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Geo Quinot, *Innovation, State Contracting and Public Procurement Law*
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INNOVATION, STATE CONTRACTING AND PUBLIC PROCUREMENT LAW

GEO QUINOT*

There seems to be strong evidence and growing consensus that public procurement can be a significant factor in supporting broad-based innovation, which can be a promising tool for states to support innovation. The sheer volume of public procurement and the possibility to tailor that significant buying power towards innovative outcomes results in a powerful demand-side measure in support of innovation, a mechanism that any economy that is serious about innovation cannot ignore. However, from a regulatory point of view, there are numerous questions that will have to be carefully considered in order to calibrate a procurement system to achieve maximum innovation policy objectives. In some respects, these are fairly fundamental questions about how we conceptualise the procurement function in law and how we subsequently design the institutional framework within which this function operates. This contribution explores the linkages between public procurement and innovation and then turns to the regulatory frameworks governing public procurement to assess the questions that must be addressed if public procurement is to serve as a vehicle in support of innovation. Particular attention is given to international regimes of procurement regulation such as the WTO's Government Procurement Agreement as paradigmatic regulatory frameworks. Three main areas of concern are investigated under the regulatory frameworks, namely, risk management rules, the transactional nature of public procurement and public procurement as a policy tool.

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I. INTRODUCTION

Innovation has become a key ingredient in economic development globally. Developed economies pursue innovation *inter alia* as a means to maintain competitiveness, while innovation is an important catch-up mechanism for developing economies. This is hardly surprising in light of the rise of the knowledge (based) economy which is based on “the production, distribution and use of knowledge and information”.¹ Innovation is an important element of this knowledge process. High-technology industries as well as research institutions, both important drivers of innovation, play essential roles in the knowledge (based) economy.²

The state has long been involved in supporting innovation. As examples, one can think of the state support for public universities and other research entities facilitating innovation. Research grants and tax incentives for innovation are also common phenomena. In recent years, one increasingly finds a government department or ministry expressly focusing, amongst others, on innovation, often in combination with portfolios such as science and technology³ or business development.⁴ There is thus nothing new in the notion of state support for innovation.

¹ See Organisation for Economic Cooperation and Development, *The Knowledge-Based Economy* 7 (1996), available at <http://www.oecd.org/sti/sci-tech/1913021.pdf>.

² *Id.* at 7, 9.

³ *E.g.*, the Danish Ministry of Science, Technology and Innovation, the Brazilian Ministry of Science, Technology and Innovation and the Malaysian Ministry of Science, Technology and Innovations.

⁴ *E.g.*, the United Kingdom Department for Business, Innovation & Skills, the Irish Department of Jobs, Enterprise and Innovation and the New Zealand Ministry of Business, Innovation & Employment.

What is fairly new in recent years is an increasing focus on the role of public procurement as an instrument to support innovation. There is now increasing focus and emphasis on the interaction between the state's role as a market participant and innovation.⁵

Again, the notion of using market mechanisms as levers to support innovation is not new. Private companies have long been investing in research and development as a means to stay current and competitive in the market.⁶ What is new in this area is the idea that the state should deliberately align its market activities to fashion a demand-side measure in support of innovation. Thus, by utilising its power as a buyer, the state can *solicit* innovation and *support* its commercialisation, two steps that can be considered as critical in the support of an innovation agenda.

This idea has gathered significant traction over the last few years.⁷ Especially in policy circles, there is now much talk about public procurement in support of innovation. For example, in the European Union, there have been a number of policy documents, reports etc. in recent years focusing on procurement and innovation and advocating deliberate attempts to strengthen the link between the two.⁸ A European Commission Expert Group Report in 2005 stated in its opening

⁵ Elvira Uyarra & Kieron Flanagan, *Understanding the Innovation Impacts of Public Procurement*, 18(1) EUR. PLAN. STUD. 123-24 (2010) [hereinafter Uyarra & Flanagan].

