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## Analysis

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### New Rules For Supplier Bid Challenges Take Effect In China

As of September 11, 2004, new rules governing how the Chinese government handles complaints by contractors under China's nascent government procurement system went into effect. These rules, entitled Measures for Handling Complaints by Government Procurement Suppliers (Measures), strive to implement Chapter Six (Articles 51-58) of China's 2002 National Government Procurement Law dealing with "Queries and Complaints." The new Measures were issued by China's Ministry of Finance (Year 2004, Order No. 20), the designated oversight agency for government procurement under the 2002 law.

The new Measures add some important details regarding how supplier protests will be handled under the 2002 National Government Procurement Law. However, the Measures, like much of Chinese legislation and regulations, suffer from a general ambiguity that renders clear guidance problematic. It is not surprising then that the new Measures raise as many questions as they answer. There also remains a huge gap between law on the books and Chinese practice, especially where limiting the exercise of administrative power is concerned. Hence, the implementation of new purchasing procedures are mocked by some as theatric cover for traditional backroom deals, unchallengeable since bidders fear that filing a complaint spells doom for their future contracting opportunities (although cases do exist). Evaluating these systemic challenges undermining the Chinese legal system is beyond the purpose of this article. Rather, this article is solely designed to introduce the reader to some of the peculiarities of the Chinese public purchasing system, and the proposed changes in China's government supplier complaints system inaugurated by the new implementing regulation.

**Problems in Defining Scope of Chinese Government Procurement**—For suppliers interested in tapping into the Chinese public purchasing market, the first step is to understand the fragmented nature of the market and the bureaucratic rivalries at work. The 2002 National Government Procurement Law applies to the pur-

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chasing of goods, construction, and services by government organs (*zhengfu jiguan*) as well as social institutions (*shiyew danwei*) and public organizations (*tuanti zuzhi*) that use fiscal funds (*caizhengxing zijin*). In the ever-changing Chinese landscape, it is not always clear what entities qualify as social institutions or public organizations covered by the law. Similarly, the distinction between fiscal funds and other publicly-owned monies creates further confusion, especially given Chinese difficulty in centralizing its national and local budgets.

Chinese state-owned enterprises—the pillars of China's socialist economy, many which continue to benefit from state largesse and privileged market positions—are not covered by the 2002 National Government Procurement law. Their purchasing activities are regulated elsewhere, with separate regimes governing their large equipment purchases and construction activities. Health care equipment for public hospitals, entities that arguably qualify as social institutions (*shiyew danwei*), are still more likely to be purchased by local health departments under regulations not yet fully integrated with the new government procurement regime. Military related procurements in China are, not surprisingly, completely outside the coverage of the 2002 National Government Procurement Law (Article 86). Rules for military procurement may exist, but not for the eyes of the general public.

The seeming uniformity reflected in the text of the 2002 National Government Procurement Law, with its more advanced bid protest mechanism, has not yet been achieved in practice. The lesson of this fragmentation is that suppliers must be keenly aware of who is conducting the purchasing, what is being purchased, and what type of funds are being used for the purchase. Each factor may affect a supplier's choice of complaint procedures. Suppliers may in fact need to consult different regulatory regimes to decipher the challenge rules governing a particular purchase, or may be subject to two sets of regulations, as illustrated by the example below.

China's 1999 Tender and Bidding Law governs the procedures for the award of large construction contracts that affect public interest or common security (*guanxi shehui gonggong liyi, gongzhong anquan de xiangmu*) or construction projects using state-owned invested funds (*guoyou zijin touzi*), state-financed projects (*guojia rongzi de xiangmu*), or loans from foreign governments or multilateral lending agencies. Coverage of this law is at once more limited than the

2002 National Government Procurement Law, in that it applies to construction only, and also broader, in that it covers a greater number of entities engaged in construction (e.g., state-owned enterprises) and a seemingly broader category of funding sources. Generally, administrative supervision of construction activities under the 1999 Tendering and Bidding Law is carried out by the State Development and Reform Commission and its local counterparts (for project planning and approvals) and the Chinese Ministry of Construction and local construction departments (for project implementation). However, certain projects subject to the 1999 Tender and Bidding Law may alternatively be supervised by China's Ministry of Transportation/Communication, Ministry of Railroads or other ministries if within their specific zone of jurisdiction. See e.g., Measures for Tender and Bidding in the Survey, Design and Construction of Highways (Ministry of Transportation, August 21, 2001).

