deliberately draft their centralised procurement catalogues and determine the products and services subject to framework agreements. One of the three further stated that the officials within finance branches generally do not have the market intelligence to draft the coverage properly.
[93] Two participants affirmed this viewpoint.

independently and are subordinate to different leading authorities, with different agendas.[94]

The administrative inconsistency could have artificially created barriers for the information sharing, talent exchange, standardisation of procurement language and the uniformity of IT infrastructure, and may, therefore, have an adverse impact on the development of framework agreements. The lack of interoperability between various online procurement platforms established in different localities could provide an example of the administrative inconsistency.[95]

Furthermore, CPAs in China are financed by public budget and are organised and managed just like other ordinary government agencies. They are staffed by ordinary civil servants. Given the organisation and funding model, together with the mandatory use of framework agreements as explained in section 3 of this chapter, CPAs arguably lack proper and genuine incentives to seek optimal procurement outcomes but to ensure procedural compliance. As further discussed in section 6.6 and 6.7, CPAs are considered less effective in training and hiring procurement expertise and professionals.

[94] See Ch. IV section 3.3 above.
[95] P. Wang, "Development of Electronic Government Procurement in the People's Republic of China" (Consultant's report to Asian Development Bank, October 2011)

6.2.3. Unclear dispersal of responsibility between CPAs and procuring entities

In the context of framework agreements, the roles and responsibilities between CPAs (purchaser) and procuring entities (user) are not clearly divided, which may adversely impact the overall efficacy of frameworks, for instance, causing confusions on suppliers in lodging complaints.

As explained in section 4, CPAs are in charge of concluding framework agreements with the suppliers for the use of procuring entities. It is unclear whether they act as the principal or as an agent on behalf of procuring entities. Such legal ambiguity may lead to disputes between CPAs and procuring entities regarding the liability in case of complaints. In reality, an aggrieved supplier may find it difficult to identify the right party to file a challenge. Such uncertainty may, on the one hand, be an excuse for the relevant entity to evade its liability for handling the dispute, and on the other may put the review entity at the risk of being alleged as nonfeasance.

Therefore, a clear division of the responsibilities between CPAs and procuring entities in the case of framework agreements is necessary to reduce the above risks. Further efforts should be devoted as to how to objectively divide up the responsibilities to reflect a fair distribution of risk. While a CPA is the primary operator of a framework agreement and therefore

largely responsible for its own inappropriateness, it seems unreasonable to hold it accountable for all the problems that may emerge throughout the procurement process. On this point, China is suggested to learn from the EU's approach. Under the EU Directives, procuring entities are left with the responsibility for the parts of the procedure it conducts, especially regarding call-offs under a framework agreement.[96]

6.3. Lack of Rationalising and Balancing Objectives in the Use of Framework Agreements

It is argued that the Chinese governments have not adequately pondered the different procurement objectives in the cases of framework agreements, *a fortiori* striking a proper balance between them, especially between anti-corruption on the one hand, and efficiency on the other.

Corruption in public procurement is a worldwide problem and presents challenges in almost all procurement systems.[97]

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[96] *The 2014 Public Sector Directives*, Article 37(6)

[97] Whilst avoiding corruption is not explicit made a procurement objective in the EU and US system, it is a primary one in the UNICTRAL *Model Law*. For corruption in public procurement, for instance, see G. M. Racca and C. Yukins (ed.), *Integrity and Efficiency in Sustainable Public Contracts: Balancing Corruption Concerns in Public Procurement Internationally*, (Bruylant, 2014); OECD, *OECD Principles for Integrity in Public Procurement,* (OECD Publishing, Paris, 2009); The ADB/OECD Anti-Corruption Initiative, "Curbing Corruption in Public Procurement in Asia and the Pacific Progress and Challenges in 25 Countries", Manila: ADB/OECD, 2006; M. Hafner, J. Taylor *et al.*, "The Cost of Non-Europe in the area of Organised Crime and Corruption: Annex II– Corruption", (CA: RAND Corporation, 2016). Corruption has characterised public procurement in African countries. See B. Basheka, "Public

In China, this problem tends to be more severe than in many jurisdictions. Framework agreements are usually associated with embarrassing corruption reports and bribery scandals that prompt expressions of public dismay and criticism. For instance, in 2011, the Finance Bureau of Fushun, Liaoning Province was reported to have purchased Apple's iPod touch devices under the name of "flash sticks".[98]

Framework agreements are particularly "vulnerable" to corruption by virtue of their inherent flexibility and uncertainty. The lack of transparency and inadequate supervision, especially at the second stage, further create opportunities for rent-seeking and irregularities. Therefore, curbing corruption is an indubitable necessity and can be given more emphasis than it deserves in its own right in framework agreements.

In light of the notorious reports, perhaps to restore or enhance the public trust in government procurement, the government chose to prioritise anti-corruption and integrity among other procurement objectives, especially in centralised procurements.[99] The mandatory use of open tendering to

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Procurement Reforms in Africa: A Tool for Effective Governance of the Public Sector and Poverty Reduction", Ch. 6 in K. V. Thai (ed.), *International handbook of Public Procurement* (2009, CRC Press)

[98] P. Xia and C. Han, "Government Tendering: The Volume-discount Price Exceeds the Retail Price", *Oriental Outlook* (in Chinese, April 21, 2011), pp. 33-34

[99] As commentators submitted, Chinese public procurement rules are grounded on the "anti-corruption" goal. See P. Wang, C. H. Bovis and X. Tu, "A Comparative Analysis of Utilities Procurement in EU and China",

conclude frameworks in most cases demonstrates the government's attempt to deter corruption through stringent transparency and competition. However, as discussed in section 6.5, there is uneven transparency between two stages of frameworks, and the second stage is often operated "below the radar", which is saddled with transparency deficiency.

Moreover, the need for integrity does not necessarily make it prevail over other procurement objectives, and there is no evidence showing the priority is determined based on any trade-offs between them.[100] As shown in history, efficiency and flexibility used to be the main reason for the rapid take-up and popularity of frameworks at all levels.[101] Efficiency is further considered as the "core" and primary motivation of using frameworks. However, administrative efficiency comes at cost, to achieve which, for instance, transparency may be exempted and integrity be compromised. Similarly, allowing challenges

component 5 of *A Report Prepared for EU-China Trade Project* (II) (August 2013); D. J. Mitterhoff, "The Four into One Platform: New Reform Initiatives Compound China's Dissected Public Procurement Governance", (May 1, 2012) U of Maryland Legal Studies Research Paper No. 2012-43; F. Cao and F. Zhou, "Internationalization of Public Procurement Law and Relevance of International Norms and Frameworks: The Case of China", Ch. 14 in A. Georgopoulos, B. Hoekman and P. C. Mavroidis, *The Internationalization of Government Procurement Regulation* (Oxford, 2017) p.395

[100] Five participants agreed that anti-corruption is the top objective in government procurement. In fact, reacting to corruption scandals through measures such as introducing new measures or guidance is common worldwide, including in developed systems. See J. Branstetter, "Darleen Druyun: An Evolving Case Study in Corruption, Power and Procurement" 34 *Public Contracts Law Journal* (2005), p.443.

[101] See the evolvement of framework agreements in Chinese government procurement in Chapter IV section 3.1 above.

against orders under framework agreements for the purpose of improving accountability would also inevitably impact administrative efficiency of the whole procurement process. All the interactions and dynamics need to be factored in when striking a balance between enhancing the integrity and ensuring flexibility in frameworks.

Besides, it is interesting to note that value for money, which is often the primary objective in many procurement systems,[102] may often be overlooked in Chinese government procurement. "Value for money" is not mentioned in the existing procurement rules, and there is limited Chinese literature that comprehensively analyses this objective.[103] In the context of framework agreements, value for money seems to be less concerned and may be sacrificed to achieve efficiency, which is considered the "core" of frameworks. The negligence of value for money may exemplify the general lack of market research and demand analysis (procurement planning) before the decision to use a framework and how to structure it in practice, as pointed out above.

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[102] S. Arrowsmith, J. Linarelli and D. Wallace, *Regulating Public Procurement: National and International Perspectives* (Kluwer Law International, 2000), pp. 28-31

[103] Chinese procurement officials may lack a proper understanding of value for money. For instance, in the interview, a senior procurement official, when asked about how to construe value for money, stated, "value for money means to get the goods and services of best quality, which can satisfy all users, without caring much about the price."

6.4. Over-Pricing Problems and Over-emphasis on Price Undercutting

Overpricing is a common problem in many procurement systems.[104] For instance, in the US, the Government Accountability Office (GAO) has repeatedly reported the overpricing issue under the GSA Schedules.[105] The problem (Tianjiacaigou), however, is arguably much severer in China, which is considered as one of the most intractable issues of using framework agreements, causing acrimonious debates about whether such procurement arrangements should be rescinded altogether.[106] According to a report by Chinese Academy of Social Sciences ("CASS"), over 80% of the surveyed items were paid at a price 1.5 times higher than the market.[107]

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[104] Overpricing is a common problem in many systems. See OECD, *Bribery in Public Procurement: Methods, Actors and Counter-Measures*, (May 31, 2007), at p.90; S. Pannell and R. Tiffen, "Managing the Risk of Procurement Fraud", (CIPFA and Local Government Association, July 2015).

[105] GAO, Contract Management: Opportunities to Improve Pricing of GSA Multiple Award, GAO-05-229 (February 2005), available at http://www.gao.gov/assets/250/245292.pdf (accessed Aug 28, 2018)

[106] See the Institute of Law of the CASS, "Investigation Report on Implementing Government Procurement in China", in *Blue Book of Rule of Law: Annual Report on China's Rule of Law* No.11 (2013, Social Sciences Academic Press), pp.294-319, available at http://www.iolaw.org.cn/showNews.asp?id=33660 (accessed Aug 28, 2018)

[107] The Institute of Law of the CASS, "Investigation Report on Implementing Government Procurement in China", in *Blue Book of Rule of Law: Annual Report on China's Rule of Law* No.11 (2013, Social Sciences Academic Press), pp.294-319. Although the research methodology of the report is questionable, it sharply demonstrates the overpricing problem in framework agreements.

Overpricing can be attributed to a number of factors, including the uncertainty regarding future needs, lack of oversight[108], the inadequate competition[109], the defect of the supplier review mechanism[110], market monopoly and price manipulation by manufacturers and large suppliers[111], collusion among the supplier parties[112], etc. On the other hand, however, it needs to be accepted that higher prices in some cases may be justified.[113] For instances, in frameworks of IT products that are subject to rapid updates by their nature, the interval between concluding frameworks and actual orders may lead to relatively high prices in part of the orders. Therefore, the duration for frameworks of IT products should not be long.

There is an undeniable need to rein in the overpricing problem, given its detrimental impact on integrity and expenditure saving. The first step may be to assess whether the price under framework agreements is overpaid, a practice which is missing in government procurement.

According to Article 17 of the *GPL*, any centralised procurement shall be made at a price lower than the average market price. The expression assumes that a price comparison should be carried out before finalising the price in orders under

[108] Eleven participants mentioned this factor.
[109] Three participants talked about this.
[110] Three participants stated this.
[111] Ten participants mentioned this factor.
[112] Four participants mentioned this.
[113] Seven participants mentioned this.

a framework agreement. Such a comparison could also be used as the basis to verify any suspected overpricing. The essence of the comparison would be to determine the base price and target price. However, the relevant laws and regulations are silent on how to define them.

Firstly, the base price cannot be determined in the context of framework agreements. Price, in the case of frameworks, can be manifested in two forms: the price established in the master agreement (referred to as the framework agreement price) and the price in a specific contract awarded (referred to as the award price). It is unclear whether the "price" in a procurement denotes the framework agreement price or the award price. Moreover, as pinpointed earlier, what the "average market price"-target price- means and how it can be objectively determined await further clarification under the current rules.

The term "average market price" seems to indicate "national pricing". Given the vast geographical spread of China, however, there is no national average price, and the prices in different regions may vary a lot. For instance, the delivery expenses are generally much lower in the East with its developed transportation conditions than in the mountainous West. The expenses will be reflected in the prices offered by the suppliers. It is thus unreasonable to rely on the price in one area to represent the average and use it as the national benchmark.

For the above, there is a lack of uniform and consistent comparability rules to determine whether the price under a framework agreement is fair or reasonable, and further to verify whether a purchase is overpriced or not. On the other hand, it is surprising that the legal ambiguity on this issue has long been overlooked and remains resolved until now.

Another concern with "pricing" is that the Chinese governments sometimes seem to go too far and seek the lowest price in the market to achieve public spending savings and to and/or to demonstrate their probity. Lowering prices is often the most intuitive indicator to showcase the efforts made and success as achieved by the governments in ensuring competition and combating corruption. However, a price lower than the average market price as required under the *GPL* does not necessarily mean the lowest price in the market.[114] It will be unreasonable and impossible to require every government purchase to be awarded at the lowest price.

More importantly, over-emphasis on undercutting prices may be counter-productive. Procurement frauds are highly likely when prices are forced too low for a supplier to make a reasonable profit. Based on the interviews, the following frauds

[114] The *GPL*, Article 17. In the US, similar doubts were raised regarding the "fair and reasonable" price in the GSA Schedules. It is emphasised that a "fair and reasonable" price is what is required under the *Federal Acquisition Regulation* 8.404 (d), rather than the lowest price in the market.

are identified as the most-common schemes associated with ultra-low pricing in framework agreements:

- Products substitution.[115] To maximise profit, a supplier may substitute products or materials of quality less than that specified in the framework. Alternatively, the supplier may use counterfeit or defective components, even posing a threat to user security.
- Charging a premium price for the after-sale service of the procured products.[116] A supplier may offer a low price of the base item under a framework agreement but then charge a high after-sale service price to recoup the lost profit.
- Price gouging.[117] Where price is established in the form of discount and no ceiling price is drawn, a supplier, at the call-off stage, may raise the price of a product to a higher level and then apply the promised discount.
- Out-of-scope orders.[118] Once a framework agreement is put in place, a supplier may, at the request of the procuring

[115] Three participants expressly mentioned this problem. For instance, as one participant stated, "…in a procurement project of computers based on framework agreements, we belatedly found that suppliers actually replaced the original memory stick and used an inferior one."
[116] Three participants mentioned this.
[117] Three participants mentioned this.
[118] One participant identified this. This problem also takes place in the US federal procurement. For instance, see the case *Western Pilot Service et. al*, B-415732 et. al, March 6, 2018. In this case, GAO (Government Audit Office) held that task orders were out of the scope of either the underlying IDIQ contract.

entities, deliver products or perform services that are beyond the original scope of the framework.

- Fictitious invoices.[119] A supplier may submit an invoice that is either false or inflated. This may emerge, for instance, when procurement officials are paid to turn a blind eye to the false information of invoices.

The above frauds may occur when a supplier acts unilaterally or colludes with a dishonest procurement official. In the latter case, though most of the irregularities are the results of individual activities of unethical officials,[120] the government still suffers political damage when the corrupts come to light. As a result, extensive time and resources are devoted to combatting frauds and restoring public confidence, adding to the overall cost of operating frameworks and undermining value for money and efficiency of the whole procurement process.

6.5. Lack of Transparency and Competition

One of the major problems with framework agreements, in Chinese government procurement, is the uneven transparency and ineffective competition.[121] Although open tendering is often made the default procedures to conclude frameworks with a

[119] Two participants identified this issue.
[120] Two participants stated that the corruptions identified in the frauds in more cases are individual dishonest acts of the procurement officials.
[121] Competition is considered "a key driver for achieving value for money" in framework agreements. G. L. Albano, and C. Nicholas, fn. 5 *supra,* at p. 172

view to maximising competition, the first-stage competition is argued to be flawed and less effective. The less than complete and precise description of what is to be procured in the solicitation is one of the contributing factors.

As explained in section 4 above, the information regarding the estimated quantity/ volume of future demands is generally missing in the solicitation (and framework agreement *per se*). The incomplete information poses difficulties for suppliers to assess whether they have interest to participate and how to prepare tenders. The suppliers, due to the uncertainty, are unaware of the scope and extent of the future tasks to be performed. They are less likely to estimate costs and profits objectively, let alone submitting best value offers that can reflect the actual requirements.[122] As a participant provides, "…suppliers submit fictitious tenders…".[123]

The uncertainty regarding the future tasks is likely to raise submitted prices.[124] Competing suppliers inevitably factor the uncertainty into their submissions and generally add on a risk

[122] An example of the solicitation notice is the "Notice of Inviting Tenders for 2017-2018 Framework Agreements on Information Products by Central Government Agencies" (in Chinese), available at http://oa.zycg.cn/article/show/456058 (accessed Sep 12, 2018). In the US, EU, and under the *Model Law*, there are express provisions regarding the contents to be included in solicitation in the cases of frameworks. The role and importance of information about demand characteristics has been analysed by Albano and Nicholas, fn. 5 *supra,* pp. 38-41

[123] This is quoted from a participant as a policy maker.

[124] See Albano, Ballarin and Sparro, fn. 12 *supra*.

premium on the offers to make sure there is enough room for recouping extra profits at the call-off stage. At the other end, competing suppliers may choose to offer an attractively low price for admission to the framework, but use other "tricks", i.e. the procurement frauds as mentioned above, to recoup the losses.[125] In either situation, the competition may be distorted.

Moreover, there is no requirement to restrict the number of suppliers admitted to a framework agreement, either maximum or minimum. As mentioned earlier, in practice, framework agreements are often awarded a large, perhaps excessively, number of suppliers. In an extreme case, all suppliers that have submitted tenders may be accepted. Apart from the difficulty to manage, the competition, in this case, is softened and becomes no more than a formality, further leading to onerous and lengthy ordering process at the second stage.[126]

A more intractable problem is the "transparency loophole" regarding the second stage, which may flaw the overall efficacy of framework agreements, especially where they are used on a centralised basis in China.[127] As explained above, there is no

[125] See Albano and Nicholas, fn. 5 *supra*, pp. 39, 131

[126] Albano and Nicholas submitted that choosing an appropriate number of awardees in a multi-supplier framework agreement is the key to balance the competition between two stages correctly. See Albano and Nicholas, fn. 5 *supra*, p.131

[127] Ten participants raised the issue of insufficient transparency in call-offs. It is reported that centralised purchasing bodies/agencies are assessed to be "less transparent, less fair and more bureaucratic" in operating centralised purchases, including framework agreements. See Europe Economic Market

requirement to advertise any up-coming awards under frameworks (except for when electronic reverse auctions are involved, and all suppliers are invited to bid). It is highly possible that the supplier parties other than the contractor have no idea that there was a call-off when the order had been delivered already. For more than a decade, the orders issued within frameworks had been entirely exempted from the transparency requirements. While publicity of procurement information is considered one of the most efficient and important methods to combat bribery and corruption,[128] the lack of transparency leaves room for rent-seeking opportunities and irregularities. The risk may particularly increase in direct awards, where the procurement entities are free to choose the supplier that they consider appropriate for the order. According to one supplier participant, "the flexibility in call-offs has been turned into a 'green passage' for the procuring entities to satisfy their own personal preferences and individual interests (author's translation)"[129].

2004/10/D, *Evaluation of Public Procurement Directives* (September 2006), available at https://ec.europa.eu/docsroom/documents/15449/attachments/1/translations/en/renditions/pdf (accessed July 29, 2018). Lack of transparency is also a common problem in the use of framework agreements in the EU and US. See S. Arrowsmith, *The Law of Public and Utilities Procurement* (2014) Ch.13; C. Yukins, "Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting" 37 *Public Contract Law Journal* (Spring 2008), p.3

[128] F. Cao and F. Guo, "Controls and Litigation of Public Contracts in China", in L. Folliot Lalliot and S. Torricelli, *Oversight and Challenges of Public Contracts* (Bruylant, 2018), p.325

[129] The Chinese text is "协议供货的自由弹性变成了很多单位满足个人喜好和利益的绿色通道".

Furthermore, the second-stage competition where involved can be flawed by the transparency "loophole" and may become meaningless. Intuitively, some suppliers, in order to know contract opportunities, may be lured to bribe the procurement officials and "lobby" for receiving orders. Moreover, rather than fair competition, Chinese businessmen, or many of them have long attuned to competition on the relationship, known as "guanxi competitions". As a result of the above, it is difficult to contemplate that competitions can always deliver value for money and lead to optimum procurement outcomes.

It is reiterated that since September 2017, awards made under framework agreements should be made public on the designated media with the prescribed contents included in the notice.[130] Although the new information obligation is believed to be for the purpose of combating corruption, it indicates that the Chinese government has recognised the issue of lack of transparency and started to address it. Such a requirement also reflects that in China, electronic communication has already been developed; otherwise publishing notices regarding all the orders under frameworks would be incredibly costly and onerous. No further guidance is provided about how such

[130] See "Notice of MOF on Further Implementing Information Publicity of Government Procurement Activities", No. 86 [2017], (in Chinese), available at http://www.mof.gov.cn/gp/xxgkml/gks/201705/t20170508_2596044.html (accessed Sep 30, 2018)

publication should be implemented. The quality of implementation, therefore, varies amongst different governments. For instance, in Zhejiang Province, all results of awards made under frameworks at the provincial level should be published on the designated media and are fully accessible to the public, just like other procurement contracts.[131] In contrast, at the central government level, only the registered suppliers and relevant procuring entities, not the general public, have access to the information of orders within frameworks.[132]

6.6. Lack of Capable and Professional Procurement Human Resources

Almost all the problems encountered in framework agreements can be partly attributed to the lack of capability and expertise in Chinese procurement.[133] The shortage of qualitatively and quantitatively adequate procurement capacity has become one major obstacle to the future reform on government procurement.

Firstly, centralised purchasing agencies (CPAs) lack procurement competencies and skills to achieve optimal

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[131] Available at http://www.zjzfcg.gov.cn/purchaseNotice/index.html?_=1537352833698 (accessed Sep 29, 2018)

[132] The login page is available at http://www.zycg.gov.cn/unified_login_page (accessed Sep 28, 2018)

[133] Seven participants held that the general lack of procurement knowledge is one main factor leading to the problematic use of framework agreements.

outcomes in centralised procurement, for instance, in analysing and defining the demands, conducting market analysis, drafting procurement documents, evaluating tenders and providing instruction to procuring entities. The challenge can be increased in framework agreements which are more complex to address due to their two-stage operation. As explained earlier, CPAs in China are staffed with ordinary civil servants. The procurement officers tend to learn procurement by practice instead of obtaining professional qualifications. Their tasks, therefore, are more of secretary natures and focus more on ensuring compliance with the procedures, rather than on making strategic procurement decisions. It is argued that procurement in China is more considered as a process-oriented "back office" support function and has a low profile, particularly at the local level.[134] By contrary, in the EU and US, CPAs are contemplated to operate as a knowledge centre of expertise within the public sector and would involve various competencies and skills to operate framework agreements successfully.[135]

Secondly, CPAs are less effective in attracting and training procurement experts and professionals. There is no career path for public procurement officials in China at the moment. There

[134] Seven participants held this view.
[135] OECD, "Centralised Purchasing Systems in the European Union", (2011) SIGMA Papers, No. 47, OECD Publishing, p.66, available at http://dx.doi.org/10.1787/5kgkgqv703xw-en (accessed Sep 29, 2018)

is not much difference in treatment, in terms of career development and salary, between an ordinary procurement officer and a procurement expert, or between a procurement officer and an ordinary public official.[136] An officer without procurement qualification or relevant education background can be designated to undertake procurement activities. There is no remuneration structure or career ladders that can attract procurement professionals and motivate them to achieve the best value.[137]

Furthermore, a lack of legal expertise is also a common deficiency. Government procurement in China is more relevant to the area of public administration rather than law. According to one participant in the interview, in the process of drafting procurement policies or relevant measures, one or none legal expert has been involved.

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[136] In the view of some academia, the centralised procurement agencies are "less effective in hiring well-trained experts because in practice the salary of the employees is comparable to that of civil servants." See N. Philipsen, S. E. Weishaar, G. Xu, *Market Integration: The EU Experience and Implications for Regulatory Reform in China* (Springer, 2005), p.114

[137] In the US, the lack of adequate salary structure and career path for procurement professional has been identified as a factor leading to the shortage of competence workforce. See United States Office of Management and Budget. Acquisition Advisory Panel, *Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress*. (Washington, D.C.: Acquisition Advisory Panel, 2007), p.337. Furthermore, it is suggested by OECD that providing attractive and competitive career development options is a key factor to enhance the professionalisation of the procurement workforce. See OECD, *Public Procurement in Nuevo León, Mexico: Promoting Efficiency through Centralisation and Professionalisation*, OECD Publishing (2018, Paris) p. 116, available at http://dx.doi.org/10.1787/9789264288225-en (accessed Sep 26, 2018)

Besides, public procurement remains to be a neglected area of study and academic research, although government agencies and practitioners have worked hard to improve procurement practices.[138] In China, only a very few higher education institutions have recognised the educational needs of public procurement expertise and have set up courses in this area.

It is generally acknowledged that having a cadre of procurement professionals is essential for a sound public procurement system. The US has relied on its experienced and well-managed procurement workforce to deliver positive contracting outcomes.[139] There is an urgent need for China to take prompt measures to build procurement capacity and the process will require extensive resources, time and efforts on a continual basis.

6.7. Lack of Proper Incentives by Various Stakeholders

Government procurement, as Gordan and Racca submitted, "requires managing conflicting interests among stakeholders to

[138] This negligence also existed in the US but twenty years ago. K. V. Thai, "Public Procurement Re-examined", (2001) 1 *Journal of Public Procurement* 1, pp. 9–50

[139] D. I. Gordon, "Protecting the Integrity of the U.S. Federal Procurement System: Conflict of Interest Rules and Aspects of the System that Help Reduce Corruption", Chapter 4 of J. Auby, E. Breen and T. Perroud (eds.), *Corruption and Conflicts of Interest: A Comparative Law Approach* (Edward Elgar, 2014)

achieve common goals, and it is very political by its nature".[140] In the context of framework agreements, the major stakeholders include the government as a generic term, the suppliers, the public, the media and other third-party bodies. The success of a framework agreement is hinged on the extent to which trust and corporation can be obtained from them. However, it is argued that the major stakeholders in Chinese government procurement, including framework agreements, have skewed incentives and they are less engaged and coordinated in the procurement process.[141]

As a multifaceted stakeholder, the government includes finance departments (supervisors of framework agreements), CPAs (implementer of framework agreements) and other government agencies (end users). Within the finance departments, the procurement (supervision) division tend to have a low profile, as pointed out in section 6.6 above. Compared with other fiscal functions such as taxation, procurement has been given too little care by the top leadership,

[140] D. I. Gordon and G.M. Racca, "Integrity challenges in the EU and U.S. procurement systems", Ch.1 in G.M. Racca and Christopher R. Yukins (eds.), *Integrity and Efficiency in Sustainable Public Contracts – Balancing Corruption Concerns in Public Procurement Internationally* (Bruxelles: Bruylant, 2014), p. 138. For more discussion about the stakeholders and their interests in public procurement, see S. L. Schooner, D. I. Gordon, and J. L. Clark, fn. 32 *supra*, 111

[141] J Gutman observed that "the key to addressing public procurement as the Achilles' heel of governance is the broad commitment and participation of all stakeholders" in the "Is There Room for Discretion? Reforming Public Procurement in a Compliance-Oriented World", Global Economy and Development Working Paper (74) (May 2014).

which may impair the incentive of the procurement (supervision) divisions to revamp framework agreements, especially in light of the public criticism.