⁶ See Organisation for Economic Cooperation and Development, *Moving up the Value Chain: Staying Competitive in the Global Economy* 80 (2007), available at <http://www.oecd.org/sti/ind/38558080.pdf>; Alix Partners, *When the Chips are Down: The Need for Greater R&D Efficiency in the Semiconductor Industry* (Jan. 2013), available at <http://www.alixpartners.com/en/Publications/AllArticles/tabid/635/articleType/ArticleView/articleId/514/When-the-Chips-are-Down.aspx#sthash.SSGif3Og.dpbs>; Johan Hombert & Adrien Matray, *Can Innovation Help U.S. Manufacturing Firms Escape Import Competition from China?*, HEC Paris Research Paper No. FIN-2015-1075 (May 30, 2015), available at <http://ssrn.com/abstract=2542495>.

⁷ Uyarra & Flanagan, *supra* note 5.

⁸ See, e.g., *Creating an Innovative Europe: Report of the Independent Expert Group on R&D and Innovation appointed following the Hampton Court Summit and chaired by Mr. Esko Aho*, at 6, 23, EUR 22005 (Jan. 20, 2006); *A Lead Market Initiative for Europe*, at 5, 7, COM (2007) 860 final (Dec. 21, 2007); *Public Procurement as a Driver of Innovation in SMEs and Public Services*, (2014), available

at <http://ec.europa.eu/DocsRoom/documents/7441/attachments/1/translations/en/renditions/native> [hereinafter *Public Procurement as a Driver of Innovation in SMEs and Public Services*]; *Innovation and Public Procurement, Review of Issues at Stake – Study for the European Commission* (No ENTR/03/24), Fraunhofer Institute for Systems & Innovation Research (Dec. 2005) [hereinafter *Innovation and Public Procurement*]; Uyarra & Flanagan, *supra* note 5; Luke Butler, *Innovation in Public Procurement: Towards the “Innovation Union”*, in FRANCOIS LICHÈRE ET AL., MODERNISING PUBLIC PROCUREMENT: THE NEW DIRECTIVE 337 (2014) [hereinafter Butler].

See

line that “Europe can drive forward research and innovation by harnessing its large expenditure on civil public procurement”.⁹ The United Kingdom House of Lords has issued a comprehensive report on public procurement as a tool to stimulate innovation in which it was stated that the “magnitude of [public procurement] expenditure provides enormous potential to influence the development of innovative solutions, to improve delivery of public policy and services and to encourage economic growth”.¹⁰ The 2013 *Annual Statistical Report on United Nations Procurement* was accompanied by a supplement focusing exclusively on public procurement and innovation in which UN Secretary-General Ban Ki-moon stated:

“Innovative procurement offers tremendous opportunities to use government buying power to shape the world around us for a better tomorrow. Through investment in new technology and research, the promotion of domestic manufacturing, increased transparency and accountability in public fund management, and support for small and medium-sized enterprises, procurement systems can help develop national capacity and attain sustainable development goals. As this report shows, innovation and procurement are viable, tested and proven policy options to achieve sustainable growth in the developed world and, increasingly, in the developing world as well.”¹¹

In 2009, an OECD Workshop on Demand-Led Innovation Policies emphasised the importance of public procurement as a policy tool to support innovation and stated as a key finding of the workshop that “governments need to align technology-push instruments like grants and incentives for R&D with demand-pull policy instruments such as public procurement and regulations”.¹² The workshop contributed to the OECD *Innovation Strategy* published in 2010, which stated under

http://ec.europa.eu/information_society/newsroom/cf/dae/itemdetail.cfm?item_id=16605, for a list of EU policy initiatives on innovation procurement [hereinafter MODERNISING PUBLIC PROCUREMENT: THE NEW DIRECTIVE].

⁹ *Public Procurement for Research and Innovation: Expert Group Report, Developing procurement practices favourable to R&D and innovation*, at 5, EUR 21793 (Sept., 2005) [hereinafter *Public Procurement for Research and Innovation*].

¹⁰ HOUSE OF LORDS SCIENCE AND TECHNOLOGY COMMITTEE, PUBLIC PROCUREMENT AS A TOOL TO STIMULATE INNOVATION, 2010-12, HL Paper 148, at 5 (U.K.).

¹¹ UNOPS, SUPPLEMENT TO THE 2013 ANNUAL STATISTICAL REPORT ON UNITED NATIONS PROCUREMENT: PROCUREMENT AND INNOVATION 1 (2014) [hereinafter UNOPS SUPPLEMENT].