The 1999 Tendering and Bidding Law was driven largely by concerns relating to construction quality and safety, at the expense of issues relating to monitoring the expenditure of government monies, an obvious focus of the Ministry of Finance—the agency subsequently spearheading the drafting of the 2002 National Government Procurement Law. During the drafting process for the 2002 National Government Procurement Law, in an attempt to thwart the expansion of supervision by the Finance Ministry, officials from the State Development and Reform Commission and Ministry of Construction argued that China should exclude construction from coverage of its government procurement law; an argument that ultimately failed given its incompatibility with the international consensus that government procurement uniformly includes the purchasing of goods, construction, and services. The passage of the 2002 National Government Procurement Law thus represents, in part, a successful effort by the Finance Ministry to assert control over public construction contracting by including construction in the definition of what constitutes government procurement.

In the end, however, this proved a limited victory for the Ministry of Finance. The 2002 National Government Procurement Law actually intensified the turf battle by mandating (at Article 4) that government agencies, social institutions, and public organizations (hereinafter referred to collectively as "public agencies") should use the 1999 Tender and Bidding Law when awarding construction contracts

through public bidding. To date then, many local construction departments continue to assert jurisdiction over construction by both public agencies and state-owned enterprises. Arguably, suppliers who wish to protest the award of construction contracts by public agencies currently have the option of filing complaints with either the relevant Financial Departments or Construction Departments (or other departments depending on the nature of the project). See *Measures For Handling Complaints Related to Tender and Bidding Activities on Construction Projects*, (State Development and Reform Commission, July 6, 2004).

One way to make sense of all this confusion is to view Chinese public purchasing under the following framework: there is now a core government procurement system—governing purchasing by traditional public agencies, albeit their scope ill-defined—surrounded by a broader public procurement regime regulating a host of other purchasing activities where public monies are being used and/or the public interest implicated. It seems only direct action by the Office of the State Council (the Chinese executive) will ultimately settle the uneasy relationship between the two regulatory regimes. Until then, suppliers need to understand the overlapping systems to best determine whether, in filing its protest, the supplier should use the new Measures promulgated by the Ministry of Finance (which implement the 2002 National Government Procurement Law), or resort to regulations issued by a different Chinese government agency under a separate regulatory framework.

**Process and Timeliness**—China’s 2002 National Government Procurement Law establishes a mandatory administrative process for the filing of supplier complaints. This process begins at the level of the procuring agency or any tender agent carrying out the procurement on behalf of a procuring agency. Tender agents are enterprises especially licensed to carry out procurement procedures and may serve as a respondent in a bid protest in lieu of any end-user government agency. For ease of discussion, both procuring agencies and tender agents will be referred to collectively as “purchasing agencies.”

In the event a supplier doubts the fairness or legality of a procurement procedure, that supplier is required to first file “inquiries” with the purchasing agency “within seven working days from the date the supplier knows or should know that its rights or interests are being harmed.” Thereafter, the purchas-

ing agency has an additional seven working days from its receipt of the supplier’s inquiry to respond. If the supplier is unsatisfied by the response of the purchasing agency, or the agency fails to respond within the time required, the supplier then has an additional 15 working days within which to lodge a complaint with the “relevant supervisory agency,” (which as noted above is China’s Ministry of Finance for national level procurement activities, or the relevant Finance Departments at the provincial, municipal, or county level for local level procurements—hereinafter collectively referred to as the Finance Department). The Finance Department has 30 working days from receipt of the supplier’s complaint to issue a decision. The supplier, thereafter, retains the right to appeal the decision of the Finance Department, pursuant to China’s 1999 Administrative Reconsideration Law or China’s 1989 Administrative Litigation Law.