Regarding CPAs, they operate like other government agencies and financed directly from the government funds. Given their organisation form and the finance model, together with the mandatory use of framework agreements, CPAs are not exposed to any form of competition and are less motivated to optimise the use of framework agreements and to maximise their benefits.[142] Moreover, in a "no carrots but only sticks" situation, they are less likely to be rewarded for delivering more positive procurement outcomes but will be held accountable for any inappropriateness. Therefore, they are less motivated to "innovate" to address the challenges but focus more on procedural compliance.[143]

As for the government agencies and public institutions as users of framework agreements, they are interested in quickly receiving the items as requested.[144] In the context of

[142] OECD surveyed the organisation forms of the centralised purchasing bodies/ agencies (CPBs) in the EU countries and how these agencies are financed/funded. According to the study, the most common organisation form for CPBs among the countries studied is the limited company. With regard to the finance model, funding by service charges remain the dominant financing method, whereas there are countries where CPBs are directly financed from government funds. They "all seem to work" in their systems, with respective pros and cons. See OECD, fn. 135 *supra*.
[143] Yukins analysed the issue of underinvestment in public procurement in C. R. Yukins, "A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model" (2010) 40 *Public Contract Law Review*, p.533.
[144] Five participants agree on this viewpoint.

framework agreements, user entities may bring some personal preferences, more or less, in issuing orders. In the absence of adequate monitoring, the discretion may be abused, leading to irregularities, i.e. favouring or colluding with specific suppliers.

Moreover, the public officials as a whole, especially the leaders, have the personal interest in maintaining their positions. [145] While anti-corruption is made the priority procurement objective, rather than procurement outcome, they tend to err on the side of caution and showed propensity of averring risks.[146] According to six participants in the interview, they tried to avoid making decisions with a view to avoiding potential challenges from suppliers and delay of the procurement process, for which they would be held accountable, irrespective of the outcome being good or not.[147] As Schooner emphasised, "improper obsession with risk avoidance can

[145] Schooner, Gordon and Clark, fn. 32 *supra.* According to the US political scientist Darrel West, "government bureaucrats know that a failure gets you on the front page of the newspaper; ten successes probably don't. And so there are kind of skewed incentives against risk-taking in the public sector". See J. Gutman, "Is There Room for Discretion? Reforming Public Procurement in a Compliance-Oriented World", Global Economy and Development Working Paper (74) (May 2014).

[146] *Ibid.* W. Debevoise and C. R. Yukins, "Assessing the World Bank's Proposed Revision of Its Procurement Guidelines" 52 The Government Contractor (2010) 21, at p.1; S. Kelman, "Procurement and Public Management: The Fear of Discretion and The Quality of Public Performance", (American Enterprise Institute, 1990)

[147] D. J. Mitterhoff, "China - Waiting for Leviathan: A Note on Modern Wo-Er Trading Co Ltd v Ministry of Finance of the People's Republic of China" (2013) 3 *P.P.L.R*, at p NA56. In fact, the fear of decision-making and responsibility avoidance is a problem in many systems. See S. Kelman, fn. 146, *supra*; D. C. Mishra, "How to Reduce Fear of Discretion in Public Procurement: Lessons from MDB-financed Projects", Conference Paper Presented at PPGR: VIII, 12-13 June 2017.

suffocate creativity and leads to the ineffective procurement system".[148]

On the supply-side, suppliers have an interest in making profits, and they are absolutely entitled to do so provided they act in good faith. However, in light of the inadequate supervision in Chinese government procurement, suppliers are likely to seek illegal profiteering in framework agreements, which can be demonstrated by the fraud schemes as identified in section 6.4.

Apart from the above parties involved, the general public is also a stakeholder outside framework agreements. As the taxpayers, the public has an intrinsic interest in knowing how the public funds are spent.[149] In China, from the perspective of the public, framework agreements are often associated with corruption and irregularities. Such stereotype may be mainly attributed to the lack of confidence in government procurement in general.[150] According to Kelman, "…the public tends to exaggerate the problem more than practitioners within government underestimate it".[151]

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[148] S. L. Schooner, "Desiderata: Objectives for a System of Government Contract Law" (2002) 11 *P.P.L.R*, p.109

[149] It is submitted by Yukins that, the public has several basic expectations, including minimising cost and integrity of avoiding corruption. See C. R. Yukins, "A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model" 40 *Public Contract Law Review* (2010) 533, at p.74

[150] Eleven participants held this view.

[151] S. Kelman, fn. 146 *supra.*

The media, as another outside stakeholder, plays a significant role in monitoring and affecting procurements in the way of providing information to the public. On the one hand, any impartial comments and criticism about framework agreements should be encouraged, which can feed into the future improvements.[152] On the other hand, however, it is problematic if the media deviates from objectivity and delivers opinions to gain clicks and for the eye-catching effects. Taking the information out of context is a common trick of this kind. For example, a report about framework agreements may reveal a large overall raw amount of an order under a framework agreement without any breakdown or explanation that the award is compliant with the rules. In that case, the public is highly inclined to focus only on the gross value and suspecting any corruptive practice. It is thus suggested to hold the media accountable for their what and how to report, as their views and how they are present do affect how the public perceives framework agreements.[153]

Taken into consideration of the above, the quality of procurement outcomes in framework agreements requires a broader look at the roles and responsibilities of the various

[152] As Yukins said, "…an active press provides low-cost monitoring (and thus reduces risk), much as whistle-blowers serve as surrogate monitors and enforcers of the principal's interest…" in C. R. Yukins, fn. 149 *supra*, p.71

[153] Eleven participants in the interview stated that the negative and sometimes biased media reports are a contributor to the public prejudiced perception about government procurement.

stakeholders involved in the entire procurement cycle. The active participation of all stakeholders is essential, and each of them should correctly and clearly understand and recognise their role in as well as their impact to the whole procurement process.

6.8. Negative Impacts of the Budget System

As a participant stated, "…the current problems in government procurement, including the failures of using framework agreements, are closely linked to China's budget system" (author's translation).[154] It is argued that some problems of the budgeting management, particularly the poor compilation and ill-disciplined execution, may impact the procurement results under framework agreements. [155] Although procurement planning and budgeting are closely related but are not properly integrated in practice.

The current law on government procurement does not specify how to compile government procurement budget and the extent to which it should be elaborated.[156] In reality, the

[154] The Chinese text is "政府采购现有的问题，包括协议供货的失败，都跟财政制度紧密相关".
[155] Eight participants held this viewpoint.
[156] Article 6 of the *GPL.* There are no detailed provisions regarding compiling government procurement budgets. See MOF, "Report of the Training Session on Government Procurement Legal System in Brazil", Part 5 of *The Government Procurement System in Brazil and Its Lessons for China* (2007), available at

budgets for government procurement, especially at the local level, are drafted vaguely, and detailed spending plans are usually missing. The uncomplete and vague budget creates breeding grounds for the improper use, especially the overuse of frameworks. The vaguer the budgets compilation, the more difficult to hold the government accountable for the expenditure, and the higher the risk of corruption.

The "rough" budgets can particularly occur in framework agreements, which are inherently flexible and uncertain to some extent. The general missing information regarding the estimated quantity and value of future purchases and the less proper/accurate description of the subject matter, as mentioned in section 4, arguably indicates the budget compilation is less effective in the cases of framework agreements.

At present, many Chinese local governments adopt the "base plus incremental" budgeting method to draft and manage government procurement budget.[157] By this method, the budget is drafted using the existing budget as a basis with incremental amounts added for the upcoming fiscal year. It is argued that such a budgeting method leads to a "spend or loss" mentality. As a result, to ensure "sustainably" adequate budget allocation, government agencies, first, tend to over-claim

http://www.mof.gov.cn/zhengwuxinxi/guojijiejian/200806/t20080603_44696.html (accessed Sep 27, 2018)

[157] One participant highlighted this.

budgets higher than necessarily needed in fact. They are "encouraged" to spend all budgets to ensure a reasonable appropriation in the next fiscal year, with few incentives of cost-savings. According to a participate from a procuring entity, "…we strive to use every budgetary penny at the end of the fiscal year because any fiscal surplus means that the budgeting was drafted poorly, and that budget approved for next year would decrease."[158]

Framework agreements arguably provide a good way out for procuring entities to use the surplus, because firstly, in framework agreements, the submitted quantity/ volume of future purchases need not be precise and the discrepancy between the submitted and actual demands is more acceptable. Secondly, the budgets for framework agreements are vague and broad, leaving additional room for the unnecessary purchases. In the absence of adequate oversight, it is highly possible that framework agreements are used as a pretext for misappropriations for other improper purposes.

The above indicates that not all problems that arise in framework agreements are only about procurement. Some of the problems may derive from the weak linkages of

[158] Ma and Yu considered that most of the problems identified in the budget execution may derive from and reflect the deficiencies in the budget compilation. See "Why Money Cannot Be Spent as Budgeted? Lessons from China's Recent Budget Reforms" 24 (Spring 2012) *Journal of Public Budgeting, Accounting & Financial Management* 1, p.104

procurement and the supporting systems, such as the budget management or the challenges in the supporting systems, such as the general "rough" budget planning and ill-disciplined budget execution. The effectiveness of government procurement, including framework agreements, requires more efforts to improve the budget management and to integrate public procurement with budget planning.

7. Summary

This chapter has explored the current use of framework agreements in Chinese government procurement and analysed the legal issues and factual problems encountered in practice that may undermine their development. While some problems are "unique" for frameworks, such as overpricing, some may reflect the underlying concerns throughout the government procurement system, such as the lack of coordination between stakeholders and less effective supporting systems. In fact, there are also cultural elements that may have adverse impact on the achievement of benefits of frameworks, with particular regard to the indifference of the top leadership towards government procurement in China, probably due to the lack of understanding of this field.

Each of the problems can be detrimental and fatal to the whole procurement process, and the synergism of their interaction can be much severer. To iron out the existing problems and to ensure the appropriate use of framework agreements, it is necessary to provide a set of rules dedicated to governing and guiding framework agreements under a more coherent regulatory framework. It is equally important to improve the supporting frameworks, such as the budgeting, to heed more to the interaction between the public and the market, and to place more emphasis on coordinating various stakeholders in framework agreements.

Chapter VI. The Use of Framework Agreements in Procurement by Chinese SOEs

1 Introduction

Chinese SOEs are also the active user of framework agreements. For instance, as far as one central SOE-China Petrochemical Corporation (Sinopec)-is concerned, the proportion of supplies acquired through framework agreements increased from 46.3% in 2008 to 85.2% in 2013.[1] However, very little in the literature about public procurement is devoted to the analysis of the use of framework agreements by Chinese SOEs. Hence, this chapter seeks to examine how Chinese SOEs are using framework agreements in their procurements and to identify the main problems undermining the appropriate use of frameworks.

As explained in Chapter IV section 3.3.1, most of works procured by Chinese SOEs are related to infrastructure and utility projects that concern public interest, therefore largely falling within the mandatory coverage of the *TL*. However, their procurement of supplies and services first, lays out of the scope of the *TL* (for not being infrastructure and utility projects), and

[1] J. Qu, "Typical Problems of the Procurement Quality of Framework Agreements and their Countermeasures (2014) 4 *Petroleum and Petrochemical Material Procurement* pp. 76-78; See also H. Lin, X. Fu and X. Meng, "Primary Study on Framework Agreements and Tendering by SOEs" 2 (2016) *Tendering & Purchasing Management* (in Chinese), pp. 24-27

secondly is not regulated by the *Government Procurement Law* (for not being considered "government procurement").

2 Defining Framework Agreements in procurement by SOEs

As explained in Chapter IV section 3.3.1, Chinese SOEs, especially the ones affiliated to the central government (central SOEs), tend to conduct framework agreements following their own procurement rules. In reality, many terms are used by different SOEs to refer to framework agreements or the similar arrangements, including "framework agreements" (kuangjia xieyi), "framework bidding" (kuangjia zhaobiao), "designated providers with fixed price" (dingshang dingjia), "aggregated bidding" (jizhong zhaobiao), and "framework plus orders" (kuangjia + dingdan).[2]

It would be impossible to provide a comprehensive assessment of all the internal rules of Chinese SOEs, and most of the rules are not accessible to the public. Therefore, this research focuses on a few giant central SOEs as examples, whose procurement rules and practice demonstrate the

[2] The most frequently used term referred to framework agreements in procurement of SOEs is "kuangjia xieyi", which is verbally different from the term "xieyi gonghuo" in government procurement. In the interviews, two participants used the term "framework agreement tendering", one using designated providers with fixed price and another one using "framework plus orders".

consistent characteristics, and may have a significant impact on that of other SOEs. The internal rules of China Petrochemical Corporation (Sinopec) on framework agreements will be used as a primary example for better understanding. Sinopec is chosen because first it has a relatively long history and experience in using framework agreements, and secondly the procurement rules are accessible to the public.

- **Definition of framework agreements under the procurement rules of Sinopec**

Sinopec, established in 1998 by the state and now supervised by SASAC, is the largest oil and petrochemical products supplier in China with many subsidiaries and companies of which it holds controlling or minority interest.[3] It is the largest oil refinery company in the world and ranked No.4 of in the Fortune Global 500 in 2016.

Sinopec has been using framework agreements for more than a decade, mainly for purchasing supplies, and the scope of its use is expanding. In 2010, up to 75% of Sinopec's supplies were acquired through framework agreements.[4] In 2011,

[3] For more information about Sinopec, see http://www.sinopecgroup.com/group/en/companyprofile/AboutSinopecGroup/ (accessed Aug 17, 2018)
[4] P. Wang, C. H. Bovis and X. Tu, "A Comparative Analysis of Utilities Procurement in EU and China", (August 2013), p.134

Sinopec adopted the "China Petrochemical Corporation (Sinopec) Rules on Administrating Procurement Through Framework Agreements"[5], to govern the use of framework agreements specifically.

According to the Rules, framework agreement procurement refers to "a procurement method conducted for centralised procurement of supplies, by which well-performing supplier(s) are selected through open competition to award a framework agreement over a given period of time so that orders can be directly placed from the selected supplier(s)."[6] A "framework agreement" *per se* is separately defined as "a legally binding contract concluded between the purchaser and the supplier in writing".[7]

In general, SOEs use framework agreements in a similar way to government agencies in Chinese government procurement. In both areas, framework agreements involve two stages of operations and are mainly used to fulfil repetitive purchases of

[5] The Chinese term used by Sinopec is "kuangjia xieyi". The Chinese text is available at http://wenku.baidu.com/view/97c45e92bb4cf7ec4bfed04b.html?re=view (accessed Aug 19, 2018). The rules are claimed to have been modified, whereas the new version is not available to the public. In fact, the old version is not from the official source, but from the generic database.

[6] "China Petrochemical Corporation (Sinopec) Rules Administrating Framework Agreements Procurement" (Sinopec Rules on Framework Agreements), Art 1.1. The Chinese text is "框架协议采购是指集合物资需求，通过公开竞争选择业绩优秀供应商，签订一时时期采购协议，执行协议项下订单操作的采购方式".

[7] "Sinopec Rules on Framework Agreements", Art 1.2. The Chinese text is "框架协议采购是供需双方协商一致、以书面形式签订的、具有法律约束力的买卖合同".

goods and services.[8] Closed, multi-user and multi-supplier frameworks are also the norm of frameworks used by SOEs.

On the other hand, several nuances deserve particular attention here. Firstly, Chinese SOEs tend to consider framework agreements as a separate procurement method on its own even.[9] This is in contrast to the situation in Chinese government procurement where framework agreements, as explained in Ch. V section 6.1, are more regarded as a technique, used as part of other procurement methods mainly open tendering.

Secondly, the Sinopec rules expressly define a framework agreement (master agreement) concluded at the first stage is itself a contract (the same as the US approach explored in Ch. III). It follows that the orders issued at the second stage are execution of the contract.[10] In contrast, it remains unclear whether in Chinese government procurement a master agreement is a binding procurement contract. The fact that this issue seems to be ignored and has been rarely discussed in the literature is disappointing.[11]

[8] See Wang, Bovis and Tu, fn. 4, *supra*.
[9] Five participants confirmed this viewpoint.
[10] Y. Qiu, "Practical Application of Procurement of Framework Agreements in Energy Saving Lighting Energy Management" 16 (2014) 6 *Power Demand Side Management* 53-55, p.55
[11] As mentioned in Chapter IV section 5, it is not clear whether a framework agreement itself is a procurement contract in Chinese government procurement.

3 Grounds for Using Framework Agreements by SOEs

In practice, SOEs use framework agreements primarily in purchases of supplies and services but may also use them in works projects in very few cases.[12] Practice shows that framework agreements are most commonly used for procuring supplies in the following circumstances:

(i) Framework agreements may be used in procurement of standard supplies that are commonly used, the need of which is expected to arise on a repeated basis. These supplies can be obtained from more than one source in the market.[13]

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[12] Three participants highlighted the use of frameworks in procurement of supplies and services. See also X. Sun, "Practice of Supply Chain Contract Theory-Framework Agreements Procurement", 13 (2010) *Manager" Journal* 120, p.120; F. Wen, "Analysis on Using of Framework Agreements to Improve Procurement of Works and Services by Power Grid SOEs at Provincial Level" 10 *Modern SOE Research* (2015) pp.170-172. There is literature also mentioned the use of frameworks in procurement of works. For example, see H. Sun, "Thoughts on the practice of the Procurement of Works Based on Non-tendering Procedures by Chinese SOEs", 2017 (7) *Tendering and Bidding*, pp. 27-30 (in Chinese). Moreover, framework agreements are also mentioned in a ministerial rule adopted to govern the procurement of works in the communication area, including that by SOEs. See Chapter IV section 3.3.

[13] Article 1.6 of the Sinopec Rules; X. Sun, fn. 12, *supra*, p. 121; W. Song, "Brief Analysis on Application of Framework Agreements in Large Construction Projects", (2011) 8 *Manager' Journal*, p111, (in Chinese); G. Ma, "The Problem Analysis and Strategic Study of the Material Purchase of Lanzhou Petrochemical Company", MBA dissertation, Lanzhou University, China (2007) (in Chinese); R. Zhou and Q. Liu, "Discussion on the Standardisation of Material and Supplies Procurement From the Analysis of the Similarities and Differences between Procurement with Designated Suppliers at Fixed Price and Framework Agreements", (2012) 8 *Petroleum and Petrochemical Material Procurement*, 110 (in Chinese); H. Wang, "The Application of Framework Agreements in Petroleum and Petrochemical Enterprises", (2015) 5 *Refining and Chemical Industry* 71, p. 72, (in Chinese); Y. Chen, "The Application of Framework Agreements Tendering" (2016) 34 *China Market*, p.182 (in Chinese). It is particularly noteworthy that financial SOEs are encouraged to use request for quotation for the procurement of standard supplies according to Article 24 of the new "Interim Measures on Managing Centralised Procurement of Financial SOEs", No. 9 [2018] of MOF.

(ii) Framework agreements may be used to procure supplies with special technical requirements. The purchaser knows that certain type of supplies will be needed at some point but is not sure when and how many they will need them.[14] These supplies are only available from a restricted number of sources.

The well-known Kraljic Product Purchasing Classification Matrix (Kraljic Matrix)[15] classifies all supplies that a company purchases into four types based on profit impact and supply risk, including leverage items, strategic items, non-critical items and bottleneck items, as reproduced by Figure 6.1. As per the Matrix, supplies in the above circumstance (i) could be classified as leverage items that have the high-profit impact and low supply risk. These supplies can be easily purchased from multiple sources in the market.[16] Employing framework agreements, in this case, can allow SOEs to leverage their purchasing power and thus to obtain competitive price and terms.

The Chinese text is "集中采购项目符合货物规格、标准统一，现货货源充足且价格变化幅度小等条件的，经企业内部集中采购管理办法列明，可以采用询价方式采购". Disappointedly, framework agreements are not mentioned in this measure. Available at http://www.mof.gov.cn/zhengwuxinxi/caizhengwengao/wg2018/wg201803/201807/t20180710_2954886.html (accessed Oct. 10, 2018)

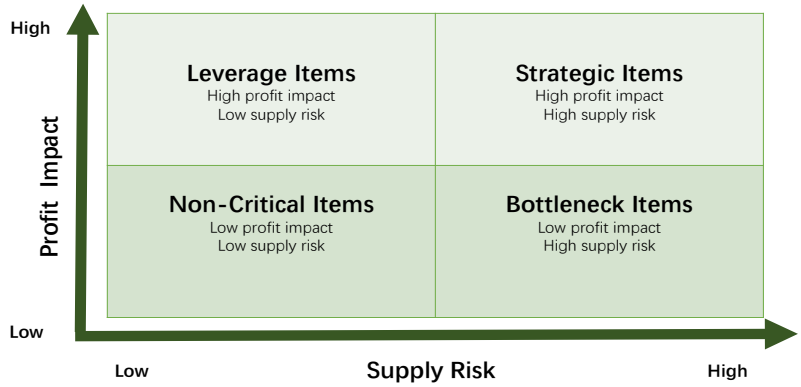
[14] See R. Ma, "The Problem Analysis and Strategic Study of the Material Purchase of Lanzhou Petrochemical Company", MBA dissertation of Lanzhou University, 2007 (in Chinese); X. Sun, fn. 12, *supra*, at p121

[15] P. Kraljic, "Purchasing Must Become Supply Management" (1983) 61 *Harvard Business Review* 5, pp. 109-117. See F. Wen, fn. 12, *supra*; Wen raised the idea of using Kraljic Matrix to classify the supplies that are appropriate being purchased through framework agreements.

[16] See F. Wen, fn. 12, *supra*.

The supplies in circumstance (ii) may fall into the category of bottleneck items that have a low-profit impact and high supply risk. Although they may not be needed frequently, they are critical to business productivity, and only a few suppliers can fulfil the particular technical requirements. The need of them is identified but the quantity of purchase and the time when the delivery will be called off is unknown. Therefore, concluding framework agreements with reliable suppliers, in this case, can effectively ensure security of supply and help SOEs establish a long-term relationship with strategic suppliers and optimise the supply chain.[17]

Figure 6.1 Product Purchasing Classification Matrix



Source: Peter Kraljic, "Purchasing Must Become Supply Management"

The main situation where SOEs use framework agreements is quite similar to those in Chinese government procurement, namely for repeated purchases of relatively standard goods and services. In addition, securing supply and developing long-term

[17] See R. Ma, fn. 14, *supra*. p.29; See also H. Lin, X. Fu and X. Meng, fn. 1 *supra*, p. 24

partnership are also a major motivation for SOEs to use frameworks. One caveat is that the above is the most-use circumstances of framework agreements by SOEs. In reality, SOEs may decide to adopt frameworks in other situations when they consider appropriate. Where frameworks are used to procure works, as mentioned above, their use may be caught by the *TL* and its implementing rules.

4 Operating Framework Agreements in Procurement by SOEs

Framework agreements by SOEs comprise two stages of operations: setting up a master agreement and issuing orders against the agreement in the call-off stage, similar to those in government procurement. In most, if not all, SOEs, there is a specific supply management and procurement department.[18] In the context of framework agreements, these procurement departments are tasked with concluding and maintaining framework agreements, performing the same role as centralised purchasing agencies (CPAs) in Chinese government procurement.

For large SOEs, particularly those central SOEs who have multiple affiliates across the country, such as Sinopec and China

[18] Hereinafter referred to as the procurement department.

Unicom, they often operate two layers/ levels of framework agreements in practice: (i) framework agreements at the headquarter/national level for the use of all affiliates; and (ii) framework agreements at the affiliate/ sub-central level.[19] According to the interview, the coverage of framework agreements at two levels cannot overlap, and affiliates can only establish framework agreements to purchase items that are not covered by the headquarter-level framework agreements.[20] The headquarter uses different methods to determine the items to be procured through the headquarter-level framework agreements, such as setting up a procurement catalogue.[21] Clearly defining the coverage between the two levels of frameworks can avoid having frameworks with overlapping scopes, thus reducing resources wastes. However, regarding frameworks at the headquarter level, given the considerable purchasing power of large SOEs, aggregating the needs of all the affiliates across the country has the risk of excessive concentration, which can facilitate the abuse of their purchasing power and distort the competition in the relevant market.

[19] According to six participants from four central SOEs in the interview, their enterprises operate two layers of framework agreements.
[20] Three participants provided this.
[21] In the interview, two SOEs set up their procurement catalogues to determine the coverage of their headquarter-level framework agreements.

4.1 The First stage: Setting up framework agreements

Large SOEs, such as Sinopec, usually require a cost-effective analysis before determining to use framework agreements for a procurement project.[22] Such requirement is considered a good practice that "forces" the procurement personnel to conduct careful planning and preparation, which is usually a missing practice in framework agreements in Chinese government procurement, as mentioned in Chapter V above. Despite the requirement, it is doubtful in reality whether the procurement personnel have properly conducted the market and demand research, as there is no proper monitoring and enforcement mechanism.[23] As a result, frameworks having too narrow or too broad specifications are likely, which may not attract sufficient competition and cause disproportional cost.

After deciding to use a framework agreement, the procurement department will develop a procurement plan based on the analysis result and the overall business plan.[24] In the process, the procurement department can specify the requirements, set up the terms and conditions to the extent of

[22] For example, see Article 3.1 of the "Sinopec Rules on Framework Agreements Procurement".
[23] The practitioners have complained that framework agreements failed to reflect the actual demands of users. See J. Qu, fn. 1, *supra.* pp. 76-78
[24] Z. Wu, "Analysis of Supplies Framework Agreement Procurement in Power Enterprises", (2011) 16 *Journal of Chongqing Electricity Power College*, p1 (in Chinese); J. Wang, "Understanding New Model of Supplies Procurement-Framework Agreements procurement", (2009) 12 *Modern Economic Information*, 127-128 (in Chinese)

known, determine the award procedures to be used to conclude the framework agreement, and how the ordering process operates.

SOEs are free to use any procedures they consider appropriate to establish a framework agreement, including open and restricted tendering, and other more flexible procedures, i.e. negotiations. In reality, Chinese SOEs are observed to favour restricted procedures, such as restricted tendering and negotiations.[25]

It makes sense that as "market players", many SOEs need additional flexibility to meet commercial needs. They are not looking for integrity, which is usually considered the priority objective in Chinese government procurement but attach more importance to efficiency and value for money. Full and open competition, in some cases, may be disproportionate to the value of the procurement and evaluating a large number of tenders post technical challenges to SOEs. Restricted procedures, thus, can effectively limit the number of participating suppliers, thus reducing the administrative cost and time that may incur. Moreover, restricted procedures are

[25] Y. Sun, "The Application of Framework Agreements Procurement", (2015) 6 *Petroleum and Petrochemical Material Procurement*; S. Chen, "Analysis of the Significance of Framework Agreements Tendering on Enterprises", (2014) 13 *Economic Vision*, pp. 64-65 (in Chinese)

more suitable for purchases of the "bottleneck" items that are only available from limited sources on the market.

Despite the above advantages, however, the procurement personnel in SOEs do not need to justify their decisions on using restricted procedures over open tendering based on careful analysis. It is possible that using restricted procedures is simply for convenience or to favour specific suppliers. At present, SOEs are still the primary receiver and spender of public funds, and their procurements involve a tremendous amount of money. It seems justifiable to require them to be responsible for at least minimum transparency and accountability.