¹² OECD Workshop on Demand-Led Innovation Policies, 14-15 Sept. 2009, <http://www.oecd.org/science/inno/oecdworkshopondemand-ledinnovationpolicies14-15september2009.htm>.

one of its policy principles that “[g]overnment procurement policies should strengthen their capacity to deliver innovative solutions to public needs that are in line with good governance, transparency and accountability.”¹³ In a number of OECD reviews of innovation policy, support for public procurement of innovation is also expressed along with calls for increased use of procurement as an innovation policy instrument.¹⁴ The pursuit of public procurement of innovation is for the most part not aimed at innovation *per se*, but rather at an underlying objective such as economic development or in support of social justice objectives.¹⁵ It is for this reason that debates about public procurement of innovation are quite often closely linked to local preferences and/or support for (local) SMEs in procurement, as is evident from many of the policy initiatives highlighted above which engage with public procurement of innovation and local economic development side-by-side. Thus, the UK House of Lords report on procurement and innovation noted above, for example, outlines in some detail the steps that the UK government has taken over a number of years to support small business in the UK and the links to procurement of innovation.¹⁶ But procurement of innovation does not necessarily have to be linked to local preferences in procurement. A government may, for example, pursue public procurement of innovation in order to solicit new ways of rendering public services. It is however, fair to claim that public procurement of innovation is largely linked to developmental agendas.

The recognition of the potential of the state’s contractual power to further innovation and the realisation of that potential are of course two different things. In this contribution, I want to explore the ways in which the law can influence the latter, that is, the realisation of the potential of public procurement to support innovation. I focus specifically on the influence of supra-national regulatory instruments such as the WTO’s Government Procurement Agreement (“the GPA”) in this respect.

¹³ THE OECD INNOVATION STRATEGY: GETTING A HEAD START ON TOMORROW 118 (2010).

¹⁴ OECD REVIEWS OF INNOVATION POLICY: KOREA 9 (2009); OECD REVIEWS OF INNOVATION POLICY: MEXICO 29 (2009); OECD REVIEWS OF INNOVATION POLICY: SWEDEN 248-50 (2012) [hereinafter OECD SWEDEN]; OECD REVIEWS OF INNOVATION POLICY: FRANCE 207 (2014).

¹⁵ See Rainer Kattel & Veiko Lember, *Public Procurement as an Industrial Policy Tool: An Option for Developing Countries?*, 10(3) J. PUB. PROCUREMENT 368, 375 (2010); *Public Procurement for Research and Innovation*, *supra* note 9, at 3; *Public Procurement as a Driver of Innovation in SMEs and Public Services*, *supra* note 8, at 5; James Binks, *Using Public Procurement to Drive Skills and Innovation: A Report for the Department of Trade & Industry*, Local Futures Group (Mar. 2006).

¹⁶ *Supra* note 10, at 32-35.

II. THE LINK BETWEEN PUBLIC PROCUREMENT AND INNOVATION

There are distinct areas of public procurement where the linkages between procurement and innovation are more readily apparent or at least more established.¹⁷

One example is defence procurement. In this area innovation is quite often driven by procurement processes. Put differently, there is a long-standing connection between innovation in defence equipment and public procurement.¹⁸ Governments invest heavily in the development of new defence equipment and a significant part of such development occurs in the private sector, with the support of public money. Public procurement is one method through which public funds are utilised to support such development on the basis of a government committing to procure the equipment developed by a private sector defence contractor. This is hardly surprising given the particular nature of the defence market, which is to a significant extent a public one. What is noteworthy about innovation and defence procurement is the spill-over effect of innovation facilitated in the defence market, *inter alia* through procurement into the civilian market; the internet being a celebrated example.

Another example of the obvious connection between innovation and public procurement is in the area of technology procurement.¹⁹ Again here it is not surprising, given the nature of the subject matter, that procurement can generate significant technological developments. The potential size of demand that can be generated through public procurement, can especially justify the significant costs in technology innovation.

What is less obvious than the examples noted above is whether there is a more general link between all public procurement and innovation. Is there a role that mundane, everyday public procurement can play in support of innovation? Can the procurement of everyday, ostensibly standard, goods and services, what Uyarra & Flanagan refer to as “bread and butter procurement”,²⁰ also support innovation? In order to grapple with these questions, one must *inter alia* interrogate general public procurement law and ask to what extent the legal rules governing everyday

¹⁷ OECD SWEDEN, *supra* note 14, at 251.