Once the complaining supplier has submitted his initial complaint, the Finance Department is required to make a preliminary review of the complaint within five working days to make the following negative determinations, if necessary: (1) whether the content of the complaint does not accord with the regulations thus requiring the complainant to revise and refile his complaint; (2) whether the complaint is outside the jurisdiction of the receiving Finance Department, and to transfer the complaint to the correct department, advising the complainant accordingly; or (3) whether the complaint does not meet other requirements, advising the complainant in writing that the complaint will not be accepted, and providing a basis for its refusal. The Measures are sadly silent as to what type of defect allows revision and re-filing of the complaint, as compared to those defects that will condemn that complaint to rejection. Jurisdictional defects are not fatal to the complaint, requiring instead that the relevant Finance Department transfer the complaint to the appropriate office. However, it is unclear how any delays associated with a transfer affect the duty of the appropriate Finance Department to file a timely ruling on the complaint.

If the complaint is not subject to any of the negative determinations cited above, the complaint is deemed accepted as of the original date of filing. The 30 working day period within which the Finance Department must render its decision runs from the initial date of filing, not from the date the Finance Department decides it will hear the substance of the complaint.

The complainant must file copies of the complaint sufficient in number to be distributed to the purchasing agency and any other suppliers having a relationship to the subject matter of the complaint. The Measures fail to identify who qualifies as a “supplier having a relation to the subject matter of the complaint” (*tousu shixiang youguan de gongyingshang*), so it is best to assume that, at a minimum, all suppliers participating in the procurement process should be provided a copy of the complaint, regardless of their respective chances of ultimately winning the contract. There are no provisions in the Measures on the effect of failing to notice all “related suppliers.”

The Finance Department only distributes the text of the complaint to other parties after it determines to hear the case, delivery of which must be effected within three working days from its accepting the case for substantive determination. Therefore, for any accepted case, the Finance Department must distribute the complaint within eight working days of its original filing. Thereafter, the respondent and other related parties have an additional five working days from their individual receipt of the complaint to compile and submit written support for their respective positions.

**Contents of Complaint**—The new Measures prescribe both formal and substantive conditions on an acceptable complaint, which can be found at Articles 8-10. Article 8 mandates that the written complaint contain (1) the names, addresses, and contact information for both the complainant and respondent; (2) specific allegations with factual support; (3) the status of any query and any response thereto by the purchasing agency, with documentary support; and (4) the date of the complaint. Article 9 approves the use of legal representatives in the complaint process (often, but not necessarily, a lawyer) with conditions for submitting proof of appointment and evidence regarding the scope of representation. Article 10 then adds a series of additional requirements to be satisfied by the complainant, although the provision is vague as to whether these matters must be set forth in the body of the complaint. Article 10 requires that (1) the complainant be a participating supplier in the relevant government procurement activity; (2) prior to filing its complaint, the supplier first institute a query to the purchasing agency as required by law; (3) the complaint accords with the requirements of the Measures; (4) the supplier file its complaint within the time required; (5) the complainant file its complaint with the Finance Department possessing the necessary jurisdic-

tion; (6) the Finance Department has not previously ruled upon the subject matter of the complaint; and (7) the complaint meets any additional conditions established by the Finance Department. Complaining suppliers would be wise to include separate written allegations in their complaint indicating that each of the above cited conditions has been met.

**Interested Parties, Evidence, and Hearings**—While Chinese government procurement law does not subscribe to the notion of “interested parties,” as understood in U.S. bid protest jurisprudence, the Measures provide a sense, albeit at times confused, of those parties recognized to have a stake in the outcome of a bid challenge. As noted, the complainant must demonstrate its interest by proving it was a participant in the procurement process at issue. Further, the Measures introduce the concept of “suppliers related to the subject matter of the complaint,” who are similarly entitled to a copy of the complaint with an opportunity to submit written argument. The core complaint process, however, appears limited to the complainant and the purchasing agency, since there are no provisions for intervention available to the “related suppliers.” Moreover, there is no special recognition of the interests of an original awardee as is found in U.S. bid protests.

The Measures never introduce the concept of a formal hearing (*tingzhenghui*) for the arguing of complaints, but rather awkwardly provide that the Finance Department can, if necessary, “investigate to collect evidence and [even] organize to solicit evidence from both the complainant and respondent in the presence of each other.” Thus, it is unclear whether some sort of an administrative hearing process will grow out of the new Measures. (Note that U.S. bid protest practice before the Office of the U.S. Comptroller General demonstrates that a hearing is not a prerequisite to a responsive protest system that dispenses justice and is acceptable to both contractors and the government.) It should be expected that most protest evaluations by the Finance Department will be conducted solely on the papers.