Restricted procedures, although may conflict with the achievement of integrity, should be permitted as long as they are for legitimate reasons. The relevant practice in the EU on this issue may provide some insights here, As explained in Chapter III section 2, contracting authorities in the utilities sector are allowed more flexibility in procurement including framework agreements, who are free to use any procurement procedures, and negotiations at the call-off stage are permitted.[26] In the Chinese context, however, as discussed later in section 6, corruption is still a severe problem in Chinese SOEs, particularly in their procurement. It may be more

[26] As explained in Chapter III section 2, EU provides separate procurement rules in the public and utilities sector and allows for more flexibility in conducting procurement in the utilities sector.

appropriate to impose proper accountability and require them to justify the use of restricted procedure.

It is particularly noteworthy that Chinese SOEs usually invite the potential suppliers to participate in a framework agreement from their approved supplier lists ("Gongyingshangku").[27] For example, Sinopec relies on supplier lists to develop long-term strategic supplier partners and to optimise its supply chain management.[28] Supplier lists are a common procurement tool used by Chinese SOEs but are not permitted in government procurement. The different treatment of supplier lists in the above two areas is similar to that of qualification systems in the EU (in the public and utilities sectors).[29]

For SOEs, working with known and trusted suppliers is commercially justifiable and has the expected benefits, such as competitive prices, better quality and reassured security of supply, particularly when they have special requirement for the subject matter. On the other hand, however, using supplier lists,

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[27] Confirmed by six participants. See also H. Lin, X. Fu and X. Meng, fn. 1, *supra*, at p.25

[28] See Wang, Bovis and Tu, fn. 4, *supra*. at p. 134. According to Wang, in Nov 2010, Sinopec signed a 5-year strategic supply agreement with 25 suppliers (22 domestic suppliers and 3 foreign suppliers). In 2010, the contracts awarded to these strategic suppliers occupied 64.6% of the total centralised procurement volume. During the six years from 2004-2010, 64.6% of Sinopec's centralised procurement contracts were awarded to more than 20 strategic suppliers covering 95% of equipment, 90% of coal and 80% of steel purchased. See http://www.sasac.gov.cn/n2588025/n2588124/c4116521/content.html (accessed Sep 16, 2018)

[29] As mentioned in Chapter III section 3, in the EU, qualification systems are only regulated in the utilities sector but not in the general public sector.

especially mandatory lists, as the qualification process of frameworks may undermine effective competition, hampering value for money.[30] Typically, SOEs choose to advertise the framework agreement within the existing supplier lists and solicit tenders from the registered suppliers only. It follows that only the suppliers on the list would have the chance to award the framework; all other suppliers are excluded just because they are not registered even though they are qualified and can better meet the requirements.

While competition is deemed to be a key driver for realising value for money, creating barriers to entry at the first stage can prevent competition and lead to undesirable procurement results. Closed framework agreements *per se* may operate as a barrier to entry to the min-market for the subject matter of the framework within the duration. Using existing supplier lists as qualification process can further prevent and exclude potential suppliers from participating, entrenching the barriers to entry and facilitating collusion and corruption.[31]

Moreover, the anti-competitive impact may go beyond framework agreements and be externalised. The adverse

[30] S. Arrowsmith, J. Linarelli and D. Wallace, *Regulating Public Procurement, National and International Perspectives* (Kluwer Law International, 2000), pp. 639-645

[31] Barriers to entry is a pro-collusive features of public procurement markets. See G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press, 2016), pp. 186-188.

impact of framework agreements through demand aggregation may include opportunity costs of excluding potential suppliers from the relevant market, especially SMEs, causing oligopolistic and monopolistic market.[32] This is especially the case where the central SOEs in the utilities sector are often the dominant buyers of the relevant market.[33] Given the above, there is a need to enhance competition in framework agreements by SOEs, especially where supplier lists are used as part of the process, as suggested in Chapter VIII.

As mentioned earlier, SOEs usually regard a framework agreement itself as a contract, which therefore should be as complete as possible so that it can be enforceable under the *Contract Law*. For instance, Sinopec requires that a framework agreement should contain information including the technical specification, the information about the supplier, terms and conditions of future purchases including the estimated quantity, pricing, payment, delivery and schedules, duration, liability for any breach of contract, dispute settlement, etc.[34]

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[32] Albano and Nicholas provide that, the logic of the two-stage process of framework agreements is to create a new, temporary procurement market for the subject matter within its duration. The effects may not be "temporary" where the government is a dominant purchaser and its decisions may impact the shape of the market. See Albano and Nicholas, fn. 31 *supra,* p.214

[33] For example, there are only three major national oil SOEs in China, including China National Offshore Oil Corporation, China National Petroleum Corporation and Sinopec Group. The three SOEs are accepted as the dominant purchasers and have significant purchasing power in the relevant market.

[34] Four participants confirmed this. For more information about the terms that should be specified in the master agreement, see J. Li, "Transforming

Price tends to be a must-have term, like that in Chinese government procurement.[35] Similarly, it may but does not need to be a fixed price; SOEs may establish a pricing mechanism/ structure, based on which the exact prices can be determined in the future call-offs.[36] In reality, for those items with stable prices, SOEs prefer a fixed price in the agreement and do not allow subsequent adjustments.[37] For those supplies whose prices are volatile, such as steel and woods, SOEs tend to set up a pricing structure that correlates the frameworks to the market.[38] Besides, a ceiling price is usually established at the first stage to prevent any arbitrary rise in price in call-offs.

It is observed that SOEs are continually striving to rationalise pricing. For example, according to one interviewee, some SOEs are piloting a new Step-ladder Pricing (Jietibaojia) mechanism, which factors the demand quantity into the price in a call-off. It requires suppliers to offer different unit prices for different quantities. The price drop is inversely proportionate to the increase in quantity. By this mechanism, SOEs are expected to buy smarter and secure more favourable prices for larger quantities. It is considered these pricing mechanisms are

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Framework Agreements into Control-Management Model in Sinopec", *Sinopec Newspaper* (Jan 22, 2015) (in Chinese); L. Wang, "Brief Analysis on Application of Framework Agreements in Petroleum Enterprises" (2015) 10 *Petroleum and Petrochemical Material Procurement*, pp. 72-73 (in Chinese)

[35] Six participants all agreed with this.

[36] Z. Wu, fn. 24, *supra*, pp. 43-44

[37] Three participants mentioned this.

[38] Four participants provided this.

worthy of particular encouragement, reflecting the enduring efforts of Chinese SOEs to allow framework agreements to better reflect the market practice and reflect the features of call-offs, such as quantity. Their efforts and trials may provide some reference value for other legal systems on this issue.

It is common practice for SOEs to divide large purchases under frameworks into lots, and such division should also be clarified in the solicitation and master agreement itself. The main factors considered in dividing the lots include: the aggregated value, geographical distribution of purchasers (users), different technical competence and production capacity of suppliers. Practice suggests that SOEs use two main methods for lots division: (a) Fixed shares[39] and (b) geographical lots.[40]

(a) Fixed shares. The total demands under a framework agreement are divided into several lots, and each lot represents a pre-determined fixed share (either in volume or amount). The lots are allocated in accordance with the ranking of the evaluation results. For instance, a SOE determines to divide demands under a framework agreement into three lots, which comprise 50%, 30% and 20%. Based on the evaluation result, 50% is allocated to the first-ranking supplier and the second and third places were respectively 30% and 20%.

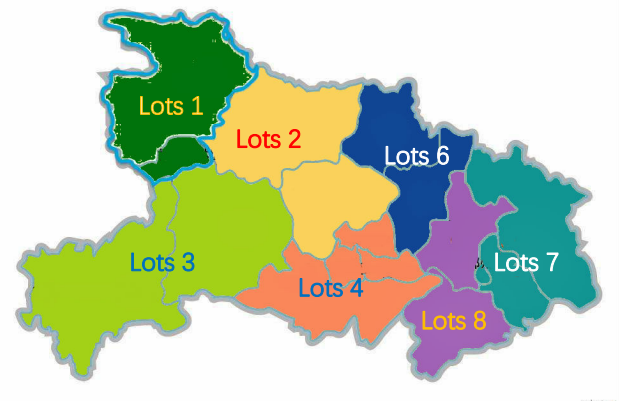
[39] One participant raised this method in the interview. This method has also been mentioned by Albano and Nicholas, fn. 31, *supra.* at p.67
[40] Four participants provided this.

(b) Geographical lots. This method is often used where the users of a framework agreement are geographically dispersed. The rationale is that the business area of suppliers is often smaller than the vast geographic span of users within a SOE, or suppliers can deliver better performance, i.e. in terms of delivery and inventory in a smaller area. Conducting geographical lots requires the procurement department to have a thorough understanding of the demands and agile market intelligence.[41] This division method is not seen in Chinese government procurement, because as explained in Ch. V, there is generally a framework agreement in each administrative area.

Figure 6.2 below shows a stylised example of a framework agreement of cables by a telecom SOE in Hubei Province. The total demands within Hubei are divided into 8 lots, based on the geographical distribution and quantities of expected needs. To secure supply, the SOE tends to have more than one supplier available in a geographic area.

[41] See Albano and Nicholas, fn. 31, *supra*. pp.296-297. They submit that the appropriate number of geographical lots should be the result of the trade-off between competing considerations in each case, without a clear-cut algorithm.

Figure 6.2 Geographical lots in a framework agreement for cables by a SOE



Geographical lots are often used accumulatively with fixed shares in a framework agreement. For example, a framework agreement covers demands from 5 cities A, B, C, D and E. The demands of A and B constitute 50% of the entire demands under the framework, and that of C and D makes up 30%, with E occupying 20%. The SOE may decide to award 50% (covering A and B) to the first ranking, 30% (C and D) to the second and 20% to the third (covering E).

Division into lots may encourage the participation of (potentially specialised) suppliers, thus promoting long-term competition and fostering supplying chain by reducing the risk of lock-in.[42] It is also a sensible choice if there is differentiation between each fraction, which for instance may arise in delivery

[42] A participant raised this concern. See also Z. Wu, fn. 24, *supra.* at p.43. For the impact of division into lots in procurement, see V. Grimm *et al.*, "Division into Lots and Competition in Procurement", Ch.7 in N. Dimitri, G. Piga and G. Spagnolo (eds.) *Handbook of Procurement* (2006, Cambridge University Press)

characteristics or in technical particularities.[43] However, the above benefits are hinged on the proper design of the lots, especially regarding the number/ value of lots. Unwise lots, otherwise, possibly allied to other design inappropriateness may adversely affect competition. More importantly, pre-disclosed the expected "market share" at this stage increases the demand predictability and thus can be pro-collusive, allowing the participating suppliers to coordinate and "share the pie". The risk can be particularly exacerbated in the context of closed frameworks where no new entrants are allowed.

In the context of framework agreements, lots design is interrelated and interacted closely with the number of suppliers admitted to the frameworks. Both decisions are sensitive and key aspects of procurement planning, because they can partly determine the mini-market for the subject matter of the framework agreement upon its conclusion and determine the degree of the competition of the framework.[44]

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[43] G. L. Albano, "Demand Aggregation and Collusion Prevention in Public Procurement", Part III Chapter 1 in G. M. Racca and C. R. Yukins (eds.), *Integrity and Efficiency in Sustainable Public Contracts. Balancing Corruption Concerns in Public Procurement Internationally* (Bruylant, 2014), p.161

[44] Chinese practitioners pointed out the importance of the ratio between the number of awardees and the number of purchases/lots to be allocated. See Qingfang Jia, "Framework Agreements: How to Make Breakthroughs", (2008) 9 *Petroleum and Petrochemical Material Procurement*, pp. 24-25. The decision regarding the optimal number of lots and that concerning the appropriate number of suppliers to be admitted to a framework agreement will not be elaborated here, which have been already analysed in many contributions. See Albano and Nicholas, fn. 31 *supra*. pp. 236, 266, 274-276; V. Grimm *et al*, fn. 42, *supra*.

However, there is very little data about the methodology by SOEs to determine the number of suppliers to be admitted and how they design lots under frameworks. In view of the lack of procurement planning and preparation, as mentioned earlier, it is doubtful whether SOEs have recognised the importance of the lots design and the extent to which they have correctly determined the number of suppliers admitted and the reasonable design of lots. Unfortunately, few studies are devoted to the relevant topics.

4.2 The Second stage: Call-offs

Once a framework agreement is in place, demanding units/ users within a SOE can place orders against the agreement. In the overwhelming majority of cases, SOEs order through direct awards. While it is possible to reopen a second-stage competition to determine a supplier for a purchase, it is only involved in very limited cases.[45] SOEs' preference for direct awards contrasts with the ordering practice in government procurement where a second-stage competition is encouraged to further lower prices.[46] The difference once again reflects that SOEs focus more on efficiency in using framework agreements.

[45] Four participants affirmed the use of second-stage competition in their frameworks.
[46] See Chapter V above.

A demanding unit (user), where a requirement arises, is unable to place an order on its own, but needs to submit its need to the procurement department, often through electronic means. [47] Upon receipt of the request, the procurement department selects a supplier for the given order based on the lots divided and the characteristics of the requirement. The user may express its preference, which is usually followed.

In general, the call-off stage of frameworks by SOEs tends to be a demand-submission and task-allocation process, typically when direct awards are involved. It is a straightforward, streamlined and easy-to-use process, which arguably reflects the importance that SOEs place greater importance on the objective of efficiency in framework agreements. The standardised allocation of orders may also be to meet the consistency and compatibility of equipment and devices by various users. On the other hand, the streamlined ordering process may indicate that, at least to some extent, SOEs are effective in conducting the first stage of framework agreements; otherwise the second stage would be complex and lengthy.

At both the headquarter/ central level and the sub-central/ affiliate level, it is usually the procurement department instead

[47] All participants from SOEs have confirmed this. For information about electronic/ online systems in performing framework agreements, see S. Chen, "Analysis of the Significance of Framework Agreements Tendering on Enterprises" (2014) 13 *Economic Vision,* pp.64-65 (in Chinese)

of the actual end-users who makes the call-off.[48] However, concentrating the decision power of selecting contractors and placing orders to the procurement department alone may create opportunities for rent-seeking and irregularities. It is possible that the procurement department gives priority to ordering with a favoured supplier. The risk of improper use may exacerbate when the internal control and external monitoring are inadequate or absent.

Furthermore, the end users are excluded from participating in both stages of framework agreements. It is sceptical whether the frameworks managed by the procurement department can always actually satisfy the users' needs. Unfortunately, there is no data in the public domain in the literature to discuss the issue.

The lack of transparency and oversight is a further problem present in the second stage of frameworks by SOEs. On the one hand, centralising the operation of frameworks as far as possible may facilitate oversight and management. However, as aforementioned, SOEs are not subject to regulation in their procurement of goods and services, including through framework agreements. Therefore, they are free to decide not

[48] The author has an impression that Chinese people tends to be obsessed with centralised procurement. This may be told from the design of the government procurement system, including the compulsory centralised procurement and the introduction of Bulk Centralised Procurement as mentioned in Chapter V. Moreover, in the interview, the author observed that all participants were quite positive about the trend towards centralised procurement in the procurement of SOEs.

to inform any upcoming order or not to publicise the award results. It is unknown how the allocated lots are implemented in reality. It is possible that a supplier receives additional orders in excess of its allocated share but without being checked.[49]

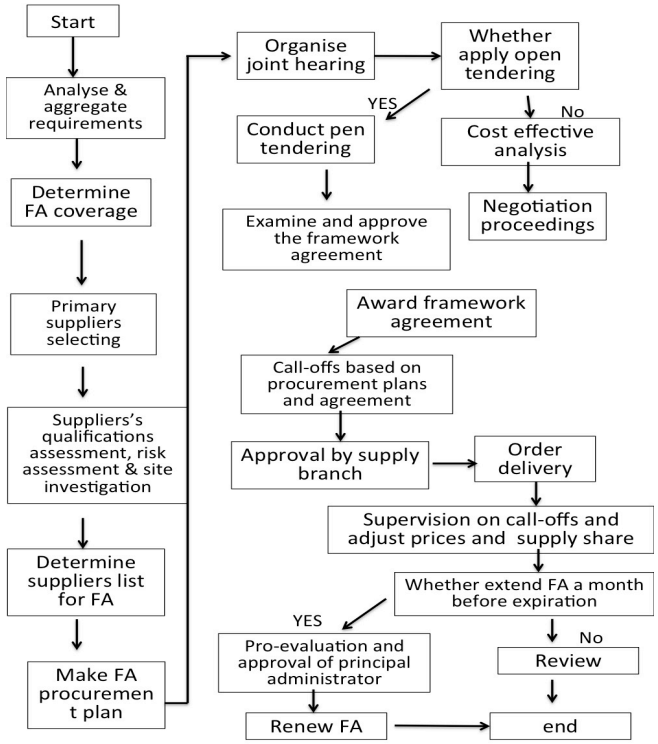
The duration of framework agreements used by Chinese SOEs is usually between one to two years. Excessively long frameworks are less concerned in the procurement of SOEs.[50] Figure 6.3 depicts the procedures of implementing framework agreements by Sinopec Group. The author has reproduced it here for clarity.

As mentioned earlier, although a second-stage competition may be involved to award call-offs under frameworks, no literature is found showing how the competition operates. As a participant said in the interview, often the second-stage competition is carried out by the procurement department through request for quotation.

[49] According to a participant working in an affiliate's procurement department of a central SOE, "In practice, we seek to satisfy requirements including preferences of demanding units as possible we can. Therefore, if they prefer a supplier which has arrived its fixed share, additional orders may be allowed, provided they will not substantially change the original contract scope and are not in breach of the laws and internal rules" (author's translation).

[50] Article 4.2 of "Sinopec Rules on Framework Agreements" even states that the duration of framework agreements cannot be less than one year. This may reflect that excessively long duration is not a problem in frameworks by Chinese SOEs. As mentioned in Chapter V, it is less a problem in Chinese government procurement either.

Figure 6.3 Use of Framework Agreements in Sinopec



Source: Sinopec, "China Petrochemical Corporation (Sinopec) Rules Administrating Framework Agreements Procurement". FA refers to framework agreements for simplicity. The figure shows that the procurement personnel should consider whether to use open tendering before concluding framework agreements or not. In practice, however, restricted procedures are more used at this stage according to the interview.

5 Supervision and Review Mechanisms

Since the procurement of SOEs lays outside of the scope of government procurement, as explained in Ch. IV, the supplier review mechanism under the *Government Procurement Law* (GPL) does not apply to framework agreements by SOEs.

Where framework agreements are used to procure works, albeit in very few cases, the review system under the *Tendering Law* (TL) may apply if tendering procedures are involved. Where

they use frameworks to procurement works based on non-tendering procedures and where they use frameworks to procure goods and services, the review system under the *TL* does not apply.

Two issues are particularly noteworthy there. Firstly, the availability of the review system under the *TL* is restricted to the tendering proceedings. It means that the first stage of framework agreements may be covered by the *TL* review system but not the second stage if frameworks are concluded through tendering procedures and are used to procure works. It follows that the second stage of framework agreements by SOEs, in any case, is excluded from applying any review system under the Chinese public procurement system.

Secondly, even if the *TL* review system applies to the first stage of a framework of works by SOEs, the effectiveness of the review system is questionable because the jurisdiction to hear and handle complaints belongs to various line ministries within their respective functions. These "supervisors" have adopted different ministerial rules on challenge proceedings.[51] The decentralised review mechanism may confuse suppliers who

[51] The division of duties among relevant departments has been provided in the "Opinions on the Division of Duties and Obligations among Relevant Organs of the State Council in Conducting Administrative Supervision upon Tendering Activities" of the State Council. For instance, Ministry of Industry and Information Technology adopted *Measures for Handling Complaints Concerning Tendering and Bidding Activities for Engineering Construction Projects* in 2004, revised in 2013. The NDRC promulgated *Interim Measures on Supervision of Major Construction Projects*, modified in 2013.

may find it difficult to identify the right authority and rules to file objections.

Beyond the public procurement regulation, SASAC and its branches, in general, do not directly supervise procurement activities of SOEs, as explained in Ch. IV.[52] After extensive searches, it is found that there are very a few local SASAC branches that set up their own challenge system that applies to the procurement of the local SOEs. For instance, the local SASAC branch in Wenzhou Municipality, Zhejiang Province issued the *Measures on Handling Complaints Arising from Procurement of Wenzhou City-owned or Handling Enterprises (Trial).*[53] The local rules are advanced in providing supplier review for the procurement of local SOEs, their coverage is rather limited and cannot develop to become a uniform review mechanism at the national level.

In reality, SOEs tend to self-regulate and self-enforce their procurement activities, including those through framework agreements. For SOEs, the focus of monitoring is more to ensure compliance of suppliers, rather than self-monitoring.

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[52] See Chapter IV above. The legal basis for SASAC and its local branches to execute supervision is the *Law of the People's Republic of China on the State-Owned Assets of Enterprises,* adopted on Oct. 28, 2008 and effectuated on May 1, 2009.

[53] *Measures on Handling Complaints Arising from Procurement of State-owned Enterprises in Wenzhou City (Trial),* effectuated on Sep. 11, 2012, Chinese text available at http://www.wzgqcgzs.cn/gzw/gqcg/gqcg_n.jsp?fid=20&tid=823 (accessed Aug 28, 2018)

Although they often have their in-house supervision and audit departments, they are less likely or willing to review or overrule their own activities or decisions which may turn out to be inappropriate. No literature is found regarding the review on procurement by the internal supervision departments of SOEs.

Notably, Ministry of Finance (MOF) in 2018 adopted the *Interim Measures on Administrating Centralised Procurement by Financial State-Owned Enterprises* No. 9 [2018] of MOF [54], in which it specifically requires financial SOEs to establish a centralised procurement management committee, one of whose main duties is to audit and review the implementation of procurement projects and other activities related to procurement. Although there is no further information about how this requirement works in fact, the Measures do reflect the MOF's recognition of the importance of having an effective review mechanism on the procurement of financial SOEs.

In general, most SOEs are observed to lack effective check-and-balance regarding their procurement.[55] The absence of an

[54] As explained in Chapter IV, financial SOEs are managed by MOF, and non-financial SOEs (most of SOEs) are supervised by SASAC and its local branches.

[55] L. Shang, "Reasons for and Solutions of Kickbacks in Procurement of SOEs" (2014) 27 *Chinese Market,* 92 (in Chinese); H. Du, "Procurement of SOEs: Problems and Solutions", (2001) 9 *China Inspection* (in Chinese). See also in China Institute of Internal Audit, "Analysis on Relationship between Three Auditing Bodies in the Supervision System of State-owned Enterprises in China" (Nov. 1 2012), available at http://www.ciia.com.cn/docs/jl1/2012-11-01/1351737225971.html (accessed July 22, 2018); X. Zhao, "Where is the Obstruction of Supervising State-owned Enterprises" (March 28 2014) *Honesty Outlook* (in Chinese)

effective supervision and review mechanism is viewed as a key factor leading to the potential improper use of framework agreements by SOEs, which may be demonstrated by the notorious corruption scandals associated with SOEs' procurement, as will be discussed in section 6.6. Given the particularity of SOEs, they are suggested to be more pro-active to subject their procurement activities to external oversight and audit to an appropriate extent.

6 Problems and Challenges in the Use of Framework Agreements by SOEs

In general, SOEs tend to use framework agreements in a more flexible manner than that in Chinese government procurement, which may reflect the different trade-offs between procurement objectives in the two areas. SOEs are not looking for integrity and attach more importance to efficiency and value for money.[56]

[56] For instance, Sinopec adopted its own "Sinopec Measures on Administrating the Procurement of Supplies and Materials", Chinese text available at https://wenku.baidu.com/view/b6d0498fac51f01dc281e53a580216fc710a535d.html?re=view
According to Article 1.3 of the "Measures", the principles of administrating tendering procedures are "(1) openness, fairness, impartiality and good faith; (2) legal compliance, process control and recording the whole process; (3) safe, timely and economic supply; (4) unified management, decentralised implementation and online operation". Integrity/ anti-corruption and accountability are not mentioned at all. In contrast, in Chinese government procurement, integrity/ anti-corruption is often considered the overarching procurement objective, as explained in Chapter V. Article 1 of the *GPL* provides that "The present law…with a view to improving the use efficiency

As market players who are exposed to the market competition, many of them may be more incentivised to make sounding procurement decisions and conduct effective procurements.

On the other hand, however, given the overall regulatory gap regarding the procurement of SOEs, there may be more problems in using framework agreements, especially in light of the huge expenditures involved. Many problems have not been criticised perhaps because they are not exposed or checked yet.

6.1 Lack of Regulatory Rules on Procurement of Chinese SOEs: A Huge Regulatory Gap

It is difficult, if not impossible, to challenge the legality of framework agreements used in the procurement of SOEs. This is because frameworks are mainly used in SOEs' procurement of supplies and services, which largely lays outside of the Chinese public procurement rules.[57] On the other hand, however, the lack of regulation on the procurement of SOEs, in general, is arguably the source of the problem.

From the literature, the procurement of SOEs was not included from the scope of Chinese public procurement

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of government procurement funds, protecting the interests of the State and the public interests, protecting the lawful rights of the parties involved and promoting the construction of a clean government."

[57] For the regulatory status of the procurement of SOEs, see Chapter IV.

regulation, at an earlier time, was intended to maintain their management autonomy, as most of them are profit-seeking companies.[58] In addition, works projects generally account for the lion share of the public procurement totality. Since the *TL* covers majority of their procurement of works, allowing SOEs to purchase goods and services without regulation at that time appeared to be acceptable. As explained in Chapter IV, SOEs often undertake procurement in a more flexible manner, even with regard to those covered by *TL*, that deviates from the current public procurement rules in many aspects. According to Wang, such deviation cannot be blamed on SOEs alone "due to the disregard of residual flexibility in formal legal rules".[59]

Despite the above, however, the regulatory gap has become one critical loophole of the Chinese procurement regulation, which needs to be addressed for several reasons. Firstly, the characteristics of SOEs arguably call for their procurement to be subject to a certain extent of regulation and oversight. SOEs are invested or controlled by the governments. At present, public funds remain the main sources of most of the SOEs. It is justifiable for the government to require SOEs to procure in a

[58] For instance, see Q. Chen, "Consumers Pay the Bill for Procurement of SOEs- Why Procurement of SOEs Is in Chaos?", Legal Daily (in Chinese, March 15, 2012), http://www.legaldaily.com.cn/index_article/content/2012-03/19/content_3438746_2.htm (accessed July 4, 2018)
[59] See Wang, Bovis and Tu, fn. 4, *supra.* at p.11

regulated and efficient manner to ensure the maintenance and appreciation of the public funds.[60] Moreover, many SOEs dominate the utilities sector and deliver public services. The considerable purchasing power of them makes their purchasing activities has impact far beyond their own business operation but to the relevant market. These facts also suggest the need to subject SOEs' procurement to proper transparency and oversight.[61] This viewpoint can be further supported by the fact that the centralised procurement by financial SOEs is now subject to the MOF regulation.

For SOEs, having procurement conducted in a regulated way can help achieve value for money. The fact that large SOEs have adopted their internal procurement rules may arguably indicate that they have recognised the value of proper regulation. Nevertheless, such self-regulation in many cases seems to be defective and poorly implemented, given the lack of internal checks and balances. Besides, the majority of their internal rules can hardly be accessible.