¹⁸ See Keith Hartley, *The Economics of Military Outsourcing*, 11 PUB. PROCUREMENT L. REV. 287 (2002); Keith Hartley, *Competition in Defence Contracting in the United Kingdom*, 1 PUB. PROCUREMENT L. REV. 440 (1992); Bernard Udis, *Weapons Procurement in the United States*, 1 PUB. PROCUREMENT L. REV. 455 (1992).

¹⁹ Uyarra & Flanagan, *supra* note 5, at 124; *Innovation and Public Procurement*, *supra* note 8, at 7, 10.

²⁰ Uyarra & Flanagan, *supra* note 5.

procurement practices realise or undermine the potential of state contracting to support innovation.

The notion of innovation procurement can cover a range of different meanings and a number of definitions emerge from the literature and policy statements. In his recent book on public procurement and innovation, Max Rolfstam defines public procurement of innovation simply “as *purchasing activities carried out by public agencies that lead to innovation*”.²¹ He points out that this broad definition includes activities both before and after the formal call for tenders and does not restrict the concept to a single instance of tendering. Viewed as a process, public procurement of innovation may thus include several tender calls that are linked to constitute a single process of public procurement of innovation.

One distinguishing feature in the various definitions of public procurement of innovation is whether the innovation is itself the subject matter of the procurement or not. On the one hand public procurement of innovation can simply mean that the state buys research and development leading to innovation, which is not that different from a research grant. The state, in effect, pays for research and development services. It is the innovation itself that is the subject matter of procurement. This understanding of procurement of innovation is closely related to the concept of “pre-commercial procurement” (PCP), which involves support through procurement for innovation without necessarily resulting in a commercialised product or service. The supply of a product or service generated through innovation does not form a part of the procurement. As Edquist & Zabala-Iturriagoitia have pointed out, this concept, while closely related to procurement of innovation, should in fact be distinguished from it since PCP is in effect a supply-side mechanism in support of innovation and not a demand-side mechanism in the way that procurement of innovation is understood to be.²²

Alternatively, the state may seek to buy a product or service that is innovative, that is something that did not exist (at least in that form) prior to the procurement. The innovation itself is thus not the subject matter of the procurement, but the innovative product or service is. The innovation is the by-product of the procurement. It is this second understanding that I am mostly interested in in this contribution.

²¹ MAX ROLFSTAM, PUBLIC PROCUREMENT AND INNOVATION: THE ROLE OF INSTITUTIONS 12 (2013) [hereinafter ROLFSTAM].

²² Charles Edquist & Jon Mikel Zabala-Iturriagoitia, *Public Procurement for Innovation as Mission-Oriented Innovation Policy*, 41(10) RES. POL'Y 1757, 1759 (2012).

The difference between these understandings is important, for example, in considering which entities will be legally mandated to adopt which approach. It is unlikely that all contracting authorities will have the mandate to procure pure innovation, including the budget to do so. It is significantly more likely to find a mandate for the pursuit of innovative products or services within the public service area of the particular entity. But focusing too heavily on the existing, identified needs of the public authority may again undermine procurement for innovation, in that it may not leave sufficient space for different ways of doing things to emerge, i.e. for the innovation to also shape the need. Procurement for innovation thus largely also calls for innovation in procurement, that is, finding ways to conduct procurement that will achieve a balance between servicing the public function of the contracting authority and supporting innovation.

It is therefore useful to think of procurement as the bridge between the innovator and the public service. It could be a function of procurement to actively bring these two nodes together without focusing on one aspect rather than the other. If it is all about the public service, then a predefined notion of what is required will undermine any significant innovation. If it is all about innovation, then the very purpose of procurement, which is to service a public function, will be lost and with it a key goal of procurement, namely value for money. One core challenge in realising the potential of procurement for innovation is that procurement tends to be reactive in its very nature²³ – it is the function of supplying the goods/services/works already identified by the contracting authority in support of a particular public programme. Procurement in the public sector is thus often conceptualised as a “support service”: it serves in support of programmatic initiatives developed elsewhere. This view problematises a conceptualisation of procurement as the focal space for innovation.