If a hearing is nevertheless convened, it will be limited to attendance by the complaining contractor and the responding purchaser only. The elusive class of “related suppliers” is not envisioned to be part of the “organized” collection of evidence, but, again, merely provides the opportunity to be heard in writing. In similar spirit, the Measures only specify sanctions for the failure of the complaining supplier or responding govern-

ment agency to cooperate in the Finance Department's investigation, and are silent on penalties for the failure of third parties to cooperate. Complaining suppliers, who do not cooperate, risk having their complaint dismissed, while non-cooperating government purchasers, who fail to provide relevant information and documentation, risk having the allegations of a supplier's complaint admitted as true. From an evidentiary standpoint, the threat against the procuring agency—that without cooperating, it will forfeit its right to contest the complaint—is compelling, since in China, the absence of respect for the judiciary, the dearth of discovery tools, and the current lack of Freedom of Information Act type legislation renders most government procurement information under the strong arm of the purchasing agency.

**Decision, Remedy, and Penalties**—The Measures provide three bases for the Finance Department to enter a decision on a supplier's complaint: (1) if the supplier withdraws his complaint, the Finance Department can terminate the process; (2) if the complaint lacks factual support, the Department can reject the complaint; or (3) if the allegations of the complaint are found to be true, then the Finance Department should deal with the case per the applicable provisions of the Measures.

The remedies provisions of the Measures are perhaps the most interesting, because they differentiate, with some confusion, between (a) cases where the solicitation documents merely suffer from a “clear slant or discrimination problem” and cause damage, or may cause damage to the complainant and other suppliers; and (b) those cases where the result of the procurement process and corresponding award result from interference or illegal activities. These remedial measures, contained in Articles 18 and 19, respectively, read initially as a distinction between pre-award and post-award disputes, but this distinction gets blurred when reviewing the remedies made available under each circumstance. Rather, it appears that the Measures are differentiating between innocent, yet incompetent, drafting of solicitation documents (where the intent to affirmatively undermine competition policy is absent), and volitional acts by parties or individuals that negatively impact on contract award and impair the rights of honest suppliers. Either case gives rise to relief for the complaining supplier, but the remedies differ.

When the investigation by the Finance Department uncovers only that the tender documents are

slanted or discriminatory, the following rulings may be made: (1) when the procurement process is not yet completed, order the revision of the solicitation documents, and restart the solicitation according to the revised solicitation documents; (2) if the procurement procedure is already concluded but the procurement contract has not yet been signed, then determine the process to be illegal and order resolicitation; or (3) if the procurement process is already completed and the procurement contract is already signed, then determine the process illegal, and order the respondent to bear corresponding liability to compensate the supplier according to relevant legal stipulations. At present, there are no “relevant legal stipulations” that indicate whether an aggrieved supplier who wins its protest is limited to collecting merely bid preparation/protest costs or will be entitled to greater compensation such as contract expectation damages.

The first remedies provision above (Article 18) reflects something greater than just a pre-award protest, because under item three, a successful protest is not grounds to invalidate an already signed procurement contract, but only grounds for an award of damages. (If there is a signed contract already, the protest is obviously post-award.) Compare this to the second remedies provision described below (Article 19), which allows for invalidation of signed, but not yet performed contracts.

When the investigation by the Finance Department demonstrates interference in the procurement process or illegal activities, then the remedies available are (1) if the procurement contract is not yet signed, then determine, based on the circumstances, whether the whole procurement process or just part thereof is illegal, and order resolicitation; (2) if the procurement contract is already signed, but not yet performed, then cancel the contract and order resolicitation; or (3) if the procurement contract is already performed, determine that the procurement activity is illegal, and order all those responsible to compensate for the damages to the procuring agency or the complaining supplier. Again, the damage calculation remains woefully indeterminate.

The remedy provisions reflect a policy that procurement contracts will only be cancelled if they result from illegal activities by individuals associated with the process, and only if the contracts have not yet been performed. (The impact of nominal or partial performance by an original awardee is not differentiated.) In cases where the contract performance has

already commenced, China is opting to compensate contractors solely with money damages, although the sufficiency of these damages remains suspect.