In the meantime, independent supervision and review mechanisms are generally absent in the procurement of SOEs either. As a result, the procurement of SOEs is almost a

[60] As explained in Chapter IV, State-owned Assets Supervision and Commission and its local branches exercise the investor's right on behalf of the Chinese governments.
[61] Wang, Bovis and Tu, fn. 4, *supra,* p.145

"blackhole", making it one of the severely hit areas of illegalities and irregularities, which can be demonstrated by the wide incidents of corruption associated with the procurement SOEs in reality.[62] In cases of framework agreements, their inherent uncertainty and flexibility may particularly lay fertile grounds for potential abuses. Therefore, SOEs arguably have incentives to regulate their procurement, including framework agreements, to achieve value for money and efficiency. Although they are not looking for integrity, combating corruption in many cases can facilitate achieving the above objectives by enhancing transparency and competition.

Thirdly, the use of tendering procedures by SOEs, when establishing framework agreements, may actually infringe the rules contained in the *TL* in some respects.[63] For instance, under the current rules on tendering, only one successful bidder is to be selected after the tendering procedure. Awarding multi-supplier framework agreements based on tendering procedures would not be permitted, at least in the procurement of works.[64] The current tendering rules in the *TL* do not allow more than one round of competition either. In addition, the requirement on

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[62] Y. Zhang, "Do not Allow Discretionary Purchases of State-owned Enterprises" (in Chinese, June 8, 2015) *Chinese Legal Daily*, http://legal.people.com.cn/n/2015/0618/c188502-27173160.html (accessed Sep 10, 2018)

[63] Q. Wang and G. Feng, "Exploring Legal Basis for Framework Agreements Through Tendering by SOEs" (2017) 8 *Theoretical Research*, 29 (in Chinese)

[64] The *IRTL,* Article 55.

the information to be included in solicitation and in the contracts would not permit the necessary flexibility in terms of quantity and price in the context of framework agreements. All these inconsistencies may jeopardise the legal certainty of the procurement rules as a whole.[65] Special rules are needed in this regard to remove the legal inconsistencies.

From the international perspective, the status quo of the procurement by Chinese SOEs has posed a salient challenge to China's negotiations on GPA accession. The exclusion of procurement of SOEs from the *Government Procurement Law*, thus excluded from China's offer, caused significant critiques from other parties.[66] Subsuming the procurement of SOEs, perhaps including that through framework agreements, into the public procurement regulation may be needed to speed up the accession process.

6.2 Inadequate Procurement Planning and Management

Procurement planning is the process to identify what is needed and to determine how the need is to be fulfilled. Accurate and proper planning allows the creation of a procurement strategy

[65] Several Chinese practitioners also raised the concerns that operating framework agreements may violate the current tendering rules. For instance, see Q. Wang and G. Feng, fn. 63 *supra*, p.29

[66] For instance, see G. Grieger, "China's WTO Accession: 15 Years on Taking, Shaking or Shaping WTO Rules?" European Parliamentary Research Service (Dec 2016); "Navigating China's Public Procurement Market: Background, Challenges and Best Practices", the US-China Business Council (Nov. 2012)

that helps SOEs to fulfil their acquisition needs timely and at a reasonable cost. While most of the potential savings in the procurement process can be achieved by improvements at the planning stage, ill-planned procurement may result in time-consuming and costly detours, and the absence of proper planning is usually the causal factor of the problems at later stages.

However, procurement planning tends to be a weakness for most Chinese SOEs, especially in the context of framework agreements that aggregate demands of multiple users over a longer period. Although a formal procurement plan is usually required by large SOEs, whether by SOEs' internal rules or by the rules adopted by several local SASAC branches or by MOF, in reality, such requirement appears to be poorly observed and the procurement personnel do not always carefully plan as required.[67]

The poor procurement planning can be attributed to multiple reasons. Firstly, there is a general lack of understanding of the importance and value of procurement planning. This is closely related to the lack of procurement capacity of SOEs. Although

[67] J. Qu, fn. 1, *supra,* pp.76-78. Regarding the formal requirement for procurement planning, for example, article 14 of the *Interim Measures on Administrating Centralised Procurement by Financial State-Owned Enterprises* explicitly provides procurement planning is a stage of the procurement cycle. The "Sinopec Rules on Framework Agreements" also contain provisions on procurement planning stage in articles 3.3-3.5.

central large SOEs often have procurement departments to execute procurement function particularly, there are a number of SOEs, especially the local ones, that still do not have functional procurement units/departments.[68] As most of them do not have qualified procurement professionals. The procurement practice is often carried out by non-qualified personnel that have no relevant knowledge and skills, in a similar vein to that in Chinese government procurement.

Given the challenge, it is not surprising that the procurement personnel pay little attention to procurement planning. Alternatively, they may find it challenging to conduct planning effectively, in the absence of detailed and proper guidance, given their general lack of procurement knowledge.[69] Moreover, most SOEs arguably lack a framework/ mechanism or detailed procedures to instruct and particularly enforce procurement planning.[70] Hence, even if the procurement departments or staff fail to make a sounding plan, inadvertently or not, they are less likely to be responsible or punished.

One negative result of poor or missing procurement planning is the inability to identify the future requirements, to determine

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[68] *Ibid.* pp.77-78

[69] J. Chen, C Gu and G. He, "The Application of Framework Agreements in Centralised Procurement of SOEs", (2015) 11 *Petroleum and Petrochemical Material Procurement*, p.15

[70] "SOEs' Procurement Management, Four Major Problems to Be Resolved" (in Chinese, Aug 24, 2015) *China Enterprise Observer*, available at http://www.ccgp.gov.cn/dfcg/llsw/201508/t20150824_5755867.htm (accessed Aug 10, 2018)

the reasonable quantities and value, to delineate the appropriate scope of framework agreements, to draft precise specification, to wisely design lots division, and to decide how the framework is to be structured. The result may be manifested in large differences between the estimate and actual quantity of demands in the use of framework agreements by SOEs.

Procurement personnel often rely on the procurement history to determine the estimated quantity of needs, regardless of the actual characteristics of the given procurement. For example, one SOE established a framework agreement for an estimated 40000 pipe fittings, whereas the actual demands turned out to be 60000 items, 50% more than the estimated quantity. These additional orders exceeded the supplier's capacity and resulted in a delay in delivery.[71]

Apart from demand analysis, thorough market research is also missing practice in framework agreements by SOEs either. For instance, concerns are raised by practitioners about that the terms established under framework agreements may fail to respond to market changes or reflect the market practice, especially when the subject matter to be procured is volatile in price, i.e. products made of metal.[72]

[71] See J. Qu, fn. 1, *supra,* pp.76-78
[72] *Ibid.* at p. 76

6.3 Insufficient Competition

Effective competition is vital to SOEs in their procurement, including through framework agreements, because it contributes immensely to the achievement of value for money, with desirable results of lower price and better quality.[73] However, the use of framework agreements by SOEs is argued to often lack effective competition and may, therefore, lead to suboptimal outcomes.

At the first stage, as explained earlier in section 4.1, Chinese SOEs tend to use restricted procedures to conclude framework agreements.[74] While it is reasonable to use less-competitive methods in some cases, in other cases, the procurement department may turn to restrictive procedures simply to avoid open tendering and thus to circumvent all the related transparency and competition requirements under the *TL*.

Moreover, in the cases of restricted procedures, there is no clear method indicated in the literature to show how SOEs select which suppliers to invite to participate in the first-stage competition. According to the practitioners, large SOEs are less proactive in exploring the supply resources themselves but often choose to "wait" for suppliers to market their products and

[73] OECD, "Competition and Procurement" (2011), p.7
[74] Negotiations operate similarly to competitive negotiations under the *Government Procurement Law*.

services, as they are usually the dominant buyers in the relevant market.[75] To avoid possible supply risks, they usually restrict the entrance to their procurement market through the demanding financial, economic and technical qualification.[76] In reality, they are more prone to work with suppliers whom they have worked with, and most of their partners are large suppliers.

By limiting access to participating suppliers, competition at the first stage would be severely restricted. Overpricing is arguably one of the most intuitive resultant problem.[77] The incumbency problem may also demonstrate the insufficient competition in framework agreements. According to the practitioners, it is all-too-common for most of the suppliers to remain unchanged under framework agreements by large SOEs.[78] Incumbency can be particularly pro-collusive since the suppliers know each other and are highly likely to collaborate and determine how to share the collusive profits.[79]

As provided in section 4.2 above, SOEs often use mandatory supplier lists as the qualification process of framework

[75] G. Chen, "Analysis on the Game of Price on Procurement by Large SOEs" (2017) 14 *Modern Business* (in Chinese)
[76] *Ibid.*
[77] Y. Zhang, "Do not Allow Discretionary Purchases of State-owned Enterprises" (June 8, 2015) *Legal Daily* (in Chinese)
[78] X. Sun, fn. 12, *supra.* at p. 122
[79] Even in open framework agreements where new jointers are allowed, "incumbency advantage", which means "the incumbent supplier's or suppliers' (potential) informational advantage", exists. The incumbency advantage may exclude new entry in some markets, acting as a partial barrier to entry, posing risks of collusion. See Albano and Nicholas, fn.31 *supra*, p.187.

agreements. Using supplier lists may help to establish the long-term relationship with trusted suppliers and ease the workload of procurement personnel in assessing qualifications. However, it will be another story if supplier lists are used to limit participation, thereby restricting the entrance to competition in framework agreements, especially when the lists are "mandatory" and when the frameworks are "closed". Their simultaneous use is argued to further entrench the barriers to enter the market, exacerbating the risks to competition than the risk that may derive from the use of any alone. Moreover, since frameworks are mainly used by SOEs for repeated purchases of common-use supplies. The likely extent of procurement demands of those supplies over a period of time may be estimated and predicated, at least for the incumbent suppliers. As Albano and Nicholas argue, the barriers to entry and the demand predictability are all pro-collusive traits in public procurement.[80] Restricting competition for entering frameworks to registered suppliers only may exacerbate the risk of collusion in framework agreements by Chinese SOEs.

Doubts are raised whether SOEs have actually considered the potentially adverse impact on the procurement and the general market before deciding to use supplier lists. Unfortunately, there is no literature devoted to the topic. It is

[80] See Albano and Nicholas, fn. 31 *supra*, chapter 8.

further unclear whether there are a set of clear and defined criteria to qualify and register suppliers. Moreover, no information is available regarding the updates of supplier lists within SOEs. It is questionable whether the supplier lists are open to new firms, and if yes how regularly they are updated.

For SOEs, they may exclude a supplier, who may best satisfy their needs and fulfil their realistic expectation only because it is not registered. In the long run, this market access restriction would increase the concentration of the relevant market, given the sheer magnitude of procurement covered by framework agreements. SOEs may run the risk of over-reliance on a few large suppliers who can discretionally manipulate the market, by which time they may find it costly to switch to other suppliers or to face supply disruption.[81]

Regarding the second stage, where orders are issued through direct awards, no further competition is involved. While a second-stage competition is reopened, no information is available regarding how it operates, which itself reflects the lack of transparency problem as discussed below.

Given the above, it is submitted that the competition in framework agreements by SOEs appears less effective, which not only jeopardises the achievement of value for money their

[81] R. M. Monczka, R. B. Handfield, L. C. Guinpero, J. L. Patterson, *Purchasing and Supply Chain Management*, (5th edn., Cengage Learning, 2011), p.221

procurement but also may impact the market beyond that. There is a need for SOEs to strengthen competition to optimise procurement results, which may start with freeing up the entrance to the SOEs' procurement market.

6.4 Lack of transparency

There is an alarming lack of transparency in the SOEs' use of framework agreements, which causes more serious problem than that in Chinese government procurement.[82] In fact, it is an issue that plagues the procurement of SOEs in general.

As mentioned above, large SOEs tend to adopt internal rules to govern their procurement, for instance, the internal rules on framework agreements adopted by Sinopec. However, these rules are to a large extent not accessible to the public, which itself reflects the transparency deficiency.[83]

In the context of framework agreements, SOEs in most cases use restricted procedures and have rarely publicly solicited tenders, perhaps to avoid the transparency required in open procedures. There is no relevant information showing how they determine to invite which suppliers to submit tenders and how they evaluate the tenders.

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[82] For lack of transparency in frameworks in Chinese government procurement, see Chapter V.
[83] See Wang, Bovis and Tu, fn. 4, *supra*. at p.21

Financial SOEs are obliged to publish notices about the contracts awarded in centralised procurement.[84] Because framework agreements *per se* are often considered contracts, their conclusion therefore should be made public for financial SOEs and the call-offs made under frameworks need not be announced. However, for non-financial SOEs, there are few notices in the public domain regarding their conclusion of framework agreements, let alone the orders issued within frameworks. It can be said that the entire procurement process of framework agreements by SOEs is a transparency "black hole", enclosed to the outside. Such gap provides greed grounds for potential abuse, which may contribute immensely to corruption and irregularities. In the absence of supplier review, as explained in section 5 above, these irregularities can happen and even become rampant but without being checked.

On the one hand, SOEs cannot be blamed alone for the "blackhole", because they are not subject to any transparency requirements under the current Chinese public procurement rules when procuring goods and services. Besides, for SOEs, especially those who are exposed to market competitions,[85]

[84] Article 28 para 3 of the *Interim Measures on Administrating Centralised Procurement by Financial State-Owned Enterprises*.

[85] On August 24, 2015, the State Council and the Central Committee of the CPC issued the "Guideline by the Central Committee of the Communist Party of China and the State Council for the Deepened Reform of State-Owned Enterprises", where SOEs are proposed to be divided into publicly-oriented SOEs and commercially-oriented SOEs. However, there are no detailed rules construing the criteria and method how such division should be made.

they may be disadvantaged for making all procurement information public for commercial confidentiality reason. Moreover, there are no uniform media to publish all procurement information of SOEs.

However, in light of the massive corruptions of SOEs as discussed soon below, there is a need to subject their procurement to appropriate transparency standards and to hold them accountable. This does not mean SOEs should comply with the same level of transparency requirements as government agencies and public institutions. As market players, they are entitled necessary flexibility in procurement activities to meet their commercial needs. For SOEs, they are not looking for integrity and value for money and efficiency are far more important objectives.

In 2015, the State Council issued "Guiding Opinion on Deepening SOEs Reform", by which SOEs are required to operate in line with the information publicity requirement and under appropriate public supervision.[86] According to this circular, a uniform information publicity mechanism regarding SOEs will be launched, where the public can access to and

[86] "Guiding Opinion on Deepening SOEs Reform of the Central Committee of the Communist Party of China and the State Council" (in Chinese, August 14, 2015), available at http://www.gov.cn/zhengce/2015-09/13/content_2930440.htm (accessed Sep 24, 2018)

monitor how the public funds are used. The procurement of SOEs is expected to be part of the reform.

6.5 Shortage of Procurement Capacity to Operate Framework Agreements

The lack of procurement expertise and professionals has also been as a challenge to SOEs. Compared with the government agencies and public institutions, SOEs may attach more attention to procurement functions, because procurement is an integral part of the business performance. The profitability and financial performance of SOEs in part depend on how the procurement personnel carry out their responsibilities effectively. Even so, the importance of procurement has not received proper understanding and recognition by many SOEs.[87]

As pinpointed earlier in section 6.1, many SOEs, especially those at sub-central level, today do not have a specialised procurement department, let alone qualified procurement workforce to carry out procurement activities. It is hard to imagine how a SOE conducts centralised procurement, including through framework agreements, in the absence of functional procurement unit.

[87] Y. Yang, "Thoughts and Suggestions to Reform Procurement Management of SOEs", 5 *Tendering & Purchasing Management* (2014), p.28 (in Chinese)

Public procurement is a complex function that requires specialised skills and knowledge. The two-stage process of frameworks is more complex to harness and calls for further expertise.[88] However, the procurement staff of SOEs are observed to lack the requisite skill and competence for procurement. Just like the procurement officials in government procurement, they also "learn" procurement by practice, instead of obtaining relevant professional qualifications.

Moreover, an important task for procurement professionals is to serve as a bridge to effectively connect and interact various departments who are involved in procurement,[89] which is especially the case in centralised procurement. However, due to the lack of procurement professionals, the relevant stakeholders, including the user departments and technical professionals may often be excluded from the procurement process, i.e. pre-award planning and post-award management.[90] Poor interaction can be manifested in the difficulty of collecting accurate and up-to-date information from users. Thus, the procurement department is unable to provide an estimated quantity of

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[88] H. Wang, "The Implementation of Framework Agreements in Petrochemical Enterprises", (2015) 5, *Refining and Chemical Industry*, p. 68 (in Chinese)

[89] K. V. Thai, "Public Procurement Re-Examined", 1 (2001) 1 *Journal of Public Procurement*, p.39

[90] S. Chen, "Analysis on the Importance of Framework Agreements to Enterprises", (2014) 7, *Economic Vision*, p. 64 (in Chinese); Q. Ma and G. Pan, "Framework Agreements and Selecting Strategic Suppliers", (2011) 7, *Petroleum and Petrochemical Material Procurement* p.89 (in Chinese)

requirements in cases of framework agreements, thus leading to the discrepancy between the estimate and actual demands.[91]

More importantly, the interference from the top leadership of SOEs is also a challenge to effective procurement.[92] It is observed that senior officials and managers can often intervene in the procurement process, leading to abuse of power and biased decisions, such as awarding a framework agreement with a favoured company, i.e. a company of the manager's relatives. In the absence of adequate oversight, the irregularities can take place but without being checked. Against this context, the procurement personnel are less able to make commercial decisions or procure effectively, if they cannot even act independently and ethically.[93]

The lack of procurement professionals may also facilitate corruptive practices and other irregularities. Given the critical role of procurement functions, it is necessary for SOEs to train procurement personnel and recruit procurement professionals. With the lack of procurement expertise becoming a common problem in China, government agencies, public institutions, SOEs and private companies may compete to absorb procurement professionals in the near future. Therefore,

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[91] See the example provided at p.306.
[92] Z. Gao and W. Ji, "Thoughts and Suggestions on Regulating the Procurement of SOEs", Chinese Public Procurement (April 1st, 2016) (in Chinese); J. Li, "SOEs March Into A New Stage of Anti-corruption", Outlook Weekly (Nov. 29, 2015) (in Chinese)
[93] Y. Yang, fn. 87, *supra.* at p. 28

immediate steps should be made. In that case, SOEs may have an advantage over the government in recruiting expertise as they can offer more attractive salary. On the contrary, the procurement expertise may find it less attractive in becoming part of the government procurement workforce as they have no career ladder there and are afforded lower payment.

6.6 Corruption and Irregularities in the Procurement of SOEs- Beyond Framework Agreements

Corruption has been endemic in Chinese SOEs. Between 2014 to 2015, more than 115 senior executives from large SOEs, such as China South Airlines, Sinopec and PetroChina, were reported to have involved in corruption allegation. The procurement of SOEs as a whole is particularly vulnerable to illegalities including bribery, corruption and misappropriation, given the sheer magnitude of expenditures at stake. The risk of corruption can be particularly exacerbated in SOEs' procurement of goods and services as it is excluded from the application of the current public procurement rules and thus exempted from any external supervision and enforcement.[94]

[94] L. Zhang, "Anti-corruption in SOEs: Many Cases Indicate that Corruptions Mainly Emerge in Lucrative Areas", China Discipline Inspection News (May 16, 2015); J. Kang and J. Xu, "Further Preventing Corruption in Major Areas and Key Segments of SOEs" China Discipline Inspection News (in Chinese, July 18, 2015),

Extensive corruption scandals have been reported in the utilities sectors, such as energy, telecommunications and transportation industries where SOEs remain monopolistic and dominant position.[95] Corruptive practices may emerge in the circumstances where private companies bribe the procurement personnel or other senior officials of SOEs, in order to receive lucrative supply contracts.

It is argued that the improper allocation of resources and discretionary powers is one key element conducive to corruption in the procurement of SOEs. In practice, the decision-making power on procurement is concentrated in a limited number of hands, for instance, the procurement departments and other senior management and there are general lack of checks and balances. Without adequate monitoring and oversight, the relevant personnel are highly likely being tempted to abuse power and involve in illegalities to gain personal benefits or to benefit others.[96]

In the context of framework agreements, due to the particularity of the structure, they may provide greedy ground for irregularities. For example, the procurement personnel may manipulate the first-stage competition to ensure a favoured

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http://www.ccdi.gov.cn/lswh/lilun/201407/t20140704_119437.html (accessed Aug 28, 2018)

[95] *Ibid.*

[96] See J. Li, fn. 92 *supra*.

supplier to be admitted to the agreement, for instance, through disclosing bid information, drafting the technical specifications, and selectively inviting certain suppliers to bid. At the second stage, it is easy for the procurement department to award orders to a specific supplier, more than its allocated lot, for kickbacks and other advantages. The dearth of procurement professionals further heightens the risk to ethical conducts.[97]

Most of the irregularities in procurement could be deterred and detected if SOEs have effective internal monitoring and/or are subject to external oversight.[98] It is reiterated that SOEs when procuring goods and services are not subject to any transparency requirements. Most of their internal procurement rules and other procurement information are not even accessible to the public. All these transparency "black holes" can increase the risk of corruption which may take place but "unnoticed, and thus unchecked".[99] Even if some SOEs

[97] Practitioners have raised concerns regarding the lack of regulatory mechanism in the use of framework agreements by SOEs. For example, see X. Liu, "Exploration of Tendering Management Practices of SOEs" (2014) *China Purchasing Development Report*; L. Shang, "Reasons for and Solutions of Kickbacks in Procurement of SOEs" (2014) 27 *Chinese Market*; Y. Yang, fn. 84, *supra.* pp. 27-30; H. Zhang, "Bribe-taking Was Worth 300 Million Chinese Yuan: How Much SOEs Have Lost", (October 26, 2016) Xinhua News (in Chinese)

[98] External supervision is a critical source to detect and remedy irregularities of SOEs. See OECD, "Combatting Corruption and Promoting Business Integrity in State-owned Enterprises: Issues and Trends in National Practices" (June 2016, Mexico), at p.10. OECD talks about corruption of SOEs as a whole, not specifically about their procurement.

[99] *Ibid*. Weak disclosure is a common factor that encourages corruption in SOEs. OECD, "Policy Brief: China's Governance in Transition", (in Chinese, Sept. 2005) p.331,

voluntarily choose to publish procurement information, the information to be published has usually been selective, bringing doubts to the credibility and timeliness of the disclosure.[100] For instance, Sinopec was reported to have modified its internal rules governing framework agreements, whereas the new rules are not available after three years of the modification.[101]

For SOEs, corruption in procurement means the expenditures being wasted and the profits that should have generated, including profits, being lost. Unfortunately, there is no empirical data about the amount drained through corruption in this area. More importantly, SOEs are closely related to Chinese governments and public funds remain their primary source. When the procurement of SOEs is corrupted by personal interests, it means a significant loss of public funds and the public's trust in the governments would be impaired.

The cost of corruption in the procurement of SOEs is not only measured by the amount of loss. Corruption can distort competition, the impact of which goes to the general market, beyond the mere purchases of SOEs *per se*, given the

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http://www.oecd.org/LongAbstract/0,2546,en_2649_201185_35312076_1_1_1_1,00.html (accessed Aug 23, 2018)

[100] Q. Chen and Q. Wen, "Costly Procurement of SOEs Leads to the Loss of State Assets: Purchasing iTouch under the Name of USB Drive" *Yancheng Evening News* (in Chinese, March 18, 2012), http://finance.sina.com.cn/china/20120318/155411616842.shtml (accessed Aug 23, 2018)

[101] The rules were modified in 2015, but until now the new rules are not disclosed yet.

considerable purchasing power of SOEs. Moreover, SOEs produce goods and many of them are in the utilities sector providing public services. Corruptive procurement may affect the quality or even the safety of their products and services.

On account of the above, it is argued that SOEs should have the responsibility to ensure certain extent of integrity and accountability in conducting procurements, including through framework agreements. They are suggested to conduct procurement following arguably certain transparency requirements and subject to appropriate external oversight. Thus, the governments and public may act as "watchdogs" against any potential corruption and irregularities. In fact, some local SASACs such as Wenzhou and Ningbo municipalities, do have issued rules to supervise procurement of the local SOEs.

On the other hand, it is equally important to consider the particularity of SOEs as market players, who may need greater flexibility to meet commercial needs. Therefore, a balance should be properly struck between the need for transparency to combat corruption and the need for flexibility.

7 Summary

This chapter has explored the current use of framework agreements by Chinese SOEs. It is observed that SOEs often

use frameworks to fulfil repetitive requirements of common-use supplies and to secure supply of “bottleneck” items. Because the procurement of goods and services by SOEs is excluded from the current Chinese public procurement regulation, framework agreements, in most cases, are not subject to any regulation and oversight at present. In practice, large SOEs tend to conduct framework agreements in accordance with their internal procurement rules, which however are hardly accessible to the public. The transparency and supervision blackholes provide great opportunities for the improper use of such procurement arrangement.

In terms of operation, SOEs favour restricted procedures to conclude frameworks and rely more on order allocation to issue orders. Compared with that in government procurement, frameworks are used in a more flexible and less competitive way, which makes sense because SOEs are not looking for integrity but value for money and efficiency. However, poor procurement planning and management, inadequate competition and lack of transparency have become problems that may detract the achievement of the expected benefits of frameworks. The acute shortage of procurement professionals and the heightened risks of corruption have become challenges that plague the procurement of SOEs in general.

In view of the special characteristics of SOEs and the prevalent use of framework agreements in practice, it is suggested to require SOEs to conduct frameworks (as well as other procurement) in a regulated way and subject to appropriate supervision to ensure they procure effectively.

Chapter VII. Proposals for Regulating Framework Agreements in Chinese Public Procurement

1 Introduction

As explored in the previous chapters, framework agreements have been prevalently used by government agencies, public institutions as well as SOEs in China. However, the regulation has fallen far behind the practice. Until today, framework agreements are not mentioned or regulated in any national laws or State Council regulations on public procurement at the national level.

In Chinese government procurement, in the absence of an adequate legal basis, the present practice of framework agreements and the numerous rules related to frameworks adopted by central ministries and local governments may be *ultra vires*. As for the case of Chinese SOEs, their use of framework agreements, at least in procuring goods and services, is outside the coverages of both the *Tendering Law* (TL) and *Government Procurement Law* (GPL). In fact, large SOEs tend to operate frameworks following their internal procurement rules, which, however, are barely accessible to the public.[1]

[1] The legality of framework agreements in Chinese government procurement has been discussed in Chapter V section 6.1. The regulatory gap of framework agreements by SOEs has been explored in Chapter VI.

Due to the lack of adequate regulation and proper guidance, framework agreements are highly likely to be improperly used, leading to various problems, which have undermined the expected benefits of frameworks and caused a significant amount of public criticism. Over-pricing, procurement frauds and corruptions are manifestations of the inappropriate use. The lack of transparency and competition, as well as the absence of monitoring and enforcement, further create temptations for abuses of frameworks. In light of the prevalent use in practice, the regulatory gap regarding framework agreements arguably further jeopardises the integrity, coherence and effectiveness of the current public procurement legal framework.

There is, therefore, a need to provide a dedicated regulatory regime for framework agreements to fill in the gap. Formal legal rules devoted to frameworks are considered necessary (i) to provide proper legal basis for framework agreements, authorising their use; (ii) to remove the inconsistencies of operating framework agreements with the current public procurement rules, thus ensuring them being used in conformity with the overall rules; and (iii) provide necessary procedural safeguards to ensure their appropriate use and prevent the inappropriate use.