Procurement regulation largely reflects this trend: it focuses heavily on the call for tenders, the adjudication and award of the tender, and to a lesser extent the contract management following that award, which is often simply left to pure commercial law. While the demand management side is something that is considered in procurement law, formal procurement rules usually apply only in a light and cursory manner in this phase. One example is rules on pre-procurement market engagement that have emerged only fairly recently.²⁴ Typically, the demand

²³ Colin Cram, *Innovation through Procurement: Another Magic Formula?* PROCUREMENT INSIGHTS EU EDITION (Jan. 26, 2015), available at <https://procurementinsightseu.wordpress.com/2015/01/26/innovation-through-procurement-another-magic-formula-by-colin-cram/>.

²⁴ The concept of Pre-Commercial Procurement (PCP) is a good example of a fairly recent development in regulating processes preceding the actual procurement of goods or services. See *Compilation of Results of the EC Survey on the Status of Implementation of Pre-*

management side is not something that procurement lawyers are particularly interested in since it is not an area where legal remedies typically apply. However, if we accept that procurement can support innovation, then we need to ask a number of foundational questions about how we approach procurement regulation. Put differently, what impact does procurement regulation have on the role of procurement for innovation?

III. PUBLIC PROCUREMENT LAW AND INNOVATION

A number of scholars have presented evidence to show that current public procurement regulation does not necessarily prohibit procurement of innovation initiatives.²⁵ That is to say, typical current public procurement regulatory regimes do not proscribe public procurement of innovation. However, many studies have indicated that public procurement regulation typically also does not actively promote public procurement of innovation and that the law may indeed pose a number of challenges in realising the potential of state contracting in support of innovation.²⁶

Commercial Procurement Across Europe (Apr. 2011), available at <http://cordis.europa.eu/fp7/ict/pcp/pcp-survey.pdf>; ROLFSTAM, *supra* note 21, at 10–11; Aure Adell et. al., *Existing Approaches to Encourage Innovation through Procurement*, at 8–13, SMART SPP (2009), available at http://www.smart-spp.eu/fileadmin/template/projects/smart_spp/files/SMART_SPP_D2.2_ExistingProcurementApproaches.pdf.

²⁵ ROLFSTAM, *supra* note 21, at 52; Nicholas S. Vonortas, *Innovation and Public Procurement in the United States*, in CHARLES EDQUIST ET AL., PUBLIC PROCUREMENT FOR INNOVATION 147 (2015); Tobias Indén & Karsten Naundrup Olesen, *Legal Aspects of Public Private Innovation*, 7(4) EUR. PUB. PRIVATE PARTNERSHIP L. REV. 258 (2012); Pheobe Bolton, *Public Procurement of Innovation: An Option for South Africa*, in UNOPS SUPPLEMENT, *supra* note 11, at 38; Victor Mourao & Rodrigo Cantu, *Innovation and Public Procurement in Brazil*, in UNOPS SUPPLEMENT, *supra* note 11, at 49; Aleksandrs Cepilovs, *Public Procurement for Innovation in Small States: The case of Latvia*, 16, available at https://www.academia.edu/3310433/Public_procurement_for_innovation_in_small_state_s_The_case_of_Latvia.

²⁶ The OECD report on innovation policy review in Sweden for example states that “public procurement has played a significant role in the history of a number of Sweden's largest and most innovative companies. However, contemporary legal frameworks, including state aid rules, now preclude many practices that were previously employed” and that “[s]ince Sweden's accession to the European Union, and with it the requirement to abide by Europe-wide Public Procurement Directives and Treaty Principles, the scope for continuing historically strategic alliances between business and the public sector, cemented through procurement, has been reduced.” OECD SWEDEN, *supra* note 14, at 32, 249.