The Finance Department is required to issue a signed written decision, which shall include the following: the names and address of the complainant and respondent; the appointment of representatives, including each representative's name, profession, address, and contact information; the specific contents of the decision, including factual support and legal bases; advice to the complainant of his rights to apply for administrative reconsideration or file for administrative litigation; and the date of the decision. Importantly, the Finance Department must provide written notice of the result of its handling of the complaint to all interested parties, and must publicize the result in a medium designated by Finance Departments at the provincial level or above. Indications are, however, that the Finance Department need only publicize the decision (e.g. sustaining or denying the protest), not the full written adjudication. China's penchant for maintaining all government information as internal, combined with its civil law tradition of not recognizing case precedents, bodes ill for the development of a body of case decisions, which could ultimately provide binding guidance to understanding the application of China's government procurement law and regulations.

**Stay of Procurement Proceedings**—Like the National Government Procurement Law, the new Measures confirm that the Finance Department has the discretion to temporarily suspend the procurement process, but for no longer than 30 days. There is no automatic stay triggered by the filing of a complaint, only a stay that may be affirmatively ordered by the Finance Department while it considers the case. No standards for applying a stay are set, leaving full discretion to the Finance Department. Any stay order takes effect only when in the purchasing agency's hand, creating an incentive for the purchaser to quickly render an award, and institute performance of the procurement contract, as to undermine a complainant's ability to later overturn the contract award.

There is no express prohibition against the contractor petitioning for a stay in its written complaint, but the 2002 Government Procurement Law and subsequent Measures are written to suggest the stay is a matter for the Finance Department, not the parties. When eventually notified of a stay order, the Measures admonish the purchasing agency to immediately cease the relevant procurement activity and not proceed

again until the 30 day stay period expires, or when the Finance Department otherwise indicates that the agency may resume its purchase, whichever is shorter.

**Protecting Supplier Information**—The 2002 National Government Procurement law recognizes the need to protect a supplier's confidential information and trade secrets, but its mechanisms to prevent illegal disclosure are basically non-existent. The Measures similarly miss a crucial opportunity to enact specific procedures for ensuring the confidentiality of supplier information by merely stating: "As to individual private matters and business secrets learned during the process of handling a complaint, the Finance Department and other persons with knowledge must bear a duty to maintain secrets." This bare policy assertion offers little comfort to a government contractor operating in a country known for its counterfeiting prowess.

**Administrative Sanctions and Other Liability**—Chinese statutes often reflect the penchant to include provisions for administrative and criminal penalties, no matter the subject of the legislation or regulation. The Measures are no exception and encourage the Finance Department to issue penalties against anyone (purchasing personnel, evaluators, suppliers) found, by virtue of the Finance Department's investigation of complaints, to have engaged in illegal activity. In cases where the appropriate penalty is beyond the power of the Finance Department to issue, the Finance Department is instructed to transfer the matter to departments with the requisite authority. Debarment awaits those suppliers that file three or more frivolous complaints within a year, or fabricate facts or provide forged documents in the complaint process. Purchasers that damage third parties should be ready to bear liability, and those Finance Department personnel handling supplier complaints should receive administrative punishment in instances where they misuse their authority, are derelict in their duties, or engage in self-dealing. Criminal liability should also attach to such personnel when appropriate. The Measures offer no guidelines (other than supplier blacklisting) for the specific punishments that await those who run afoul of its provisions.

**Party at Fault Pays Costs**—While the Finance Department is prohibited from taking fees to handle complaints, the party found to be at fault, (which may in some cases be both parties), is responsible for paying any calculable costs associated with the procedure. It is not clear whether this is a loser pays rule or something different, but a similar provision was

contained in earlier drafts of the 2002 Government Procurement Law, but later omitted from the final text. It may reflect more of an administrative concern as to how to fund the complaint process, than a policy of sanctioning the unsuccessful party. Nevertheless, in a country where “taking on city hall” remains fraught with risk and the prospects of succeeding against the Chinese government in litigation uncertain at best, the chilling effect of this type of rule on suppliers already cautious about filing a complaint should not be underestimated.

**Conclusion**—Hope remains that the new Measures for Handling Complaints by Government Procurement Suppliers reflect one more step in the Chinese journey to establish a government procurement system free of corruption and local protectionism, where all suppliers may compete equally. If contractors in the Chinese market prove brave enough to challenge government contracting decisions, and the Finance Department treats all complaints thoroughly and fairly, we might just witness such a marvelous result.



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