Such need is particularly urgent in the Chinese text. This is due to, first and foremost, the daunting task of combating

corruption. It is reiterated that Chinese public procurement regulation has been grounded on combating corruption, which remains the top priority among the procurement objectives.[2] The inherent flexibility and uncertainty of framework agreements may create opportunities for irregularities. The use of framework agreements by Chinese SOEs is more prone to corruption due to the vast amount of money involved and notably the absence of formal regulation. Therefore, clear and detailed rules are required to guide and supervise the use of framework agreements with a view to deterring and detecting corruptive practices. This is also in line with the high-profile anti-graft campaign launched by the current Chinese leadership.[3]

Furthermore, having framework agreements conducted in a regulated and transparent way can help to achieve better value for money, especially in the light of the general dearth of procurement professionals in China.[4] The numerous piecemeal

[2] P. Wang, C. Bovis and X. Tu, "A Comparative Analysis of Utilities Procurement in EU and China", component 5 of *A Report Prepared for EU-China Trade Project* (II) (August 2013); D. J. Mitterhoff, "The Four into One Platform: New Reform Initiatives Compound China's Dissected Public Procurement Governance", (May 1, 2012) *U of Maryland Legal Studies Research Paper* No. 2012-43

[3] Jinping Xi, Chinese President and General Secretary of the Communist Party in 2012 launched a high-profile cross-country campaign targeting at the Communist Party, government, military and SOEs officials suspected of corruption, http://www.scmp.com/topics/xi-jinpings-anti-graft-campaign (accessed Sep 12, 2018)

[4] In Chapter V section 6, it is explained that value for money is not explicitly provided among the procurement objectives under the *Government Procurement Law*. On the other hand, however, the Chinese government also

regulations on framework agreements in Chinese government procurement, despite their questionable legality, soundness and effectiveness, may nonetheless demonstrate that the importance and value of appropriate regulation in achieving value for money have been recognised.

In view of the above needs and incentives, providing formal legal rules to govern framework agreements in China is arguably the correct way forward. This chapter intends to provide a set of proposals that reform the Chinese public procurement system so as to accommodate for a proper use of framework agreements in an effective and acceptable manner. To that end, section 2 discusses the possibilities of improving the legal and institutional frameworks for the consolidation of the proposed rules on framework agreements. Section 3 then suggests the main contents of the proposed regulatory rules and section 4 concludes.

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fine-tunes the objectives and has started to attach importance to achieving value for money. For instance, Ministry of Finance in2013 in the national Online Conference on Government Procurement Work Network firstly stated that "…the priority objective should shift from anti-corruption and expenditure saving to value for money…". See http://gks.mof.gov.cn/zhengfuxinxi/gongzuodongtai/201311/t20131128_1017919.html.

2 Proposal of the Legal and Institutional Framework for Regulating Framework Agreements in China

To establish the appropriate legal and institutional frameworks is of paramount importance to ensure effective implementation and oversight of the proposed rules on framework agreements. They are the cornerstone of the formal rules and thus should be considered first.

According to the *Legislation Law* of China, Chinese legislation comprises: at the first level, national laws promulgated by the National People's Congress or its standing committee; at the second level, administrative regulations enacted by the State Council; at the third level, local decrees issued by Provincial People's Congress; and at the fourth level, ministerial rules adopted by central ministries and local rules issued by local governments.[5]

It should be noted that ministerial rules and local rules are in the same legal standing and have the equal legal force.[6] Where the provisions under the ministerial rules and local rules are inconsistent on the same subject matter, the ministerial rules will not automatically prevail, and the conflict will be

[5] *The Legislation Law of the People's Republic of China*, enacted on March 15, 2000 and effectuated on July 1st, 2000, as amended on March 15, 2015, Articles 87, 88 and 89, available at http://www.npc.gov.cn/pc/12_5/2016-01/27/content_2006351.htm (accessed Sep 25, 2018)
[6] *The Legislation Law*, art. 91

adjudicated by the State Council.[7] However, the question herein is who should submit the request for such review procedures before the State Council and in what manner, which remains unclarified as the *Legislation Law* is silent on this. The lack of clear review procedures may be part of the reason for many potential conflicts between ministerial rules and local rules that remain unsolved.

As explained in the previous chapters, at present, framework agreements in Chinese government procurement are only regulated by various ministerial rules and local rules at the fourth level of legislation inconsistently, whose legality remains uncertain. In the procurement of SOEs, framework agreements almost fall in the "lawless area", as the procurement of goods and services by SOEs, where frameworks are mainly employed, lays outside of the Chinese public procurement regulation. The internal rules adopted by SOEs are not a formal legal source although they may have a significant impact in reality.

Regarding the institutional framework, as explained in Chapter IV, many government ministries and agencies are involved in regulating Chinese public procurement. Their interests will be inherited in the proposed regulation on framework agreements. In Chinese government procurement, the main "players" are Ministry of Finance (MOF) and its local

[7] *Ibid.* art. 95

branches (supervisor of government procurement) and centralised purchasing agencies (CPAs, implementer of framework agreements) at various levels.

The government ministries and agencies that have interest in regulating the procurement by SOEs mainly include: the National Development and Reform Commission (NDRC, supervising procurement of large infrastructures by SOEs), State-assets Supervision and Administration Commission (SASAC, overseeing state assets management of non-financial SOEs), MOF (supervising management of financial SOEs), Ministry of Commerce (administrating the import of mechanical and electronic products by SOEs), and other relevant ministries in their jurisdictions, such as Ministry of Housing and Urban-Rural Development (supervising procurement of general construction), Ministry of Industry and Information Technology (administrating procurement of construction works in the communication sector), Ministry of Transportation (supervising works in the transportation sector), etc. Notably, the interest of most of these ministries is restricted to works projects involving tendering procedures. It means that they may have little say in framework agreements, at least when they are used in purchases of goods and services by SOEs.

It is suggested that a few balances should be carefully and appropriately struck in designing the regulatory framework for

framework agreements in Chinese public procurement. They mainly include: (i) the balance between the attempt for an integrated framework for all framework agreements and the difficulty (if not inability) to achieve caused by the institutional fragmentation and complexity in reality; and (ii) the balance between the desire for a radical settlement of regulatory boundaries to achieve the best interest of the country in the long run and the need to consider the interests of various stakeholders, which may mean compromises[8]; and (iii) the balance between the need of SOEs for greater flexibility and the need for necessary transparency and oversight in their use of framework agreements.

2.1 An Integrated Approach

It would be an ideal if an integrated approach to regulating all framework agreements in China, no matter who uses them can be adopted. Such integration can only be achieved through merging the *TL* and *GPL* into a full-feathered public procurement law. In that case, the use of framework agreements by government agencies, public institutions and social organisations as well as by SOEs would comply with a uniform set of rules and are subject to consistent management and

[8] Wang, Bovis and Tu, fn. 2 *supra*, pp. 147-148; See D. J. Mitterhoff, fn. 2 *supra*, p.43

supervision, regardless of the nature of the users and whether tendering procedures are involved or not.

An integrated legal framework requires a harmonised institutional framework. A supra-ministerial institution, such as a newly established Public Procurement Commission under the State Council, will be necessary. The Public Procurement Commission is envisaged to be the supreme supervisory authority as well as the policy-maker on public procurement in China, including through framework agreements. The integration approach can put an end to the long-time "territory battle" between the MOF and NDRC, the "guardian" of the *GPL* and *TL* respectively, for the leading position in the public procurement area.[9]

There is also a need to set up a uniform system that manages the implementing agencies or bodies to ensure consistent operation of framework agreements, recalling the fact that framework agreements are mainly used in centralised procurement. Currently, two main categories of implementing bodies exist: the CPAs and public resources trading centres at various levels. CPAs are tasked with undertaking centralised

[9] It is argued that an integrated public procurement framework can harmonise not only framework agreements but also more procurement methods and arrangements, including Public-Private-Partnerships (PPP) in China. At present, the MOF and NDRC are also in competition for regulating PPP. Apart from adopting different rules, they compete in establishing their own PPP research centres, see https://wallstreetcn.com/articles/258782 (accessed Aug 18, 2018)

purchases in government procurement, and one of their essential functions is to carry out framework agreements.

The public resources trading platforms are set up at various levels intending to remedy the fragmented procurement regime by centrally administrating tendering in construction, government procurement, and transfer of land-use rights and mining rights.[10] SOEs are also required to conduct most of their works projects through these platforms. [11] Despite the ambitious commitment, the results have so far been less fruitful after several years of efforts. Indeed, in some localities, i.e. in Hangzhou municipality[12], the local CPAs have been merged into the new public resources trading centres, which, however, may arguably violate the *GPL* because CPAs shall be independent legal entities.[13] In other cases, the local CPAs and the trading centres co-exist, i.e. those at the provincial level in Guangdong province.[14]

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[10] For more information about public resources trading centres reform, see Chapter IV.

[11] For instance, Ministry of Transportation and Ministry of Water Resources have issued guidelines requiring transportation and water construction projects to be procured through the relevant trading centres/platform. See Ministry of Water Resources, "Guiding Opinion on Conducting Water Construction Projects in Public Resources Trading Centres", (4 May 2012) , Chinese text available at http://www.mwr.gov.cn/ztpd/2009ztbd/slgcjslytcwtzxzlgz/gzdt/201205/t20120504_320718.html

[12] See http://www.hzctc.cn/NewsShow/Home?id=6197&ModuleID=8&AreadID=72 (accessed Aug 26, 2018)

[13] *The IRGPL*, Art. 17

[14] See http://www.360doc.com/content/17/0717/21/45199333_672164653.shtml (in Chinese, accessed Oct 1, 2018)

Should the integrated approach be adopted, the CPAs and public resources trading centres are envisaged to be harmonised into a uniform system of centralised purchasing bodies, who are expected to carry out framework agreements at the central and local levels.

A further advantage of such an integrated approach is to facilitate construction of a nationwide integrated electronic platform for public procurement. Framework agreements are increasingly "electronicised" and becoming an essential function of the existing e-procurement platforms established by both government agencies and SOEs.[15]

The co-existence of the *GPL* and *TL* (derived from the tension between the MOF and NDRC) have led to multi-fold electronic public procurement systems/platforms. They mainly include: (i) the electronic government procurement platforms (E-GPs) at various levels (supervised by MOF and its local branches); and (ii) the Electronic Tendering and Bidding Platform (the national information hub of tendering, supervised by NDRC); and (iii) public resources trading platforms (operated by public resources trading centres).[16] Apart from the above

[15] Many existing E-GPs in China also enable procurement of the off-the-shelf goods through Electronic Marketplace. It is argued above in Chapter V that Electronic Marketplace originates from the idea of framework agreements and may be considered as an advanced version of framework agreements.
[16] In most localities, i.e. Zhejiang and Anhui provinces, the local E-GP and public resources trading platforms co-exist. The Zhejiang Provincial Public Resources Trading Platform and the Provincial E-GP are available at

government-led e-platforms, a number of SOEs, typically the centre SOEs, such as the State Grid Corp of China and Sinopec, have started to establish their electronic procurement platforms.[17] The existence of various e-platforms managed by different agencies and SOEs not only means redundant construction and waste of resources but also artificially creates barriers for information sharing and data collection and leads to different operational rules, resulting in unnecessary extras for suppliers to participate. Thus, regulating framework agreements may help to establish a nationwide integrated electronic procurement platform, or at least to standardise the procurement language, enhance data-sharing and improve the interoperability of the existing systems.

Furthermore, the integration approach may bring in the benefit of aligning Chinese public procurement framework to the Plurilateral Agreement on Government Procurement of the WTO (GPA). This is because the dual-track legal framework for public procurement and the resultant left-out of the procurement of

http://www.zjpubservice.com/ and http://www.zjzfcg.gov.cn/. The corresponding platforms in Anhui are available at http://www.hfggzy.com/hfzbtb/ztbzx/default.aspx and http://www.ahzfcg.gov.cn/indexController/indexMain (accessed Sep 24, 2018)

[17] Respectively available at http://ecp.sgcc.com.cn/ and http://ec.ceec.net.cn (accessed Aug 24, 2018)

SOEs from the offer is considered a key obstacle to China's accession to the GPA.[18]

Despite the above advantages, however, such an integrated approach is less practical and may be hardly to achieve in the foreseeable future, as the author considers. The root cause is the "turf battle" between different ministries empowered to regulate public procurement can hardly be settled in the short and medium term. Such conundrum can be demonstrated by a series of unsuccessful attempts made so far to integrate the segmented regime, such as the recent reform of public resources trading platforms.[19] These attempts indicate that no central ministry, either the MOF or NDRC, is capable of dissolving the conflict on its own. There is less chance for the integrated approach to be adopted unless a harmonised institutional framework is established.

Nevertheless, the recent normative reform of market competition may bring a glimmer of hope to this approach.

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[18] See Wang, Bovis and Tu, fn.2 *supra*, pp.147-148. President Xi Jinping stated that China would seek faster progress toward joining the GPA at Bo'ao Forum on 10th April 2018, http://www.chinadaily.com.cn/a/201804/10/WS5acc15a6a3105cdcf6517259_2.html (accessed Oct 1, 2018)

[19] The historical evolvement of Chinese public procurement regime is discussed in Chapter IV. For more information about the historical attempts of unifying Chinese public procurement regulatory regimes, see P. Wang, "China's Evolving Legal Framework on Public Procurement" 6 *P.P.L.R*. (2004) p.285

China in March 2018 launched a massive institutional reshuffle reform, and it has been implemented swiftly.[20]

As part of the administrative overhaul, a new State Administration for Market Regulation was set up, tasked with uniformly regulating competition and supervising the market. This has been achieved by absorbing the functions related to market supervision that was entrusted to several ministries and agencies, including the supervision function of the previous State Administration for Industry and Commerce, the NDRC's power in the anti-trust law enforcement against price-fixing and the Ministry of Commerce's power in the anti-trust law enforcement against the concentration of business operators.[21] The reshuffle ended the previously fractured regulatory system on market competition, and the NDRC and Ministry of Commerce will no longer have interests and excuses to interfere with competition regulation. Now that the integration can be achieved in the competition area, presumably, it may be possible in the Chinese public procurement area.

[20] "Notice of the State Council on the Setup of Institutions", No. 6 [2018] of the State Council, Chinese text available at http://samr.saic.gov.cn/jg/ (accessed Sep 28, 2018)

[21] Apart from the NDRC and Ministry of Commerce, functions of the previous Standardisation Administration and Certification and Accreditation Administration, the Food and Drug Administration, the Executive Office of the State Council Anti-Monopoly Commission are all incorporated into the new Administration for Market Regulation.

2.2 A Hybrid Approach

The second option for China to regulate framework agreements can be a hybrid approach, by which framework agreements in government procurement and procurement by SOEs will be governed under separate rules, following the EU's approach (namely having the public sector rules combined with the utility rules).[22] Such a hybrid is considered a more pragmatic and acceptable form of regulation in China because, firstly, it is in line with the existing two-dimensional public procurement regime. Secondly, it can take account of the vested interests of different government ministries and agencies involved, which means less resistance and pushback. Thirdly, it allows for the consideration of the particularity of SOEs, and it is able to grant additional flexibilities to SOEs in using framework agreements to meet their commercial needs.

On account of the above, such a hybrid approach to regulating framework agreements in China is suggested to be a more practical move. The legal and institutional frameworks in government procurement and the procurement of SOEs under this approach will be discussed in turn below.

[22] See Chapter III section 2.

2.2.1 Legal and institutional frameworks for the regulation on framework agreements in Chinese government procurement

This section will propose a set of options for improving the existing legal and institutional frameworks for public procurement so as to accommodate the regulation of framework agreements. Through the discussion of their respective advantages and disadvantages, the most acceptable and viable option will be identified.

2.2.1.1 The modified *Government Procurement Law* and/or the modified *Implementing Regulations of Government Procurement Law*

It would be an ideal way forward to have the *GPL*, after necessary amendment, to include the legal rules on framework agreements. In that case, the amendment should include two broad aspects: (i) incorporating the new provisions on framework agreements into the *GPL*; and (2) revising the existing rules to accommodate framework agreements, i.e. the requirements on solicitation and contract notices publication, contract awards, and rules on supplier review.

Having the *GPL* as the forum for the rules can statutorily authorise the use of framework agreements and resolve the legality issue once for all, because the *GPL* is the legal base for

all the rules on government procurement. Moreover, the modified *GPL* being the forum can secure consistent implementation and enforcement of the rules at all levels. The legal certainty can be assured at least so far as framework agreements by government agencies and public institutions is concerned.

MOF, the supreme regulator of government procurement, in March 2018 expressed an intention to modify the *GPL.*[23] It would be desirable to bring regulating framework agreements into the scope of the potential changes to the law, i.e. as an explicitly regulated procurement method/procedure. However, the proposal does not provide any details regarding the modification scope and cannot be found in the MOF official agenda. It is believed that it will take a long time before the proposal can be crystallised, and whether or not framework agreements will be considered in the proposal is still doubtful.

On the other hand, modifying the *GPL* to accommodate to framework agreements is arguably a less optimistic option, the main obstacle to which may be the reluctance of MOF. As analysed in Chapters IV and V, MOF may choose not to regulate

[23] "Legislative Plan of Ministry of Finance in 2018", MOF (March 20, 2018). It was reported that Ministry of Finance held a symposium on revising *Government Procurement Law* on July 19, 2018, where around ten topics were discussed regarding government procurement, tendering, entering into GPA and etc. However, the details and contents are not available to the public, Chinese text available at http://jjs.mof.gov.cn/mofhome/mof/xinwenlianbo/neimenggucaizhengxinxilianbo/201807/t20180727_2973968.htm (accessed Sep 24, 2018)

framework agreements to avoid the much-maligned public criticism on the improper use of frameworks. This view can be supported by the successive removal of the provisions that mentioned framework agreements from the draft *IRGPL* and the amended *Measures for the Administration of Government Procurement Through Non-Tendering Methods*. [24] As the "ostrich syndrome" sustains, it is less likely that MOF would change its tune abruptly and determine to resolve the challenges regarding framework agreements under the *GPL*.

It is also advisable to modify the *Implementing Rules of the Government Procurement Law* (IRGPL), on its own or following the amendment of the *GPL* as suggested above to include rules regulating framework agreements. As the only State Council regulation implementing the *GPL*, the *IRGPL* is capable of integrating the existing ministerial rules and local rules on government procurement. Therefore, the modified *IRGPL* being the forum can have similar advantages to the modified *GPL*.

However, the possibility of accepting this option is shimmer, recalling the removal of drafting provisions related to the framework agreement from the previous draft *IRGPL*. The fact that MOF decided to authorise another popular procurement

[24] *Measures for the Administration of Government Procurement Through Non-Tendering Methods*, No.74 [2013] of MOF, adopted on Oct 28, 2013, and entered into force on Feb 1, 2014. Hereinafter referred to as the *Non-Tendering Measures by MOF*.

method-competitive dialogue- through a separate ministerial rule rather than the modified *IRGPL* may also indicate the slim possibility. Furthermore, MOF may not plan to amend the *IRGPL* immediately, considering that it was enacted after a five-year pending period.

2.2.1.2 A new ministerial rule on framework agreements enacted by Ministry of Finance

The most practical option proposed would be for the MOF to issue an *ad hoc* ministerial rule for framework agreements in Chinese government procurement. In view of the prevalent use of framework agreements, it would be more desirable if the *GPL* or the *IRGPL* can provide a legal basis for framework agreements, for instance by briefly referring to them. The main advantages of such option are as follows:

First, the MOF has the authority and capacity to adopt a ministerial rule designated to regulating framework agreements. According to the *GPL*, the MOF has the exclusive authority to authorise new procurement methods in addition to the five statutory ones.[25] MOF has issued the *Interim Measures on Administrating Competitive Dialogue in Government*

[25] Article 26 of the *GPL*.

Procurement to govern competitive dialogue, setting a typical and recent precedent for this option.[26]

Secondly, in reality, the local finance departments have adopted numerous local rules related to framework agreements, despite their questionable legality, and thus have accumulated years of experiences and skills in supervising this mechanism.[27]

Thirdly, ministerial rules enable relatively easy and fast amendments while relevant experience is gained through practice, without the need for approval from the National People's Congress and its Standing Committee and State Council, which is required for the amendments of national laws and State Council regulations.[28]

On the other hand, however, the fatal disadvantage of the ministerial rules as the forum for regulating framework agreements is that they are unable to coordinate relevant local rules. As explained earlier, ministerial rules are at the same legal level as local rules, and if there is a conflict between the rules, they will not prevail over the latter automatically. Given the lack of a review mechanism to solve the conflict, a government agency may choose not to apply the ministerial rules but the

[26] *Interim Measures on Administrating Competitive Dialogue in Government Procurement*, No. 214 [2014] of MOF.
[27] See above in Chapter IV for the status quo of regulating framework agreements.
[28] *The Legislation Law*, articles 2, 7 and 68.

local rules. In this case, framework agreements may operate and manage inconsistently in different areas.

Moreover, as suggested earlier, MOF's "ostrich syndrome" on framework agreements tends to impede regulating and developing framework agreements through formal rules.[29] Evasion does not address problems permanently, and thus MOF should face and accept the issues, devoting efforts resolve them.

Apart from the *ad hoc* rules, another option might be to regulate framework agreements as a non-tendering procurement method and to consolidate the proposed rules as part of the *Non-Tendering Measures* after necessary amendment. However, the regulation of competitive dialogue through a separate ministerial rule seemingly offers a counterexample for this option, which implies a higher possibility for the MOF to adopt *ad hoc* rules governing new procurement methods.

2.2.1.3 Soft Law/ Guidance issued by Ministry of Finance

It may be another option for MOF to use soft law as the forum and issue guidelines, such as a manual, on framework agreements. The guideline would suggest centralised purchasing agencies and individual procuring entities on what to and not to do in using this arrangement. As a soft law

[29] See Ch. V section 6.1 above.

instrument, the guideline possesses no legal force and has no enforcement mechanisms. Given its non-binding nature, it has the advantage of being adopted and modified more easily and quickly whenever needed, thus allowing the rules to respond to a fast-changing procurement environment.

The guideline may have power and be widely followed in by Chinese governments at all levels. As mentioned earlier, framework agreements have been widely used in Chinese government procurement, while the *modus operandi* among different areas varies to some extent, especially regarding the second stage. A guideline created by MOF (the supreme supervisor and policy-maker on government procurement) can be useful in establishing a standard of operating frameworks and inducing compliance with the standard. Druzin pointed out that codifying existing practices is enough to trigger large-scale compliance.[30] In fact, the circulars and policies issued by MOF are not formally recognised a source of law but are well respected in general. As long as the soft law is clearly and carefully drafted, it may be perceived and implemented as a de facto "hard law".

However, the soft law has no legal force and is particularly lacking in a concrete enforcement mechanism. Therefore, there

[30] B. H. Druzin, "Why Does Soft Law Have Any Power Anyway", (2017) 7 *Asian Journal of International Law*, p. 367

is always a risk of non-compliance with the "law", which nevertheless could not be reviewed or enforced. This may directly jeopardise the meaning and effectiveness of the rules. Soft law may be understood as *no law* in fact. Apart from that, soft law cannot resolve the potential violations of the current government procurement rules that may be caused by operating framework agreements, as discussed in Chapter V.

2.2.1.4 Improving the institutional framework for regulating framework agreements in Chinese government procurement

In Chinese government procurement, the institutional framework already exists, as explained in Chapter IV section 2. There is no doubt that MOF is and will continue to be the supreme legislator, supervisor and policy maker of the framework agreements, whether the forum is the modified *GPL*, *IRGPL* or the *ad hoc* MOF ministerial rules.[31]

In light of the inconsistent organisation and management of framework agreements in practice, as discussed in Chapter V, two issues need to be addressed to improve the institutional framework. Firstly, it is suggested that the finance departments

[31] Although where the modified *GPL* or *IRGPL* were selected to regulate framework agreements, the promulgator would be the National People's Congress or its standing committee and the State Council respectively, the actual drafting task will reside with the MOF as it has expertise and experience in the respect.

strictly abide by the separation of roles between the supervisor and purchaser under Article 6 of the *GPL*. For instance, local finance branches should be mandated not to over-reach, directly or indirectly interfering with the operation of framework agreements, i.e. determining their coverage, which is the *ex officio* function of CPAs.[32] Only when the duties of CPAs are clarified and guaranteed, can they be fully committed to achieving the best results through improving procurement knowledge and skills.

Secondly, efforts should be made to rationalise the administration of all CPAs to ensure consistent implementation of the proposed regulatory rules. As analysed in Chapters V section 6.2, CPAs in different areas are currently subordinate to different leading government agencies. In the absence of a unified administration system, such decentralised management may artificially segment the procurement market, undermine the unification of the procurement process and create complications for suppliers who wish to participate in the procurement markets in different areas.

In view of the above, it is suggested to establish an integrated system for administrating all CPAs to ensure they operate and manage framework agreements in a consistent manner. The Centralised Government Procurement Centre

[32] The *GPL*, art. 60

(CGPC, the central purchasing agency at the central level) is advised to be in the leading position, at the central level, to coordinate the other existing CPAs. At the local level, provincial CPAs undertake centralised procurement, including through framework agreements, under the supervision and guidance of the CGPC. All CPAs should follow uniform procurement process and standards to ensure consistency. A centralised management system helps to consolidate CPAs' status as independent public bodies and to guard their "territory" against the finance departments. The consistent operation of CPAs will also facilitate establishing an integrated nationwide E-GP platform.

Furthermore, it is advisable to reorient the organisational system of the CPAs. As mentioned in Chapter V, at present, a procuring entity should use framework agreements established by the same-level CPA and is not allowed to opt out or to use frameworks set up by other CPAs. The main disadvantages of this organisational model include: (i) the segmented procurement market may facilitate local protectionism; and (ii) CPAs are not incentivised to pursue the best outcomes of framework agreements.

Therefore, it is proposed to liberalise the "right of option" of procuring entities regarding framework agreements and CPAs.[33]

[33] In the US federal system, the use of the GSA Schedules was originally mandatory for the federal agencies, whilst the situation changed after the

It means a procuring entity can move to a framework agreement established by another CPA, which is considered more satisfactory with justified reasons, without being subject to the geography or government-level restrictions. In that case, CPAs will be exposed to competition, the "invisible hand" of which can motivate CPAs to maximise the procurement results to "win customers"; otherwise they may be "punished" for poor performance. The possibility of opt-out may prevent the supplier parties from submitting offers that do not reflect the market, so over-pricing may be avoided to some extent.

2.2.2 Legal and institutional frameworks for the regulation on framework agreements in the procurement of Chinese SOEs

SOEs as procuring entities are not regulated under the Chinese public procurement framework. Their acquisition of works and the works-related supplies and services may be caught by the *TL* because of the involvement of tendering procedures and the type of the procurement project, not due to the special characteristics of SOEs *per se*. This background should be taken into consideration when proposing the regulatory framework on framework agreements by SOEs.

1990s and the GSA had initially been the mandatory source of supply, as mentioned in Ch. III section 4.