Developments in EU procurement law provide a good example of the challenges experienced in this regard. The new 2014 EU Directives on public procurement were, to a significant extent, put forward on the basis of renewed focus on procurement of innovation and the sense that the previous (2004) Directives were outdated in this regard.²⁷ Moving from virtually no mention of innovation in the 2004 Directives, the new 2014 Directives provide expressly for procurement of innovation, including through the adoption of a new procurement procedure aimed specifically at procurement of innovation, namely the innovation partnership.²⁸ Despite this overt and dedicated turn to incorporate public procurement of innovation in the regulatory regime, a number of scholars have questioned whether the new law will be useful in promoting innovation.²⁹ In his detailed treatment of the new provisions of the 2014 EU Directive aimed at facilitating innovation, Butler, for example, states that it “is fundamentally questioned whether Directive 2014/24/EU is adequately calibrated to act as an effective instrument to facilitate the achievement of innovation”.³⁰

In what follows, I explore a number of challenges for the use of state contracting in support of innovation in what may be viewed as paradigmatic public procurement regulatory approaches. This is a “high altitude” view that does not focus on any particular legal system, but attempts to raise regulatory questions about the use of public procurement in support of innovation in a generalised manner. In forming this view, international instruments in public procurement regulation, like the GPA, are extremely useful as they are not tied to a particular legal system. As Max Rolfstam has thus indicated in his extensive work on public procurement of innovation, the GPA is, along with the UNCITRAL Model Law

²⁷ Dacian C. Dragos & Bogdana Neamtu, *Sustainable public procurement in the EU: Experience and Prospects*, in MODERNISING PUBLIC PROCUREMENT: THE NEW DIRECTIVE, *supra* note 8, at 301, 313 [hereinafter Dragos & Neamtu].

²⁸ Butler, *supra* note 8, at 337–38; Pedro Telles & Luke R.A. Butler, *Public Procurement Award Procedures in Directive 2014/24/EU*, in MODERNISING PUBLIC PROCUREMENT: THE NEW DIRECTIVE, *supra* note 8, at 160, 161 [hereinafter Telles & Butler]; Miguel Ángel Bernal Blay, *The Strategic Use of Public Procurement in Support of Innovation*, 9(1) EUR. PUB. PRIVATE PARTNERSHIP L. REV. 3 (2014).

²⁹ Telles & Butler, *supra* note 28, at 178–80; Marta Andrecka, *Innovation Partnership in the New Public Procurement Regime - a shift of focus from procedural to contractual issues?* 24 PUB. PROCUREMENT L. REV. 48 (2015). See Albert Sánchez Graells, *Innovation Partnerships under Regulation 31 Public Contracts Regulations 2015* (Apr. 9, 2015), available at <http://howtocrackanut.blogspot.com/2015/04/innovation-partnerships-under-reg-31.html>, for similar criticism in respect of the direct transposition of this new procedure into UK law by means of the Public Contracts Regulations 2015; Pedro Telles, *Public Contracts Regulations 2015 - Regulation 31* (Apr. 9, 2015), available at <http://www.telles.eu/blog/2015/4/9/public-contracts-regulations-2015-regulation-31>.

³⁰ Butler, *supra* note 8, at 338.

on Public Procurement, at the highest “institutional level relevant for analysis of public procurement of innovation”.³¹

A. Risk management rules

The first issue is the due diligence or risk management requirements one typically finds in procurement adjudication and that is quite often premised on particular rules about a qualifying bid.

The issue here is that these requirements can have an impact on whether or how easily start-ups can compete in a tender. Such requirements may include financial statements, tax compliance information, insurance guarantees and past performance records. The GPA for example provides for such requirements in its article VIII on conditions for participation, where it allows parties to include conditions “that are essential to ensure that a supplier has the legal and financial capacities and the commercial and technical abilities to undertake the relevant procurement”.³² The article furthermore expressly allows for prior experience to be set as a condition for participation³³ and for exclusions based on tax-compliance information.³⁴

These requirements serve the important purpose of minimizing the risk of contracting with a supplier that will not deliver and/or to ensure that performance will be of the required standards. However, start-ups may be at a distinct disadvantage in this respect, in that they may not be able to provide all of these safeguards or at least not to the same level as established suppliers.³⁵ At the same time we know that start-ups play a crucial role in innovation.³⁶ For that, one has hardly to think beyond the early years of Silicon Valley enterprises, most of which are today the giants of the ICT sector and emerged from small start-up enterprises pushing highly innovative technologies. Support for start-up suppliers should thus,

³¹ Max Rolfstam, *An Institutional Approach to Research on Public Procurement of Innovation*, 25(3) EUR. J. SOC. SCI. RES. 303, 312 (2012); ROLFSTAM, *supra* note 21, at 42.