2.2.2.1 The modified *Tendering Law* or the *Implementing Regulation of Tendering Law*

It would be the direct path if the *Tendering Law (TL)* or the *Implementing Regulation of the Tendering law (IRTL)*, after substantive amendment serve as the forum for regulating framework agreements by Chinese SOEs. As mentioned above, the *TL* has always been the most relevant national law to the procurement of SOEs, because it covers the majority of their works procurements. Moreover, the *TL* and *IRTL* are the legal base for the relevant ministerial rules as well as internal rules of SOEs on procurement activities, so choosing them as the forum for regulation can ensure consistent implementation and supervision.

However, such option is less viable. Only works and works-related goods and services may be subject to mandatory coverage of the *TL*, whereas framework agreements are mainly used to procure goods and services. Moreover, the *TL* only provides open and restricted tendering, and there is no room for other flexible methods. Therefore, framework agreements based on non-tendering methods (such as competitive negotiations) will be excluded from the *TL* regulation.

An alternative approach is to turn the *TL* into a law that specifically regulates the procurement of SOEs, and framework

agreements could be added and become part of the Law. With the *TL* refocusing on the procurement of SOEs, the *GPL* may be turned into a comprehensive public procurement law. Such re-orientation of the *TL* could fill in the regulatory gap regarding the procurement of Chinese SOEs, remedy the fragmented regulatory system of public procurement and address the "turf battle" between MOF and NDRC.

Unfortunately, such an option is considered less feasible either. In China, the *TL* is classified as civil and commercial law, covering all tendering activities, public or private.[34] Either repositioning the *TL* as a law governing the procurement of SOEs, thus changing the nature of the law, or incorporating framework agreements into the non-tendering methods, thus changing the coverage of the law, would mean a substantial deviation from the original legislative mandate, which would not be allowed. Such substantial amendments, in a way, are arguably equivalent to drafting a new national law. Similarly, there is little chance for the *IRTL*, after substantial amendments, to be selected as the forum for consolidating the rules on framework agreements, because it is based on the *TL* and its provisions should be within the scope of the legal basis; otherwise, it would *be ultra vires*.

[34] National People's Congress classifies the *TL* into Civil Laws in its catalogue of Chinese laws, available at http://www.npc.gov.cn/englishnpc/Law/2007-12/11/content_1383557.htm

2.2.2.2 New Ministerial rules enacted by the State-owned Assets Supervision and Administration Committee of the State Council

Another option is to regulate SOEs' framework agreements through ministerial rules. NDRC may be a candidate for the legislator and supervisor of the proposed rules, considering that it is the drafter and "guardian" of the *TL* and *IRTL*. It is also the coordinator of public resources trading platforms reform, as explained in Ch. IV. Thus, the NDRC has capacity and experience in drafting and enforcing new ministerial rule on the procurement of SOEs. However, its relevant experience is restricted to large infrastructure projects and has not directly involved in supervising SOEs. Therefore, the NDRC is less likely to be the best candidate.

It is argued that the more appropriate and viable option would be for SASAC to adopt a new ministerial rule that regulates the procurement of SOEs specifically, which includes framework agreements. SASAC is considered to be the best candidate for guiding and supervising the procurement of state-owned enterprises for the following reasons.

First, SASAC and its local branches perform the investor's (state) responsibilities, supervises and manages the State-owned assets of SOEs (excluding financial SOEs). They can

extend the right of supervision and management to the procurement of SOEs and thus become the *ex officio* supervisor on framework agreements by exercising the right of investors.[35]

In fact, several local SASAC branches, such those in Ningbo and Wenzhou municipalities, commissioned by the local governments, have issued rules governing the procurement of local SOEs to prevent the loss of state-owned assets and combat corruption.[36] Although these local initiatives can hardly go further, they help to accumulate experience for SASAC to enact rules regulating the procurement of SOEs at the national level.

More importantly, SASAC has been taking charge of the reform of SOEs.[37] In recent years, China has been carrying out a new round of SOEs reform, of which the SASAC is in the driver's seat. As Wang proposed, this on-going reform has provided SASAC with a "golden opportunity" to establish uniform regulations on the procurement of SOEs.[38] Framework

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[35] As explained above in Chapter IV, financial SOEs are managed and supervised by the MOF.

[36] As mentioned in Chapter IV, Wenzhou Municipality used both the *GPL* and *TL* as the legal base to establish the local rules governing procurement by the local SOEs, under which more procurement methods than tendering procedures are available. However, framework agreements are not mentioned in the local rules either. See *Administrative Measures on Procurement of State-owned Enterprises in Wenzhou* (Trial), Aug. 3, 2012, available in Chinese at http://wzgzw.wenzhou.gov.cn/art/2017/8/31/art_1387617_12501478.html; *Guiding Opinion on Administrating Bulk Purchases of Supplies by State-owned Enterprises in Ningbo Municipality*, May 7, 2013, available at http://www.nbgz.gov.cn/art/2013/6/6/art_8228_1471235.html

[37] The responsibilities of SASAC is available at http://en.sasac.gov.cn/2018/07/17/c_7.htm (accessed Aug 5, 2018)

[38] See Wang, Bovis and Tu, fn.2 *supra*, p.22

agreements procurement may be part of the rules, especially given their increasing use by SOEs. Indeed, SASAC has actively released policies and guidance on their procurement, reflecting the increasing attention it pays to this aspect.[39]

On the other hand, however, in the past few years, the "fruits" of SASAC's efforts in the procurement of supplies and services by SOEs are restricted to policy guidance only, and no formal legal rules have been introduced. This may point to the question: whether SASAC has a genuine incentive to regulate the procurement of SOEs. Furthermore, even if the *ad hoc* ministerial rule has been issued, they cannot prevail automatically over local rules where there is any inconsistency, according to the Chinese legislative hierarchy.

2.2.2.3 Soft Law adopted by SASAC

SASAC may formulate guidelines, e.g. issuing handbooks and manuals, on framework agreements for SOEs. Having soft law as the regulatory forum has the advantages of flexibility that allows prompt adaption to the development in the procurement area, as mentioned in section 2.2.1.3 above. It can also respond to the characteristics of SOEs' procurement, i.e. additional

[39] For instance, SASAC in 2010 issued a "Guiding Opinion on Addressing Major Problems in Procurement of Construction Works by Central SOEs", No. 171 [2010] of the SASAC, available at http://www.sasac.gov.cn/n2588035/n2588320/n2588335/c4260831/content.html (accessed Aug 7, 2018)

flexibility and less transparency than government procurement. More importantly, adopting informal rules that guide the procurement of SOEs will not affect the current public procurement regulatory regime and is, therefore, less likely to cause any push-back from the stakeholders.

However, the soft law is always at risk of non-compliance, which especially the case for SOEs whose procurement is substantially unregulated and un-supervise as a whole. In this regard, it is unclear whether and to what extent SOEs will be committed to its implementation seriously.

2.2.2.4 Establishing the Institutional Framework for Regulating Framework Agreements by Chinese SOEs

As explained in the above sections, SASAC should take the lead in the proposed regulation on framework agreements by SOEs, recalling that it has both the incentive and capacity to regulate the procurement of SOEs.[40] Notably, this does not mean that other relevant government ministries and agencies would be excluded from the regulation process. On the contrary, NDRC and MOF should play an active role in framing the regulatory structure and formulating the rules and policies, because NDRC plays the leading role in coordinating different procurement

[40] For the advantages of the SASAC being the leading role, see above in section 2.2.2.

regulators while MOF supervises the management of the financial SOEs. An inter-ministerial committee involving the above ministries as well as other relevant ministries who have interest in regulation should be set up to coordinate the efforts. As mentioned earlier, recently, MOF promulgated an *ad hoc* ministerial rule aiming to regulate the centralised procurement of financial SOEs.[41] However, the fact that the above *Measures* do not mention framework agreements that have frequently been used in practice is disappointing.

In addition to the central ministries, it is also necessary to have local governments that control the local SOEs to engage in the process of norm-setting. Equally important is to ensure close connection and proper consultation with large SOEs such as Sinopec, since they have adopted internal rules and have gained extensive experience in this aspect, from insiders' perspective and reflecting their needs.

Proposing the institutional framework for framework agreements by SOEs almost amounts to designing an institutional framework for the entire procurement of SOEs, which may lead to an overhaul of the overall public procurement

[41] *Interim Measures on Administrating Centralised Procurement by Financial State-Owned Enterprises*, No. 9 [2018] of MOF, available at http://jrs.mof.gov.cn/zhengwuxinxi/zhengcefabu/201802/t20180208_2810447.html (accessed Aug 10, 2018)

system. Such potential, in turn, demonstrates the importance of establishing a viable institutional structure from the outset.

3 The Essence of the proposed regulatory rules

The following section attempts to, informed by the relevant experiences from the selected procurement systems, develop the substance of the proposed regulatory rules on framework agreements. The rules draw substantially from the *Model Law*'s provisions on framework agreements, as they aim to help developing countries such as China that do not have adequate regulatory framework to strike a proper balance between integrity and other procurement objectives. The proposed rules provide only the main contents and necessary procedures and can be applied to any forum chosen for the regulation. There are several caveats to consider in the rule design.

Firstly, as Albano and Nicholas highlight, to achieve "comprehensiveness" of regulatory rules is impossible, no matter how detailed the provisions are, as not all eventualities are foreseeable, especially considering the rapid development of public procurement.[42] Secondly, not all problems related to framework agreements that may arise are legal issues.

[42] G. L. Albano and C. Nicholas, *The Law and Economics of Framework Agreements: Designing Flexible Solutions for Public Procurement* (Cambridge University Press, 2016), p.310

Ineffective implementation and inadequate supporting infrastructure, i.e. inconsistent management of CPAs, equally pose significant obstacles to this procurement instrument.[43]

Moreover, the effective implementation of the proposed regulation also requires detailed guidance, instructions and possibly standard documents issued by the relevant regulatory authorities, as a complement to the formal legal rules, especially in the light of the general lack of procurement professionals in China.[44] As suggested by Albano and Nicholas, "laws and rules set out what a procurement official may and may not to do, but the guidance advises him on what it is appropriate to do."[45]

Last but not least, public procurement is all about trade-offs, which should be properly struck in the rule-design process. The main trade-offs may include first, the balance between the need

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[43] *Ibid.*

[44] For instance, the *Guide to Enactment of the UNCITRAL Model Law on Public Procurement* is provided to support the *Model Law*. In the UK, the Crown Commercial Service also issued the *Guidance on Framework Agreements* to ensure the effective implementation of the legal rules. The latest update was in Oct. 2016, available at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/560268/Guidance_on_Frameworks_-_Oct_16.pdf. In the US, General Services Administration issued the *Multiple Award Schedules Desk Reference* as a guidance tool for the users to use the GSA Schedules, the latest version was made in 2016, https://www.gsa.gov/acquisition/purchasing-programs/gsa-schedules/schedules-news-training/mas-desk-reference.
Apart from that, the OECD also provides "Manual for Framework Agreements", (OECD, 2014) which provides detailed and useful instructions on how to structure and manage framework agreements, drawn from the EU's experiences, available at http://www.oecd.org/gov/public-procurement/publications/ (accessed Aug 12, 2018)

[45] See Albano and Nicholas, fn. 42 *supra*, p. 310

for more robust transparency to combat corruption and improve integrity on the one hand[46], and the need for flexibility to achieve value for money and efficiency on the other. SOEs particularly need additional flexibility to meet their commercial needs. It is also necessary to balance between the intricate design and operation of the first stage and the ease of use of the call-off stage.[47] A further trade-off should be made between the need to improve supervision and enforcement by allowing challenges against orders under frameworks and the potential risk of excessive disruption to the procurement process. These trade-offs will be reflected in the rules.

3.1 Definition

Proposed Definition:

> A framework agreement is an agreement between by one or more procuring entities with one or more suppliers for the purpose of establishing the terms and conditions for future procurement contracts during a given period.[48]

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[46] As explained in Chapter V and VI, anti-corruption was the starting point to regulating public procurement and is considered the top procurement objective. The flexibility and uncertainty of framework agreements due to their particular structures create more opportunities for corruption.

[47] Albano and Nicholas consider such balance is a key distinction in framework agreements procedures. See Albano and Nicholas, fn. 42 *supra*, p.322

[48] The proposed provisions are intended to provide an example, based on the legal language and expression under the *Model Law*. The author does not mean to make laws herself. On the other hand, it is her interest and plans to identify the critical issues for the consideration of Chinese policy-

Providing a clear definition of framework agreements is essential because it reveals the nature of frameworks, allowing to have a general understanding of framework agreements and to distinguish them from other procurement methods. Therefore, it is an essential starting point of the proposed regulation and requires much preparation and thought. The following issues need to be considered when defining framework agreements.

- **Entity coverage/ The scope of the procuring entities**

Procuring entities in the definition are used as a generic term referring to the establishers and users of framework agreements. In government procurement, procuring entities include government agencies, public institutions and social organisations (users) as well as CPAs (initiators) at the central and local government levels.[49]

On the other hand, the entity coverage regarding Chinese SOEs has been less considered and may merit a second thought. It is recalled that the application of the public procurement rules to the procurement by SOEs is primarily determined by the type of the subject matter to be procured and the involvement of tendering procedures. The special characteristics of SOEs as

makers. The legal techniques and expression are beyond the scope of this thesis.

[49] The scope of procuring entities covered by the *GPL* is under art. 15

purchasers and the sectors they operate have not been factored in. As a result, their procurement of goods and services remains unregulated to date. As discussed in Ch. IV section 6.1, there is arguably a need to subject the procurement of SOEs to appropriate regulation and supervision. Compared with the current basis to determine the regulatory coverage, the characteristics of SOEs as purchasers/ procuring entities-entity coverage-tends to be more appropriate and simplified.

The question herein comes: should all SOEs as purchasers be covered by the proposed regulation? Almost all Chinese SOEs are direct or indirect controlled or influenced by the governments. In light of the extensive incidents of corruption involved, the procurement of all SOEs, including through frameworks, should in principle be subject to regulation. However, it is strongly suggested that the competitive environment where an SOE operate should also be taken into consideration when determining the scope of coverage, following the EU's approach on this issue under the *Utilities Directive*.[50] For instance, when an SOE operates in a fully competitive market, there is no need to regulate their framework agreements, which may be exempt from the

[50] See Wang, Bovis and Tu, fn. 2 *supra*, p.152

regulation, as competitive pressures will drive SOEs to procure based on commercial considerations.[51]

In September 2015, the State Council and CPC issued *Guiding Opinions on Deepening the Reform of State-Owned Enterprises* and instituted a system for classifying SOEs into (i) publicly-oriented SOEs (gongyixing guoqi), which are those in utilities sector providing public goods and services; and (ii) commercially-oriented SOEs (jingzhengxing guoqi), which seek to obtain commercial goals.[52] SOEs are envisaged to be divided into two groups by virtue of the commercial/ competitive environment where they operate.

This new classification system may coincidently provide a way forward to determine the entity coverage of SOEs for the proposed regulation. Specifically, the publicly-oriented SOEs may be covered by the proposed regulation, and the commercially-oriented ones may be exempted, as the latter need to be fully competitive. However, the classification system has not been fully implemented in practice. To this day, there is

[51] Article 30 of the *EU Utilities Directive*. For more discussion, see C. Bovis, *EU Public Procurement Law*, (2nd edn, Edward Elgar, 2013); OECD, "Procurement by Utilities", Brief 16 of the *SIGMA Public Procurement Briefs* (August 2011); S. Arrowsmith (ed.), *EU Public Procurement Law; An Introduction* (2011), available at https://www.nottingham.ac.uk/pprg/documentsarchive/asialinkmaterials/eupublicprocurementlawintroduction.pdf (accessed Sep 1, 2018)

[52] "Guiding Opinions of the Central Committee of the Communist Party of China and the State Council on Deepening State-Owned Enterprise Reform", State Council Gazette Issue No. 27, Serial No. 1530 (Sep. 30, 2015), available at http://english.gov.cn/archive/state_council_gazette/2015/09/30/content_281475201435679.htm (accessed Sep 10, 2018)

no unified definition of publicly and commercial oriented SOEs. It remains unclear how to classify SOEs objectively to date.

- **Types of Framework Agreements Permitted**

As explained in Chapters V and VI, multi-supplier and multi-user framework agreements are the norm in both Chinese government procurement and procurement of SOEs and operate primarily in centralised purchases. The proposed rules are suggested to allow and reflect the established practice. On the other hand, this is not to say that single-supplier and/or single user framework agreements should be prohibited. It may be more appropriate to keep room for single user and/supplier framework agreements, especially for Chinese SOEs. It is possible for SOEs to award a framework agreement to establish a long-term relationship with one or multiple strategic suppliers. It may be an option for China to establish a statutory preference for multi-supplier framework agreements, following the US approach, to encourage competition while providing the possibility of single-supplier and single-user frameworks.[53]

Regarding framework agreements with second-stage competition and those without, they are both common in practice and should be permitted under the proposed regulation. As described in Chapter V, in Chinese government procurement,

[53] *Federal Acquisition Regulation* (FAR), 16.504 (c)

the ordering procedures mainly depend on the size/value of the order and the proposed rules regarding the second-stage may repeat the existing practice. SOEs rely more on order allocation in call-offs, with less involvement of second-stage competition.

There is little dispute as to whether framework agreements should be binding on either or both parties in the proposed regulation, since the use of framework agreements in Chinese government procurement for centralised purchasing has always been mandatory. For Chinese SOEs, framework agreements are usually regarded as sales contracts and therefore are binding on both parties.[54]

As per the classification in Chapter II, framework agreements can also be divided into closed and open framework agreements, based on whether new suppliers can join after the conclusion. It is clear from the previous chapters that almost all of framework agreements in China are closed. Open framework agreements are rare in practice and have received little attention so far. Doubts may be expressed whether to include and permit open framework agreement in the proposed rules.

It is widely known that open framework agreements have various potential benefits, such as enhanced transparency, more effective competition and greater efficiency. They allow

[54] For example, see the definition of framework agreements under Sinopec internal rules in Ch. VI section 2.

certain terms to be finalised close to the moment when a specific need arises and better reflect the actual market conditions. Therefore, open framework agreements are considered to be very suitable for off-the-shelf items and/or purchases with volatile prices, such as some IT items.

Despite the benefits, the author decided not to include open framework agreements in the proposed regulation and the main reasons are as follows. Firstly, open framework agreements are rarely used or even noticed in practice. Secondly, introducing a "new" form of frameworks may provide overlapping options for purchasers that add complexity to their decision-making on the use of framework agreements, in light of the general poor procurement capabilities in China. Thirdly, the advantages of open framework agreements are expected to be largely achieved through closed frameworks based on electronic techniques and, particularly, electronic marketplace, which has been rapidly developing.

As explained in Chapter V, there has been a trend towards developing electronic marketplace in Chinese government procurement, providing a transparent, streamlined and rapid way to purchase off-the-shelf goods and services. Large SOEs are also establishing their own internal electronic platforms to

achieve efficient acquisitions.[55] It will be desirable to have formal rules dedicated to electronic marketplace to provide an adequate legal basis, provide procedural safeguards to ensure their appropriate use, and more importantly, to improve the interoperability of various electronic marketplaces built by different government agencies and SOEs, such as formulating uniform technical standards.

- **Whether the subject matter of framework agreements is restricted to goods and services?**

It is suggested to restrict the subject matter of framework agreements to goods and services. It means that framework agreements will not be allowed to procure works. This limitation on the subject matter is based on the following considerations.

First, established practices indicate that both government agencies and Chinese SOEs use framework agreements primarily, if not all, for purchasing goods and services. There are too few cases in which the works are procured through frameworks. Secondly, the inherent flexibility and uncertainty of

[55] For instance, Sinopec operates its own online shopping mall called "EPEC", available at https://mall.epec.com/ecmall (accessed Aug 10, 2018). A number of large SOEs have established their own electronic marketplace, such as China Telecom Group (in communication sector), State Grid Cooperation (in electricity sector), China Guodian (in electricity sector) and China Railway Group (in transport sector), whose internal e-marketplaces are respectively available at http://www.ctebuy.com/pmsWebIndex.do?action=index; http://ecp.sgcc.com.cn/html/center_server.html#; https://www.neep.shop/; and http://mall.crecgec.com/?channelType=02 (accessed Aug 18, 2018)

framework agreements may pose a higher level of risk of irregularities to procure works, especially considering the fact that corruption remains to be endemic in China. Thirdly, framework agreements are not a necessary option for procuring works. Government agencies and SOEs have other methods available that enable them to acquire works with flexibility, including competitive dialogue and competitive negotiations.

- **The legal status of a framework agreement**

There is no concept of "procurement contract" or "public contract" in Chinese public procurement laws. Article 43 of the *GPL* stipulates that the *Contract Law* shall apply to the contracts for government procurement, which however does not necessarily mean that government procurement contracts are equal to civil contracts.[56]

Clarifying the status of a framework agreement as a matter of *Contract Law* is crucial in that it defines the roles and responsibilities of the involving parties in a framework agreement. Based on established practice, it is recommended that framework agreements be defined as a procurement method, following the *Model Law*'s model, and that a framework

[56] In contrast, the *Model Law* defines "procurement contract" in Article 2(k). At the EU level, the 2014 Public Sector Directive defines "public contracts" in Article 2(5). In the US federal procurement, the *Federal Acquisition Regulation* 2.101 also explains the meaning of "contract".

agreement/master agreement itself be distinguished from a procurement contract. A master agreement is the result of the first stage (conclusion stage), and specific procurement contracts are awarded at the second stage. The purpose is to ensure both stages of a framework agreement are covered by the procedural safeguards, with particular regard to the supplier review and remedy mechanism.

It is worth noting that this approach does not rule out the possibility that a framework agreement can be converted into a contract under the Chinese *Contract Law*, as is the case in the EU. In fact, as mentioned in Chapter VI, Chinese SOEs such as Sinopec tend to regard framework agreements themselves as sales contracts.[57]

- **Encouraging the use of electronic techniques and tools**

Promoting e-government procurement and e-tendering has become an essential component of China's strategic e-governance initiative to enhance transparency and good governance.[58] In reality, electronic techniques have been used

[57] "China Petrochemical Corporation (Sinopec) Rules Administrating Framework Agreements Procurement", art. 1.2, available at https://wenku.baidu.com/view/d614cd77ec630b1c59eef8c75fbfc77da369970b.html?re=view (accessed June 10, 2018)

[58] P. Wang, "Development of Electronic Government Procurement in the People's Republic of China" (Consultant's report to Asian Development Bank, October 2011), pp.19-20

in procurements by Chinese governments at both central and local level for long. Framework agreements have become the main "carrier" for electronic techniques such as electronic reverse auctions. Most of the existing e-government procurement platforms involve e-procurement subject to framework agreements, and an increasing number of SOEs have also started to conduct electronic procurement.

All the above facts suggest the possibility of operating framework agreements on an electronic basis and the electronic infrastructures are gradually improving. On the other hand, the effective use of electronic techniques and tools in the context of framework agreements can contribute immensely to fulfilling the robust transparency and competition requirements in the proposed regulation. For instance, the mandatory notification of upcoming orders and award notices after orders are placed will be required. Given the above, e-procurement should be encouraged in the cases of frameworks.

3.2 Conditions for Use of Framework Agreements

Proposed condition for use in Chinese government procurement:

> Framework agreements may be used to procure common-use and relatively standard goods and services that are expected to be repetitively needed within a given period.

Proposed condition for use in procurement for Chinese SOEs:

> Framework agreements may be used to procure goods and services when the timing and quantity of the need cannot be defined at the time of agreement award.

Not all procurement systems impose "conditions for use" of framework agreements in their legal rules. Among the three systems reviewed in the research, the "conditions" are provided under the *Model Law* and in the US, albeit in different ways, but are absent in the EU Directives. The *Model Law* define the circumstances, and the US federal procurement describe the circumstances where frameworks may be used.[59] Then the question may arise, that is whether or not to impose "conditions for use" of framework agreements in the proposed regulation.

The current author believes that "conditions" are needed, based on the general lack of procurement professionals and skills. The decision on whether to employ a framework agreement is a complicated task that goes beyond the mechanical application of thresholds used for determining some "traditional" procurement methods (such as open tendering)[60].

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[59] For more discussion about the different approaches to providing "conditions for use" of framework agreements in different procurement systems, see Albano and Nicholas, fn. 40 *supra*, pp.311-315; L. Ș. Filipon, *Non-Traditional Regular Purchasing Arrangements in Public Procurement- A Doctrinal and Comparative Analysis of Regulation and Implementation Systems*, PhD Thesis, University of Nottingham, School of Law (March 2018), pp. 294-300. According to Filipon, the EU's "liberal approach" in this respect may be understandable, on account of their role at the EU level.

[60] *Ibid.*

A sound decision requires procurement capacities and experiences, whereas China now lacks quantitively and qualitative sufficient procurement workforce. The procurement officers may have no idea whether a framework agreement is appropriate or not for a procurement project and do not know what goes into the decision-making. Nevertheless, if the conditions for use are imposed, once the conditions are met, frameworks may be used. Therefore, having conditions for use may be more effective in Chinese public procurement.

In Chinese government procurement, the conditions for the use of framework agreements can largely replicate the expressions in many local rules, as described in Chapter V. The established practice indicates that framework agreements are mainly and only used in repetitive purchases of common-use and relatively standard goods and services, i.e. office supplies and maintenance services. Moreover, it is reiterated that a precondition to the use of framework agreements in government procurement is that the subject matter should be within the centralised procurement catalogues, which, in fact, effectively cover off-the-shelf items only.

As regards framework agreements by SOEs, Albano and Nicholas suggest to adopt a soft and broad approach to providing conditions of use, that is to describe but not define the main circumstances where framework agreements may be

used.[61] The broad approach is considered more appropriate because, first of all, it is less feasible to define exhaustive, clear and unambiguous conditions for the use of framework agreements. This can be demonstrated by the uncertainty under the *Model Law* on how to construe "expectation" in the condition for use of framework agreements.[62] Moreover, this approach allows SOEs to have greater flexibility in using frameworks and to avoid the risk of being overly restrictive.

The proposed conditions of use above embrace the two scenarios in which SOEs primarily use framework agreements. Firstly, framework agreements may be used in purchases of goods and services that are expected to be continuously or repetitively required for a given period. According to Kraljic classification, these items are often referred to as leverage items, such as the pipeline for SOEs in the communication sector. [63] This condition is identical to that in Chinese government procurement. Alternatively, framework agreements may be used to procure certain goods or services to ensure the security of supply. These items can be referred to as bottleneck supplies as per the Kraljic classification. For instance, a SOE

[61] The *FAR* states that "…with a simplified process for obtaining commercial supplies and services at prices associated with volume buying". As Albano submitted that, "describing circumstances rather than defining circumstances tends to be a more effective approach". See Albano and Nicholas, fn. 39 *supra*, p.314
[62] See Chapter III section 2
[63] See Chapter VI section 3 above.

may use a framework agreement to establish a long-term supply relationship with a supplier for components with special technical requirements.

Notably, the aim of proposing conditions for use is to encourage the appropriate use of framework agreements. Fulfilling the conditions does not guarantee frameworks can always be used in appropriate circumstances. A robust and thorough analysis of the procurement requirement and potential consequences is further needed to justify the use of frameworks, as will be suggested right below.

3.3 Procedural rules

Albano and Nicholas suggested that the procedural rules for both stages of a framework agreement should be clear and unambiguous because they directly lead to contractual relationships between the procuring entities and suppliers.[64] Uncertainty can otherwise cause discretion and further lead to irregularities. The text in brackets is intended for application by Chinese SOEs.

[64] See Albano and Nicholas, fn. 40 *supra*, p. 314

3.3.1 The first stage: Conclusion of a Framework Agreement

Proposed procedural rules:

1. Procurement planning is an essential phase to set up a framework agreement. [A procurement plan may be required by the end of planning phase]

2. The procuring entity shall conclude a framework agreement:
(a) By means of open tendering procedures;
(b) By means of other procurement methods when open tendering is considered inappropriate.

3. A solicitation for a framework agreement shall include:
(a) description of the subject matter of the procurement, including the estimated quantity or value of the supplies and services that will be required;
(b) the terms and conditions upon which suppliers are to provide the subject matter of the procurement under the framework agreement;
(c) the criteria that will be used to select the suppliers admitted to the framework agreement;
[(d) the estimated number of suppliers or any restriction on the number of suppliers to be admitted to the framework agreement;]
(e) the duration of the framework agreement;
(f) Whether there will be a second-stage competition involved; and the procedures and criteria to be used in issuing orders at the second stage.

[4. where the SOE intends to use an existing supplier list as pre-qualification to set up a framework agreement, it shall:
(a) maintain the supplier list open to the market; or
(b) solicit tenders from suppliers beyond the supplier list, except in justified circumstances, subject to justifications]

5. The provisions governing the evaluation of tenders, award of procurement contracts as well as the public notice of awarding procurement contracts, after necessary modification, shall apply *mutatis mutandis* to the conclusion of a framework agreement, i.e. the period of awarding a contract after the award decision and the media for award notice publication.

6. A framework agreement shall be concluded, and its contents shall include:
(a) the description of the subject matter of the procurement;
(b) the terms and conditions of the procurement that have been established;
(c) the procedures and criteria to be used in issuing orders;
(d) any information regarding electronic procurement tools or mechanisms where applicable in the second stage.

- **Procurement Planning**

Benjamin Franklin once said, "If you fail to plan, you are planning to fail". Framework agreements are not a substitute for

procurement planning. The success of a framework agreement depends on careful procurement planning, especially in light of its two stages of operations. Two broad questions need to be appropriately addressed in the planning phase, including (i) whether to use a framework agreement in a specific procurement; and if so, (ii) how to design and structure the framework agreement to obtain the best procurement result.

Deciding whether a framework agreement is a more appropriate solution to address the procurement need is far more than mechanical application of thresholds used for determining the use of open tendering. A thorough demand and market analysis and a robust assessment of the expected benefits and the potential risks of using a framework agreement will be necessary.[65] The analysis should be conducted by procurement officials of CPAs (in Chinese government procurement) and that of the procurement department within SOEs. The proposed conditions for use provide some "aid" in the planning process at the legal/policy level, with the aim of encouraging the appropriate use of frameworks. However, this is not to suggest that meeting the conditions can always guarantee the appropriate use of frameworks. Therefore, a cost-effective analysis, based on demand and market research, can

[65] See L. Ş. Filipon, fn. 59 *supra*, p.299

be further useful to support the decision-making process, as an option provided in the *Guide to Enactment of the Model Law*.[66] Only when the expected advantages overweigh the potential disadvantages, the use of framework agreements can be justified as a more effective solution than other methods.

The procurement officers would be less bothered to determine the type of frameworks to be used. In Chinese government procurement, multi-supplier multi-user frameworks will be the norm for centralised purchases. The CPAs need not choose between closed or open types because all frameworks are closed in that context. Moreover, they don't need to ponder whether to award contracts with reopening the second-stage competition. As for Chinese SOEs, the procurement department may need to carefully determine the type of frameworks to be used on the basis of the demand and market analysis.[67]

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[66] See Ch. III section 2 above.

[67] The section will not elaborate on the appropriate conditions for using each type of framework agreements. The advantages and risks of different types of frameworks have been briefly analysed in Chapter II section 3 above. For discussions about selections among types of framework agreements, see L. Ș. Filipon, fn. 59 *supra*, pp. 301-324. Among the systems reviewed in the research the UNCITRAL *Model Law* itself does not provide conditions for the use of different types of framework agreements, but the Guide to Enactment provides relevant guidance. The US federal procurement provides the factors to consider in determining whether to use multiple IDIQs and the number of awardees to be selected. See Chapter III sections 2 and 4 above. The EU Directives have no equivalent requirement.

Where the procurement officials decide to use a framework agreement, they will proceed to design and structure it. The design should cover both the conclusion and ordering stages. It is important to keep in mind from the outset that good design is critical to reducing risks and ensuring ease of use at the later stage, and to securing competition and transparency throughout the procurement process.[68] Care should be taken in considering a number of sub-issues, such as the award procedures to conclude a framework agreement, setting terms and condition for future awards, the involvement of a second-stage competition, the awarding mechanisms at the second stage, the consistency between two stages, etc.

For a multi-supplier framework agreement, especially in centralised purchases, which is the most common form of frameworks in China, the appropriate number of suppliers to be admitted to the framework, the level of demand aggregation, the design of lots division should also be properly addressed at this stage. Where a second-stage competition is involved, it is necessary to consider how to balance the competition between two stages.[69] All the considerations and results of all relevant issues can be fed back to the fundamental question as to

[68] See Albano and Nicholas*,* fn. 42 *supra,* Chapters 9 and 10.
[69] Albano and Nicholas have discussed these two issues from an economic analysis. *Ibid.*

whether a framework agreement is more effective for the given procurement than other procurement methods.

As discussed in Chapters V and VI, in China, CPAs and SOEs often bypass the planning stage and seemly rush to the solicitation process. Apart from the fact that the value of planning has been usually overlooked, the reasons for the weak procurement planning includes the difficulty or inability of the most procurement officials to plan effectively and correctly, as they may have no idea what goes into the planning process and how they should proceed.

Given that, it is firstly suggested to establish a formal obligation of conducting procurement planning for using framework agreements, by which procurement officials should undertake a meticulous and thorough demand and market analysis. In the US, the *FAR* clearly states that deciding to use IDIQs is part of planning. The *Model Law* and US federal system both require the procurement officials to justify the decision to use frameworks (and the type of frameworks) and to document the decision (as well as the reasons). China is suggested to learn from the "good practice". The obligations are envisaged to force the procurement officials to take planning seriously.

The obligation does not in itself lead to effective planning, which requires detailed procedures and guidance to clarify how the planning process should be carried out, especially in light of

the lack of procurement capacity in China. Thus, it is necessary to provide some assistance at the policy level. Internal rules and guidance adopted by the regulatory authorities in cooperation of external expertise will be necessary. The various guidelines issued within the Member States in the EU are excellent examples.[70] It would be rather useful to provide a template which provides an illustrative list of the most important information about frameworks in line with the procurement process. Such as list should be completed and documented by the end of the planning phase. This task can alert procurement officials to consider the issues listed in a consistent way.[71]

Procurement planning process should involve effective communication and engagement with various stakeholders. They may include suppliers, user entities, supervision authorities, external experts and potentially media and the public in a transparent manner. The interaction not only helps

[70] For example, in the UK, the Scottish government and Welsh government provide clear instructions on the planning process of a framework agreement. See "Scottish Government Guidance on Framework Agreements" SPNN 05/2010, available at http://www.gov.scot/Topics/archive/spdlowlevel/framework (accessed Aug 6, 2018); "Framework Agreements: Procurement Advice Note (PAN) for the Welsh Public Sector", Welsh Government (July 2017)

[71] In the Annex part of the "Manual for Framework Agreements", OECD provides the "Summary form template" and the "Feasibility study template". They provide valuable examples of what to include in the supposed guiding template. More template documents and index can be found in the "Public Procurement in Chile: Policy Options for Efficient and Inclusive Framework Agreements", (OECD 2017), Annex, available at http://dx.doi.org/10.1787/9789264275188-en (accessed Aug 6, 2018)

to better formulate the framework agreement but also helps to gain public trust.[72]

- **Which method will be used to conclude a framework agreement?**

It is suggested that open tendering should be considered first to conclude a framework agreement, and other methods are only available in reasonable circumstances with justifications.[73] This provision, following the *Model Law's* approach[74], is based on three considerations.

First, the established practice indicates that open tendering has been the default method to set up framework agreements in Chinese government procurement. Secondly, open tendering can promote wide participation, thus enhancing competition and transparency in purchases of standard supplies and services, consistent with the primary objective of anti-corruption and further the value for money. Thirdly, it allows SOEs to choose methods other than open tendering when they consider more

[72] OECD, "Manual for Framework Agreements", (OECD 2014), p.38
[73] From the relevant international experience, open procedures are also the main method used in other procurement systems to establish framework agreements, as is the case of Multiple Award Schedule Contracts (the equivalent of framework agreements) in Korea. See OECD (2016) "The Korean Public Procurement Service. Innovation for Effectiveness", OECD Governance Reviews, p.64
[74] Article 58 of the *Model Law*. In the EU, procuring entities can use any procedures allowed under the Directives. However, this can hardly apply in China because of the poor procurement capacity and the lack of adequate and ongoing transparency throughout the framework agreements process.

appropriate. In reality, SOEs favour restricted procedures to set up framework agreements.

One caveat is that, in designing the rules applicable to SOEs, their common practice of using supplier lists (known as qualification system in the EU) should also be considered. As described in Chapter VI, Chinese SOEs often use supplier lists as the qualification process before launching a framework agreement, and only those registered suppliers may be invited to submit tenders and participate in the first-stage competition. It is not uncommon for supplier lists to be "closed" after the original licencing/ registration, which thus wall off the procurement market.

Ensuring an effective qualification and selection process is critical as they often result in a reduction of the number of competitors in the tendering, thus immediately affecting the degree of competition in a specific procurement.[75] The use of supplier lists as a qualification mechanism has an immediate and negative impact on fair competition through restricting the relevant market entrance. More importantly, the procurement personnel of SOEs are highly likely to abuse the discretion in registration to favour or discriminate certain suppliers. In that

[75] S. Treumer, "Exclusion, Qualification and Selection of Candidates and Tenderers in EU Procurement", Ch. 1 in M. Burgi, M. Trybus and S. Treumer (eds.), *Qualification, Selection and Exclusion in EU Procurement* (DJØF Publishing, 2016), p.15

case, supplier lists may become a shelter for irregularities and be pro-collusive.[76]

The above risks make it necessary for supplier lists to be "open" to new potential suppliers, following the EU's model in regulating qualification systems in the utilities sector.[77] In that case, new suppliers with interest have the opportunity to request registration and thus have the chance being invited to participate in the competition for frameworks. Another option can be to make the competition to enter into frameworks be "open" to the market. It means SOEs should also solicit tenders from suppliers beyond the supplier lists to ensure adequate competition. For instance, SOEs may advertise the solicitation for a framework agreement and at the same time invite the suppliers on the lists to submit tenders. All received submissions should be assessed equally. The key here is to ease or reduce the barriers to entry and attract wide participation, which may be achieved by keeping the either lists or the solicitation open. On the other hand, where SOEs have justified reasons to restrict competitions to supplier lists, for example, due to commercial confidentiality reason, the exceptions should be allowed.

[76] The magnified anti-competitive effect of using mandatory supplier lists and closed framework agreements simultaneously is pinpointed in Chapter VI section 4.
[77] *The EU 2014 Utilities Directive*, Art. 77(1)

- **Information to be included in solicitation documents and a framework agreement**

It is necessary to provide information that should be included in the solicitation documents and the master agreement to enhance transparency and accountability. This is to ensure that the terms and conditions are known and consistent throughout the process.[78] Any deviation from the established can be easily identified. The *Model Law,* EU Directives and US federal procurement have similar provisions specifying the contents in the procurement documents.[79]

A solicitation should include the description of the subject matter that details the general nature and scope of the required supplies and services. They should also include an estimated total quantity or value of future requirements, because higher accuracy can elicit better offers, as analysed earlier in Chapter VI. Detailed contents and effective accountability measures will force procurement officials to focus on and devote efforts to procurement planning, especially demand analysis.

It is strongly suggested to include the estimated number of suppliers or any minimum or maximum limit on the number of suppliers that to be admitted to the framework agreement in

[78] Guide to Enactment, p.276
[79] *The Model Law*, Article 58-59; Articles 49 and 50 and the relevant Annex V Part C of the EU *Public Sector Directive*; *FAR* 16.504 (4)

the solicitation, to the extent of known.[80] A right number of awardees matters because it determines the market for the subject matter within the duration, thus determining the competition involved. And either too many nor too few awardees can adversely impact the competition.[81] In China, as analysed above in Chapter IV, in few cases the procurement officials have pondered over the right number of awardees for a framework agreement. It is common that a framework is concluded with a higher number of suppliers than actually needed, especially in government procurement. An excessive number of awardees may not only soften the competition at the first stage but also lead to an onerous and lengthy ordering process. Given the above, by requiring the information on the expected range of number of awardees, CPAs and SOEs may be forced to carefully consider this issue during the planning phase. While transparency can lead to effective competition, it may also facilitate collusive strategies among the participating suppliers because it improves the demand predictability and allows coordination on pie-sharing.

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[80] Such similar requirement is also provided under Article 58 (2)(c) of the Model Law, Annex V Part C of the *EU Public Sector Directive*. In the US regime, the *FAR* 16.504 (c)(ii)(A) states that the number of awardees should be considered.

[81] According to Albano and Nicholas, a right number of supplier parties to a framework agreement strikes an appropriate balance "between competition at the first stage and supply diversification at the call-off stage." See Albano and Nicholas, fn. 42 *supra*, pp. 263-264; OECD, "Public Procurement in Chile: Policy Options for Efficient and Inclusive Framework Agreements" (2017); "Manual for Framework Agreements" (2014)

All the terms and conditions to the extent of known should be included in the solicitation document. The terms include qualification and evaluation criteria (of both stages), the terms of the master agreement and those of the future contracts, etc. From the practice, price has been generally included in the procurement documents. Instead of a fixed price, a pricing mechanism is also permitted. As provided in Chapter V and VI, discount rate and price ceiling are common-use pricing mechanisms. Procurement officials should ensure the terms are consistent between two stages to avoid any irregularities in subsequent call-offs, i.e. favouritism and corruption.

The result of concluding a framework agreement should be publicised. In Chinese government procurement, the provisions on publishing award notices under the *Administrative Measures on Government Procurement Information Publicity* should be modified to accommodate framework agreements. As to the case of SOEs, it is desirable to have a unified portal that conveys all information regarding the procurement of all Chinese SOEs. At present, it seems feasible to require SOEs to advertise and publish award notices on the Public Resources Trading Platforms as mentioned in Chapter IV. For those SOEs that have their own electronic platforms, they are encouraged to make the information public therein.

All of the above requirements are designed to promote transparency, which is identified to be one of the most effective ways to achieve integrity and accountability of public procurement. However, transparency may wield a double-edged sword. On the one hand, transparency may be an element that may heighten the risk of collusion among suppliers that are parties to the framework, especially the disclosure of their identities and the estimated value and frequency of call-offs to be made.[82] The information may induce supplier parties to prepare and coordinate to split the call-offs. On the other hand, however, the impact of transparency in collusion tends to be often overestimated. The risk of limiting transparency is often greater than the possible benefits in terms of preventing collusion. As Albano and Nicholas suggest, "…any doubts about whether to disclose or withhold information should be resolved in favour of disclosure".[83]

On consideration of the above, the author considers that lack of transparency has been endemic in Chinese public procurement, which may create opportunities for irregularities and also lead to negative and biased public perceptions in this

[82] See G. L. Albano, A. Ballarin and M. Sparro, "Framework Agreements and Repeated Purchases: The Basic Economics and A Case Study on the Acquisition of IT Services", *International Public Procurement Conference* (Seoul, 2010)
[83] Albano and Nicholas, fn. 42 *supra*, p.191

area.[84] The procurement policies and design therefore may tilt towards anti-corruption and pro-competitive disclosure than withholding information for collusion prevention. This is also the policy approach adopted behind the provisions under the *Model Law*.[85] Nevertheless, there is always risks of collusion and anticompetitive behaviours do exist. Albano and Nicholas have elaborated the transparency-related considerations in framework agreements and have raised measures that help address risks of collusion (including the preventing measures and the measures to detect and punish collusions if any).[86] The procurement regulatory authorities in China are suggested to use their study as a reference, and in light of its own procurement context, considers the appropriate balance between transparency and the risk of collusion in frameworks

[84] According to a report by the Rules of Law Index Research Centre, Chinese Academy of Social Science (CASS), there was a general lack of transparency in procurement through framework agreements. 31 provincial governments and 93 municipal governments were involved in the investigation, among which 4 provincial governments and 33 municipal governments did not publish notices regarding the conclusion of framework agreements at all. Furthermore, 5 provincial governments and 14 municipal governments did not disclosure any information regarding the call-offs awarded under framework agreements. See "Assessment Report on Transparency of Government Procurement in China", Rules of Law Index Research Centre (2016).

[85] UNCITRAL, "Report of Working Group I (Procurement) on the Work of Its Fifteenth Session" (New York, 2-6 February 2009), A/CN.9/668, para.146-148

[86] This research does not elaborate how to determine the appropriate extent of transparency requirements in framework agreements to balance the need for integrity and the need to mitigate the risks of collusion. For in-depth discussions about how to address collusion risks in framework agreements, see Albano and Nicholas, fn. 42 *supra.* Chapter 9 and 10.

and issues guidance that assist procurement officials on how to mitigate the risks of collusion.

3.3.2 The second stage: Call-offs under a framework agreement

Proposed rules governing the second stage of a framework agreement in Chinese Government Procurement:

1. Orders based on a framework agreement should be placed in accordance with the terms and conditions of the framework agreement and the following provisions.
2. An order under a framework agreement may be awarded only to a supplier that is a party to the framework agreement as concluded.
[3. Where a framework agreement is concluded with a single supplier, orders based on that agreement should be placed within the limits of the terms established in the framework agreement.]
4. Where a framework agreement is concluded with multiple suppliers, an order shall be placed in one of the following ways:
(a) Direct award. For an order valued not exceeding ¥ X (threshold), the procuring entity may choose a supplier party it considers appropriate;
(b) Second-stage competition. For an order valued exceeding ¥ X (threshold), the procuring entity shall
(i) invite at least three supplier parties to the framework agreement to submit their offers for the requirement, in accordance with the prescribed procedures; and

(ii) notify all supplier parties of the upcoming second-stage competition, so that the un-invited suppliers that have interest in and are capable for the order can request to participate;

(iii) evaluate all submissions and determine the supplier that presents the best tender to place an order in accordance with the disclosed award criteria.

5. The procuring entity shall publish a notice of the procurement result for each order placed under the framework agreement on the designated media.

6. The procuring entity shall document all order(s) under a framework agreement in terms of the reasons for placement and price of each order.

Proposed rules governing the second stage of a framework agreement by Chinese SOEs

1. Orders based on a framework agreement should be placed in accordance with the terms and conditions laid down in the framework agreement, which may or may not include a second-stage competition among the supplier parties to the agreement.

2. Where a second-stage competition is involved, all the supplier parties to the framework agreement should be informed of any second-stage competitions, regardless of whether being invited to participate or not. The procuring entity shall accept the best tender on the basis of the award criteria set out in the framework agreement.

3. The procuring entity shall group notices of the procurement results for orders placed under the framework agreement on a periodic basis and send the grouped notices by the end of each prescribed period.

4. The procuring entity shall maintain a record of order(s) under a framework agreement.

- **Procedures of order placement: Whether the second-stage competition is involved or not in Chinese government procurement**

It is proposed that whether the second-stage competition is involved or not at the ordering stage depends on the size/value of the purchase, in Chinese government procurement. The threshold for the mini-competition should be determined based on an in-depth and thorough analysis, and adjusted periodically according to the market practice, for example, every three years. The suggested procedures for the second stage are similar to the US approach in governing the ordering stage under IDIQ contracts, where the size of the order is used as the primary criterion for deciding the procedure.[87] This proposal is based on several considerations.

Firstly, under the Chinese government procurement system, as described in Chapter V, it has been usual practice to determine the second-stage procedures based on the size of the order, and to require large orders to be issued through a mini-

[87] See Chapter III above. In fact, using the value development in separate orders as the primary criterion for the second-stage procedure is also seen in other procurement systems, such as in Korea. In framework agreements (known as Multiple Award Schedule Contracts) in Korea, direct awards are used to award simple transactions, while the second-stage competition applies in larger purchases. See OECD, "The Korean Public Procurement Service: Innovating for Effectiveness" (2016), pp.71-72

competition, such as request for quotations. The *Measures on Managing Government Procurement via Framework Agreements in State Administration of Taxation System (Trial)* provides the testimony of the practice.[88] Therefore, the proposed rules reflect the practice.

Secondly, the size of the order is a clear-cut criterion that can be determined objectively and clearly. By contrast, other methods, such as the completeness of the terms in the *Model Law*, involve uncertainty and discretion, which may present risks of improper use. Considering that procurement officials generally lack the procurement skills and the ability to make commercial judgments, the author believes that the use of a straightforward standard is more appropriate to reduce the risk of irregularities.

In small orders (below the threshold), procuring entities are still free to choose, while the second-stage competition in large orders (at and above the threshold) can ensure the offers reflect the quantity and other specific characteristics of each purchase. On the other hand, relevant mechanisms are needed to prevent any deliberate splitting of large orders into smaller ones to evade further competition. Thus, measures should be taken to prevent any deliberate division into lots. Such a requirement

[88] See *Measures on Managing Government Procurement via Framework Agreements in State Administration of Taxation System* (Trial) No.73 [2007] of the State Administration of Taxation, art. 18(3)

may be specified at the legal or policy level. Regarding specific measures, for example, post-award management and auditing, especially electronic system, can be used to monitor and detect repetitive orders for identical purchases from a single procuring entity within a period. Any further orders from this entity will be temporarily blocked and rejected if there is no reasonable justification.[89]

More importantly, framework agreements are mainly used to purchase standard goods and simple services in government procurement. The requirements can be described in detail, and the terms and conditions for purchases can be clarified as complete as possible in most cases if not all.[90]

- **More robust transparency and competition at the second stage**

As aforementioned in Chapters V and VI, the second stage of framework agreements at present is usually "below the radar", becoming a fertile ground for rent-seeking and irregularities. It

[89] The "blocking" measure is used in framework agreements in Korean public procurement. See OECD, fn. 87 *supra*, p.72

[90] Under the 2014 EU Directives, a multi-supplier framework agreement may include both direct awards and re-opening competition for awarding orders. The option between the two methods is based on objective criteria, which are defined broadly and can relate to the "quantity, value or characteristics" of the subject matter under the Recital 61 of the 2014 *Public Sector Directive*. Therefore, awarding call-offs below a specific value through direct award and above the established value through a second-stage competition is actually in line with the EU practice as well.

is therefore imperative to increase transparency and secure competition at the ordering stage. The relevant experiences of the EU and US federal procurement also suggest that more robust transparency is a way forward.[91]

To that end, two information obligations are suggested to be included in the proposed rules: (i) prior announcement of upcoming second-stage competitions, and (ii) publication of awards after orders being placed under framework agreements. It is to be recalled that, in Chinese government procurement, orders issued under a framework agreement have been required to be made public in a policy circular issued by MOF since September 2017.[92] It is advised to consolidate this requirement in the proposed regulation to make it enforceable. In the case of SOEs, they should be allowed to have greater flexibility in implementing the information obligations, on account of their procurement environment in a competitive market. For instance, they may issue grouped notices on awards made under frameworks on a periodical basis, and justified derogations should be allowed, such as for commercial confidentiality.

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[91] C. R. Yukins, "Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting", (Spring 2008) 37 *Public Contract Law Journal* 3, p.568

[92] An example of the award notice for five desktops under a framework agreement is available at http://www.zjzfcg.gov.cn/innerUsed_noticeDetails/index.html?noticeId=11 21884 (accessed July 8, 2018)

Where a second-stage competition is involved, the proposed rules also require a notice of the second-stage competition to be sent to all suppliers that are parties to the framework at the same time with the invitations to tender being sent, following the *Model Law*'s cautious approach.[93] Notification about upcoming competition is an important safeguard against the improper use. The information can help to engage the maximum number of supplier parties in participating in the second-stage competition. It also allows any non-inviting supplier to defend their right to participate where appropriate.

Where a second-stage competition is not involved, procuring entities are free to choose the supplier parties to issue orders within the original scope of frameworks. The proposed rules do not further limit the freedom of procuring entities to select suppliers for small orders. Since the contracts at the second stage are suggested being procurement contracts as above, they should be awarded based on the general award criteria under the government procurement laws: lowest price

[93] Article 62 of the *Model Law*. The 2014 *EU Public Sector Directives* in Article 33(5)(a) requires a procuring entity to invite all qualified supplier parties, whereas it is unclear what "qualified" means. This uncertainty may lead to the discretion of contracting authorities at the second stage. In the US GSA Schedules, only for orders valued exceeding the simplified acquisition threshold, contracting officers may be required to notify the ordering activities. Alternatively, they can choose not to publicly advertise but to invite certain contractors under the Schedule, as long as it receives responding offers from at least three contractors. See *FAR* 8.405-1.

or comprehensive evaluation method.[94] This arguably means random selection may not be permitted.[95]

The flexibility may lead to the risk of abuses. Such risk may be at least partially be deterred by the requirement of award notices after orders are placed. Care should also be taken to prevent large orders from being divided into smaller ones for the "freedom" to choose. Internal rules and guidance will be necessary to guide procuring entities how to properly select suppliers from the value and equal treatment perspectives.

As described in Chapter VI, Chinese SOEs in most cases use direct awards at the second stage of framework agreements, which essentially involves mechanical allocation of orders based on predetermined lots division. Specific attention should be paid to the situation where the allocated/ guaranteed quantities for a supplier party has been met, and the purchasers should not be allowed to issue additional orders from the supplier above the allocated lot. This is because the maxima for each supplier party is guaranteed and allowing discretionary additional orders could result in inadequate value/ quantity of purchases received by the rest of suppliers and could be abused for favouritism.

[94] Article 34 of the *IRGPL*.

[95] Filipon stated that awarding call-offs under framework agreements without reopening competition has received limited attention and analysed some key issues that need to be considered in these cases. See L. Ș. Filipon, fn. 59 *supra*, pp. 340-344

Furthermore, both government agencies and SOEs should maintain a documentary record of the procurement proceedings throughout the process of a framework agreement to enhance transparency and to promote accountability. The similar requirements can be found in the EU and US regime as well as under the *Model Law*.[96] The information collected provides reliable data and empirical evidence for further research. The analysis can in turn feed into developing future procurement plans and improving budgetary and assets management related to procurement in the long term. The above-proposed publication and notification can be undertaken on an electronic basis. The existing electronic infrastructure provides solid back for the new information obligations.

- **Ensure ease of use at the call-off stage**

Framework agreements should be easy to use. As the major planning and substantive procedures have been completed at the first stage, the call-off stage should be designed as a "simple, rapid, and efficient process".[97] The second stage should exempt the user entities from excessively complex decision-making;

[96] Article 25 of the *Model Law*; Article 84 of the *EU Public Sector Directive;* the *FAR* 16.505 (c)(7)
[97] See Albano and Nicholas, fn. 340 *supra,* pp. 320-322

otherwise, administrative efficiency, the core motivation of using framework agreements will be offset.[98]

On the other hand, however there is also a need to increase transparency and boost competition in call-offs, as just mentioned above, which may lead to administratively burdensome and lengthy process. The existence of overlapping choices for user agencies under the GSA Schedules in the US was criticised for making the whole system "incredibly complex".[99] Taking into consideration the above, procurement officials when establishing framework agreements should juggle the need to ensure ease of use against the risk of complex process derived from pro-competition measures at the call-off stage. Good design and effective planning are essential to achieving the right balance.

An efficient second stage may be most likely to be achieved by using the lowest price method or one involving simple quality criteria to the extent that they can be monetised, considering fact that framework agreements are mainly used to purchase standard items. As OECD states, "Simple design pays out".[100]

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[98] *Ibid*., p.321. One participant in the interview particularly highlighted this view.
[99] J. I. Schwartz, "Katrina's Lessons for Ongoing US procurement reform" 15 *P.P.L.R* (2006), p.373
[100] See Albano and Nicholas, fn. 40 *supra*, p.322; OECD, "Manual for Framework Agreements", (2014), p.30

- **Determine the price in an order**

The price in an order will be determined by applying the pricing mechanism laid down in the framework agreement. Procuring entities may and are encouraged to "bargain" before awarding call-offs for a more favourable price. However, they are not responsible for obtaining the lowest price in the market, as pinpointed in Chapter VI. The "fair and reasonable price" requirement under the US federal system may shed light on how to construe a favourable price under framework agreements. In Chinese centralised government procurement, the price of awards under framework agreements should be below the average market price, as mentioned in Chapter IV. There is a need for the competent authorities, i.e. MOF, to clarify what it means and how to determine it. Overly pursuing lowest price in the market as indicated may cause skewed incentives.

Regarding the endemic overpricing in framework agreements, it is suggested that efforts should be devoted in two main aspects to address this issue: (i) boosting competition to attract favourable offers from the suppliers, which requires good design and effective planning; and (ii) increasing transparency and strengthening oversight, especially at the second stage, to prevent the occurrence of irregularities. For instance, requiring orders placed under frameworks being made public may be an effective measure.

As explained in Chapter V, in Chinese government procurement, suppliers are usually required to lower prices or provide competitive offers when market prices fall. More stringent measures are needed to ensure the requirement is properly implemented and to make it enforceable. Thus, if the suppliers fail to adjust the price in accordance with the established terms, it may be necessary to impose penalties, such as blacklisting and temporary suspension of the transaction, cancelling the agreement, debarment from future participation of the supplier for a period.[101] These penalties may be useful to deter and punish the quiet resistance.

- **The need for more flexible rules on framework agreements by Chinese SOEs**

It has been explained when Chinese SOEs engage in framework agreements, they should be subject to appropriate procedural and oversight safeguards, due to the facts that they are controlled by the governments, that they are the primary spender of public funds and that many of them operate or dominate in the utilities sectors and provide public services. Their procurement comprises an enormous procurement market and has always been a high-risk area of corruption. Therefore,

[101] These management measures are seen in ensuring most favourable prices under framework agreements in Korea. See OECD, fn. 87 *supra*, p.73

the proposed regulation covers the entire procurement process of framework agreements by SOEs. As major planning and substantive decision making, i.e. setting up terms and conditions and selecting supplier parties, are at the first stage, SOEs are suggested to follow stringent procedural rules in concluding framework agreements.

On the other hand, however, on account of their roles as market players, additional flexibility and discretion than is offered in Chinese government procurement should be allowed for SOEs to meet their commercial needs, especially for those "commercially-oriented" SOEs that operate exclusively in competitive markets. Given the above, it is advised to adopt a principle-based approach to regulating the second stage of framework agreements by SOEs, following the EU's approach.[102]

To that end, the proposed regulation imposes a general requirement on SOEs to order within the limits of the terms and conditions laid down in the framework agreement. Flexibility

[102] As mentioned in Chapter III section 3, the new rules under the 2014 *EU Utilities Directive* are more prescriptive than the old rules adopted in 2004, mainly regarding the procedures for the conclusion of framework agreements, with the aim of increasing transparency. This change also supports the view of introducing more robust transparency requirements in frameworks. However, in general, the provisions governing the second stage of frameworks are less prescriptive than those in the general public sector under the 2014 *Public Sector Directive.* For instance, the criteria for awarding contracts on the basis of a framework agreement must be "objective and transparent". Contracting authorities in the utilities sector, therefore, still have more flexibility in call-offs under frameworks. For example, negotiations are permitted in the call-off stage in the utilities sector but not in the public sector. See Article 33 of the *EU Public Sector Directive* and Article 51 of the *EU Utilities Directive*.

and discretion may be allowed, provided it is not beyond the original scope.

The obligation imposed on SOEs to publish award notices regarding orders under framework agreements is considered an important safeguard for checking the purchaser has acted within the scope of a framework agreement and ensuring the terms of the frameworks and the procurement rules are followed. However, SOEs, as commercial entities, are different from government agencies and public institutions and they are not looking for integrity. Prompt disclosure of notice after each order is placed seems to be excessively onerous and unnecessary for SOEs, which can diminish value for money and administrative efficiency. Therefore, the periodical disclosure of grouped notices regarding orders is considered more acceptable to SOEs.[103] Such consideration also reflects the trade-off between the need for transparency and the need for efficiency in the procurement of SOEs.

[103] The idea of publishing the grouped notices of the results of contracts based on a framework agreement on a periodic basis is provided in the EU Directives. As explained in Chapter III section 3, in both the utilities and public sectors, Member States may opt not to require contract award notices (individual or grouped) for call-offs under framework agreements. However, the contract award notices are required for call-offs under dynamic purchasing systems.

3.4 Challenge Proceedings

Proposed Provision:

> A supplier that has participated in the procurement may bring a complaint against all the decisions and acts that it considers have caused losses or damages throughout the procurement proceedings of a framework agreement.

- **Challenge proceedings applicable to both stages of framework agreements**

At present, challenge proceedings in Chinese government procurement are provided under the *GPL, IRGPL* and the *Handling Complaints of the Government Procurement Suppliers*.[104] In the context of framework agreements, the challenge procedures are available at the first stage, as mentioned in Chapter V, whilst challenges against orders under frameworks are generally not allowed. This is because the conclusion of a framework agreement itself is usually considered to represent the end of the procurement process, and procurement rules would cease to apply from then on. It is suggested to extend the challenges proceedings to the second-stage of framework agreements in the proposed regulation, following the *Model Law*'s approach.[105] This is in line with the

[104] The *MOF Review Measures*, No.94 [2017]
[105] See Chapter III, section 2.

idea that framework agreements themselves are not procurement contracts, which are awarded at the second stage only, as proposed earlier.

The existing public procurement rules do not provide an *ad hoc* supper review mechanism applicable to the procurement by SOEs, as clarified in Chapter VI, and framework agreements by SOEs, which are mainly used to acquire goods and services, are not subject to either supplier review mechanism under the two procurement laws. In reality, disputes about their framework agreements procurements are more often considered as internal management issues to be addressed in private. Given the significance of an effective challenge mechanism in a procurement system, a supplier review mechanism should be provided for dispute resolution by SOEs. For example, if the SASAC promulgates ministerial rules for framework agreements by SOEs as proposed, supplier review should be part of the rules and be available at both stages of frameworks.

There are few doubts that the first stage of frameworks should be covered by the supplier challenge/ review mechanism, just like other procurement methods. The proposed regulatory rules further require subject to the supplier review, following the Model Law's approach as provided in Ch. III. This is based on a trade-off between the need for improving integrity and accountability and the need for ensuring a rapid and

straightforward ordering process. There is no denying the risk of excessive complaints, especially malicious complaints, which will cause considerable and unnecessary disruption to the procurement process, thereby undermining the overall efficiency and value for money.

However, the US experience indicates that if the second stage lacks proper supervision and enforcement, potential of abuses and misuse are highly likely. Therefore, to extend the challenge mechanism to cover both stages of framework agreements is argued to be more appropriate in China, based on the following considerations.

First, an affective oversight and enforcement mechanism is essential to ensuring compliance with the regulatory rules and enforcement of other procedural safeguards. Otherwise, the transparency safeguards imposed at the second stage, i.e. the requirements on award notices regarding call-offs and notification of the upcoming competition, may be meaningless. Secondly, subjecting the ordering process to the supplier review can discourage and deter any knowingly non-compliance at an early stage, thereby preventing framework agreements from being a “haven” to avoid normal transparency or competition. Moreover, the existence of the review mechanism at the second stage helps to gain public confidence in the overall procurement.

It is further acknowledged that the achievement of integrity may be at the cost of other objectives, particularly efficiency.

In the EU and US federal system, there is a tendency to incrementally liberalise protests and remedies against orders under framework agreements. As the relevant international experience shows, opening the gate of supplier review to the second stage tends to be a way forward.[106]

It is suggested to adopt a narrow approach to granting the standing to challenge to avoid unnecessary challenges that may unreasonably disrupt the procurement process, given the fact that multi-supplier framework agreements are the norm in China. For instance, it may be an option that a supplier has the standing to challenge only when it has actually participated in the relevant procurement process. It means that prospective suppliers, i.e. sub-contractors, and that public as well as the third parties will not be eligible to challenge any issues within frameworks. Similarly, to avoid unnecessary disruption, the policy-maker and legislature may opt to allow challenges against large orders only and small orders may be exempt, as is the case in the US federal system. Designing a supplier review

[106] For instance, in the US federal procurement, all orders against the GSA Schedules can be protested. For IDIQ contracts, protests against an order are allowed provided the order exceeds the simplified acquisition threshold, or the order is alleged to have alternated the scope of the original contract. In the EU, although procuring entities are voluntary to apply standstill period in awards made under framework agreements, they are encouraged to do so since any illegal direct awards may risk being void.

mechanism that is properly balanced between different procurement objectives in the context of framework agreements is undoubtedly an uneasy task, which deserves detailed and further discussion.

4 Summary

Framework agreements, while being widely used in Chinese government procurement and SOEs' procurement, are not covered by the current primary laws or State Council regulations on public procurement at the national level. The legal issues and improper use due to lack of regulation have undermined the benefits of this procurement arrangement. There is a need to provide formal legal rules on framework agreement that govern their use, firstly to address their legality issue, secondly to eliminate the inconsistencies of operating framework with the current procurement rules and thirdly to provide procedural safeguards to ensure their appropriate use.

To that end, a number of proposals have been set out to reform the building blocks of the regulatory framework, including the legal and institutional frameworks for and the essential contents of the regulatory rules on framework agreements. The author proposes two broad approaches to regulating framework agreements in China: an integrated/

harmonised approach (regulating all framework agreements, irrespective of the nature of procuring entities) and a hybrid approach (regulating framework agreements in government procurement and by SOEs separately). The hybrid approach is suggested to be more appropriate and practical, considering the fact that the dead-lock between different government ministries involved in regulating public procurement mainly the MOF and NDRC can hardly be broken in the short and medium term.

In Chinese government procurement, the *ad hoc* ministerial rule adopted by MOF are considered to be the most appropriate forum to consolidate the rules on frameworks. The proposed rules governing framework agreements by SOEs are preferable to be incorporated in the new ministerial rule issued by the SASAC. Proposals to improve the institutional framework that supports the regulatory framework are accordingly made.

Detailed suggestions regarding the essential contents of the regulatory rules, such as definition, condition for use, procedures, and challenge procedures, are also put forward, based on the factual challenges that arise in framework agreements in Chinese public procurement and informed by the relevant experiences from the *Model Law*, EU and US federal procurement. The author does not intend to actually draft the law but to identify the key issues that deserve consideration. Generally, the suggestions are intended to strike an appropriate

balance between various procurement objectives, especially between integrity and efficiency in the context of framework agreements. It needs to be noted that the beneficial use of this procurement instrument requires more detailed guidance, and internal rules and instruction manuals can be constructive to guide procurement officials in practice.

Furthermore, adequate capacity is a key to empowering the success of each step of the way through the procurement journey. Given the general under-professionalisation of the procurement workforce in China, there is an urgent need to build capacity in public procurement and develop a proper career ladder for public procurement professionals, thus ensuring effective use and sustainable development of framework agreements.[107]

[107] OECD has a guideline to develop a strategy for capacity building public procurement based on its experiences working with a number of countries, which may be useful for China in this respect. See "Roadmap: How to Elaborate a Procurement Capacity Strategy" (OECD, 2016)

Chapter VIII. Conclusion

To summarise so far, the thesis has examined the use of framework agreements in Chinese public procurement (in the government procurement and procurement of SOEs) and investigated the main problems and challenges that may undermine the potential benefits of this framework agreements. Informed by the relevant experiences from the UNCITRAL Model Law, the EU and US federal systems, the research has also suggested a number of options that may inform China to improve the public procurement regulatory system so as to accommodate to a more proper use of framework agreements. The chapter seeks to encapsulate the main research findings that cover all these issues.

Chapter II provides a comprehensive survey of the main features of framework agreements, which essentially are a procurement arrangement involving two stages of operational procedures. The first stage is used to set out the terms and conditions for future purchases and to select one or more suppliers to enter into a master agreement before an actual requirement materialises. At the second stage, when a specific need arises, the procuring entity is enabled to issue an order from the supplier(s) admitted to the framework agreement, following with the pre-established method and terms.

The main classifications of framework agreements are also explored in order to unravel the variables and elements of such procurement arrangement. The common variables include the singularity or plurality of the parties involved, the involvement of second-stage competition, the degree of openness to new suppliers, and whether the agreements are of binding nature (also the extent of the commitment). These variables are not mutually exclusive but interact with each other, forming various permutations of framework agreements used in practice.

As set out in Chapter 2, the primary motivation for using framework agreements is to improve administrative efficiency mainly in repeated procurements due to effective aggregation of demands. The other main incentives of using framework agreements include greater economy of scale, ensuring security of supply, greater transparency and competition for smaller purchases, effective responsiveness for urgent procurements and enhancing participation of SMEs through division into lots.

On the other hand, however, framework agreements are complicated to operate and maintain, entailing a higher level of procurement expertise and skills. Deficient planning and ineffective implementation may detract the achievement of the above benefits, making frameworks vulnerable to abuse and misuse. Therefore, procuring entities should always be aware of the risks and carefully undertake market and demand analysis

to determine whether to use a framework agreement in a given procurement, and if yes, how to structure it properly. As for regulators and policy-makers, they should make efforts, such as setting up legal rules and issuing guidance, to facilitate the appropriate use of framework agreements while mitigating the inappropriate use.

Chapter III explores how framework agreements (and similar techniques) are dealt with under three selected systems: the UNCITRAL Model Law, the EU and US federal systems. It is observed that the three systems adopt different regulatory approaches, by virtue of their disparate contexts and reflecting the different trade-offs of procurement objectives. It has been indicated that the use of framework agreements and IDIQs contracts in the EU and US is often saddled with inadequate transparency and uneven competition, mainly at the second stage. Moreover, in both systems, orders under framework agreements and IDIQ contracts are exempted from the remedy/ protest mechanisms to a varying degree. All these deficiencies create opportunities for improper use of this instrument. The experience on both sides of Atlantic indicates that the second stage of frameworks tend to be high-risk area of irregularities, which informs China on the significance and necessity to enhance transparency and impose effective oversight at the second stage. Besides, the US experience in continually fine-

tuning the procurement objectives and adjusting the rules on IDIQ contracts reflect the proper trade-offs is of great importance for countries, especially those with less-developed procurement system on the similar issue.

Regarding the *Model Law*, its provisions on framework agreements mark a high standard of transparency and competition. This, for instance, can be demonstrated by the mandatory announcement of the second-stage competitions and award notices required for call-offs under frameworks. Further, the *Model Law* allows challenges against any acts and decision throughout the procurement process. Setting such a high benchmark is intended to help the enacting States to strike a balance between integrity and efficiency.

It is of value and interest for China to draw on the international experiences and lessons, because first they provide insights into how framework agreements may present in different forms in practice. Secondly, they indicate the good practice and high-risk areas of using framework agreements. Moreover, they highlight the importance of balancing and adjusting procurement objectives "in context". Apart from the express legal rules, the EU's “bifurcated” model in having separate rules in the public and utilities sectors may inspire China to address the regulatory gap regarding the procurement of Chinese SOEs, as pinpointed in Chapter IV.

Chapter IV gives an insight into China's public procurement regulatory system and analysed the underlying inconsistencies and tensions thereof. Over the last three decades, China has made monumental achievement in establishing a modern structured public procurement system. However, it is still characterised and saddled with fragmentation, which has been the major hindrance to any reform on public procurement in China, including that regarding framework agreements.

Currently, China has two sets of laws governing public procurement: The *Tendering Law (TL)* adopted in 1999, and the *Government Procurement Law (GPL)* enacted in 2003. They are respectively implemented by a State Council Regulation, various ministerial rules and local rules. The effective coverage of the *TL* includes the majority of works projects based on tendering procedures procured by the government agencies, public institutions as well as SOEs. The *GPL* mainly governs purchases of goods and services as well as procurement of works based on non-tendering procedures by government agencies, public institutions and organisations using public funds.

The two laws co-exist uneasily with overlaps and tensions in many aspects. The scope of their coverages is mainly defined by virtue of the type of the procurement projects and the involvement of tendering procedures. As a consequence, the procurement of Chinese SOEs as a whole arguably remains a

regulatory gap. On the one hand, SOEs' procurement is excluded from the government procurement coverage, because SOEs fail to fall into the entity coverage under the *GPL*. On the other hand, although most of the works procured by SOEs are "caught" by the *TL.* Such regulation is a by-product of the *TL*'s mandatory coverage but not due to the special characteristics of SOEs. Their purchases of goods and services, where framework agreements are mainly used, are unregulated at all.

It is explained that the root cause for the duelling procurement laws is the underlying institutional tensions-the "turf battle" amongst different government ministries involved in regulating public procurement, mainly between National Development and Reform Commission (NDRC) and Ministry of Finance (MOF), the "guardians" of the *TL* and *GPL*, for the supreme leading role in regulating public procurement. The fractured administrative framework indicates that the difficulty of regulating all framework agreements in an integrated manner. The institutional deadlock further suggests that the EU approach in having separate procurement rules in public and utilities sectors is a possible option for China in addressing the regulatory gap regarding the procurement of SOEs, including that related to framework agreements.

Chapter IV has further examined the gap between the use and regulation of framework agreements in China, and,

together with the following two chapters, cast doubt on the legality of framework agreements, mainly under the government procurement system. It is explained that, on the one hand, framework agreements have been widely used in government procurement and by SOEs in reality to acquire goods and services that are commonly needed. On the other hand, however, the regulation has been far behind the practice. Until today, framework agreements are not mentioned at all by the two national laws and their State Council regulations, which have legal force nationwide, serving as the legal basis for all the other rules implementing public procurement.

In Chinese government procurement, it is contended that framework agreements lack an adequate legal basis being a separate procurement method for two reasons. Firstly, the *GPL* and its State Council regulation are silent on the legality of framework agreements. Secondly, MOF, who has the exclusive right to permit procurement methods other than those already approved by the *GPL,* has not authorised the use of frameworks as a separate procurement method, either deliberately or not.

Furthermore, the operation of frameworks often violates the existing government procurement rules in many aspects. For instance, more than one round of competition is not allowed under the current seal-based system, as a result of which framework agreements with the second-stage competition

would not be permitted. For another example, the necessary flexibility in the context of framework agreements, with particular regard to price and quantity, would not be permitted under the present requirement on the contents of solicitation documents. As a result, the use of framework agreements in Chinese government procurement can be *ultra vires*. Moreover, the numerous rules adopted by local governments and central ministries related to frameworks are generally beyond their legislative mandate and are arguably invalid. The uncertain legality and potential breaches of the relevant rules may not only hinder the beneficial use of frameworks but also jeopardise the legal certainty of the public procurement regulation.

So far as framework agreements by Chinese SOEs are concerned, the question of legality is less relevant, because they are mainly used in purchases of goods and services whereas these types of procurement lay outside of the current public procurement rules. In reality, major SOEs tend to adopt their internal rules to instruct and self-regulate the use of framework agreements, whereas these rules are largely not accessible to the public. The "invisibility" itself arguably indicates the lack of transparency regarding the procurement of SOEs.

Chapters V and VI have firstly investigated how framework agreements are operated in practice, in Chinese government procurement and by SOEs respectively, applying the same

structure in Chapter III used in considering the international practice. The chapters then move to examine the main problems and challenges that may arise, detracting from the achievement of benefits of framework agreements. The analysis is based on the official documents and literature available in the public domain, supplemented by the data obtained in the interviews.

Framework agreements, in both government procurement and procurement of SOEs, operate close to what we know as "framework agreements" under the *Model Law* and the EU system and IDIQ contracts in the US federal system. They are also mainly used to fulfil repeated purchases of standard goods and straightforward services. Multi-supplier multi-user framework agreements tend to be the norm in both areas.

On the other hand, individual differences of *modus operandi* between two areas are also identified. While open tendering is made the default method to conclude a framework agreement in government procurement, Chinese SOEs tend to adopt restrictive procedures and often use existing supplier lists as the qualification process. While government agencies and public institutions are often encouraged to use second-stage competition and other techniques in awarding call-offs, direct awards (order allocation) in accordance with the division into lots are more commonly seen in framework agreements by Chinese SOEs. The nuances can reflect the different trade-offs

made between the various procurement objectives in each area. In Chinese government procurement, although efficiency is also valued, anti-corruption/integrity tends to be more important and even the overarching objective. In contrast, Chinese SOEs are not looking for integrity but attach more importance on efficiency and value for money in procurements, including through framework agreements.

After exploring the practice, the thesis then analysed the legal uncertainty and practical problems that may be encountered in using frameworks. The lack of adequate regulation is considered to be the most important issue, which shelters framework agreements from full monitoring, auditing and supplier review, leading to misuses and abuses. This is especially the case in the procurement of SOEs, due to the large amount of money involved and the lack of accountability and integrity. The extensive incidents of corruption by senior officials and managers of major SOEs with recent years provide firm testimony for that. As SOEs are the primary receiver and spender of public funds, it is considered justifiable to ensure that their procurement, including through framework agreements, is conducted in a regulated manner. On the other hand, express rules and guidance on this arrangement may also facilitate the achievement of value for money in their use.

As far as practical operations are concerned, poor procurement planning and management (i.e. inadequate demand and market analysis), lack of transparency and competition (mainly at the second stage), and the absence of involvement of relevant stakeholders are common problems in the current use of framework agreements in both procurement areas, though to the variable extent and manifesting in different aspects. The shortage of procurement capacity is another common obstacle in China that not only negatively impact beneficial use of framework agreements but also the development of the Chinese public procurement as a whole.

In absence of adequate regulation, and given the above operational risks, framework agreements have often been improperly used, leading to overpricing, procurement frauds, and corruption (especially in procurement of SOEs). Apart from the above, some deficiency in the supporting framework, i.e. budget system and cultural elements that may derail beneficial use of framework agreements are also considered.

In light of the above problems and challenges encountered in practice, it is suggested that formal legal rules dedicated to framework agreements are necessary first to authorise their use, addressing their legality, secondly to remove the potential inconsistencies of operating frameworks with the existing rules, and thirdly to set out mandatory procedural safeguards to

encourage appropriate use while avoiding inappropriate use. Well-designed rules and adequate guidance are envisaged to help fight against corruption, enhance efficiency and achieve better value for money. The existence of the numerous rules adopted by local governments and the internal rules of SOEs related to framework agreements has arguably demonstrated the above incentives.

Chapter VIII has therefore presented proposals on how framework agreements may be regulated under the current public procurement regime in China in an effective and viable manner. Two approaches have been proposed: a harmonised/integrated approach and a hybrid approach, and their respective strengths and weakness were analysed.

An integrated approach to regulating framework agreements would be the most desirable and simplified option, under which all framework agreements conducted under the government procurement system and by SOEs in China comply with a uniform set of rules. The prerequisite for the integrated approach is a harmonised legal framework and a coordinated institutional framework for public procurement. Therefore, this approach arguably calls for the "merger"[1] of the *GPL* and *TL*, as well as their implementing regulations. It is suggested that a

[1] "Merger" is the word used by Ping Wang in P. Wang, C. Bovis and X. Tu, "A Comparative Analysis of Utilities Procurement in EU and China", component 5 of *A Report Prepared for EU-China Trade Project* (II) (August 2013), p.162

supra-ministerial agency, i.e. Public Procurement Commission, led directly by the State Council, may be necessary to set up the institutional framework. Only when the institutional framework is coordinated and consistent, such a unified legal framework can be possible.

However, it is argued that the fragmented institutional framework, due to the turf battle between different government ministries, is the most intractable challenge for any reform on public procurement and can hardly be addressed in the short or mid-term. The repeated unsuccessful attempts so far to dissolve the regulatory fortress and unify the procurement system has arguably proved such difficulty, if not an impossibility. The enactment of the *Government Procurement Law* itself, the inter-coordinated mechanism, and the issuance of the separate *Implementing Regulations on Tendering Law* and *Implementing Regulations on Government Procurement Law* all represent the failed efforts made. Regarding the current reform to set up the public resources trading platforms for unified management, as explained in Chapter VIII, it is less likely to be fruitful and sees few possibilities of dissolving the dead-lock between various central ministries. It is argued that the Chinese fractured regulatory framework for public procurement would persist, and therefore the integrated/harmonised approach to regulating all

framework agreements through unified rules appears to be impractical and unworkable in a short term.

In light of the above, an alternative hybrid approach was proposed, following the EU's model (having separate rules in the public and utilities sectors), to regulating framework agreements under government procurement and by SOEs separately. The hybrid approach is considered more down-to-earth and acceptable in the Chinese context for three main reasons. First, it is in line with the existing two-dimensional legal framework for public procurement. Secondly, it takes account of the vested interests of various government ministries, thus reducing their backlash against the reform. Last but not least, it takes into consideration the need for necessary commercial flexibility of Chinese SOEs, therefore allowing greater flexibility in their use of framework agreements.

In both regulatory areas, several options for the legislative forum to consolidate the legal rules have been discussed. In Chinese government procurement, it is suggested that the MOF, the supreme regulator of government procurement activities, should adopt a new *ad hoc* ministerial rule to provide formal legal rules governing framework agreements by government agencies, public institutions and social organisations.

As for the case of Chinese SOEs, the proposed provisions are preferably being consolidated in the new ministerial rule issued

by the State-owned Assets Supervision and Administration Commission, who is in the driving seat for leading the current SOEs reform in China. In reality, it has become increasingly active in issuing policies and instruction on the procurement of SOEs. The suggestions as to the institutional framework to support the legal framework are also proposed.

Detailed suggestions regarding the essential contents of the proposed regulatory rules, including the definition, condition for use, procedures, and challenge procedures, are also put forward. The purpose of these "sample" rules is not to establish "golden rules" or "a single recipe" to be applied but to highlight the critical issues, mainly the operational risks identified in Chapters V and VI, that need to be addressed, in structurally using framework agreements. For instance, given the general absence of procurement planning in using framework agreements in China, it is suggested to make conducting procurement planning a mandatory requirement, and the decision should be documented. On account of the endemic corruption and under-professionalisation in public procurement area, the author tilts towards integrity at present. The need for greater flexibility has also been considered in designing the rules applicable to SOEs to cater to their commercial needs.

For the effective use and implementation of the rules, a series of internal rules and guidance are particularly needed,

apart from the primary legal rules, especially in light of the lack of procurement capacity in China. It has been further suggested that substantial efforts should be devoted in improving other legal infrastructures and administrative systems to interact with and support the public procurement regulations as a whole in a holistic manner.

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