³² Revised Agreement on Government Procurement, Annex to the Protocol Amending the Agreement on Government Procurement, art. VIII.1, adopted on Mar. 30, 2012 (GPA/113) [hereinafter GPA] (all references to the GPA are to the revised text).

³³ GPA, Article VIII.2.(a).

³⁴ GPA, Article VIII.4.(f).

³⁵ See UNOPS SETTLEMENT, *supra* note 11, at 114.

³⁶ *Supra* note 13, at 12; Vivek Wadhwa, *The Importance of Start-ups: Which Are We Going to Bet On?* (Aug. 23, 2010), available at http://www.investorsinsight.com/blogs/john_mauldins_outside_the_box/archive/2010/08/23/the-importance-of-start-ups.aspx; G.M. PETER SWANN, THE ECONOMICS OF INNOVATION: AN INTRODUCTION 138-39 (2009).

be an important strategy in procurement for innovation. This can be viewed as at least part of the reason why there is such a strong link between public procurement of innovation and support for SME participation in public procurement in the literature and policy debates.

While one can thus readily see the legitimate rationale for the inclusion of these risk management rules in public procurement regulatory systems, they may pose a significant challenge to increasing the inclusion of start-up suppliers in public procurements. A key question for any procurement system that is intent on leveraging procurement for innovation should thus be what the best ways are to regulate the risk of non- or poor performance, taking into account the potential impact of such risk management rules on innovation. It may be that the stock approach of using bid qualification rules pulls the scales too heavily in favour of the risk management objectives vis-à-vis the pursuit of innovation.

The problem with these risk management rules becomes aggravated since these requirements are mostly not captured in award criteria, but in qualification or selection criteria. That is to say, the procurement rules cast such requirements as selection criteria, not as award criteria. As the examples from the GPA above illustrate, these rules are typically framed as conditions for participation. When these rules are formulated as qualification or selection criteria suppliers may simply be excluded from the competition even before their proposals have been evaluated against that of their competitors. If such conditions were framed as award criteria, they would allow comparison between suppliers in the award phase of adjudication. The framing of risk management conditions as selection or qualification criteria thus undermines the possibility for the contracting authority to properly weigh up the risk of contracting with the start-up offering an innovative solution against the potential benefits of procuring that innovation. If the risk management conditions were framed as award criteria, the contracting authority would be able to conduct this type of weighing up. This would allow for a proper consideration of the relative values of the innovation and the risk and a consequent rational contracting decision in terms of both the system's approach to risk in its state contracting and its support for innovation. The way in which the risk management rules of a public procurement law system thus frames or characterises its risk management conditions is all-important.

B. Transactional nature of public procurement

A second set of concerns relate to the legal conceptualisation of public procurement as a transactional endeavour. Despite many developments in procurement procedures in recent years, public procurement is still largely conceptualised as a distinct transaction.

This trend is clearly borne out in the GPA, which deals with the concept of a procurement largely as an individualised transaction. For example, it contemplates a “notice of intended procurement” to stipulate, *inter alia*, the “time-frame for delivery of goods or services or the duration of the contract”, “any final date for submission of requests for participation in the procurement” and “the final date for the submission of tenders”.³⁷ Tender documentation for every procurement must include a description of “the nature and the quantity of the goods or services to be procured”.³⁸ The aim of any procurement under the GPA is to “award a contract”.³⁹ These provisions portray a view of the procurement process as aimed at and revolving around a single transaction. At the same time, the GPA also expressly provides for the conclusion of multiple contracts following a procurement,⁴⁰ for recurring contracting with a specific supplier,⁴¹ for the award of a contract following a design contest⁴² and for negotiation with tenderers.⁴³ These provisions may be viewed as signalling an acceptance of a relationship between the contracting authority and suppliers beyond a single contract. However, despite these signals of a long-term relationship between the parties, such relationship is still conceptualised *in terms of* one or a series of transactions. The GPA thus confirms the distinct, transactional nature of public procurement from a regulatory perspective.

From an innovation point of view this may be problematic for a number of reasons. In innovation studies, it is widely accepted that innovation is a highly collaborative endeavour and that “collaboration persists over long periods”.⁴⁴ Innovation thus emerges from a long-term non-linear process in terms of which an innovative product or service is created from the initial impetus to develop it, which originates in some perceived need, to the eventual successful commercialisation of the new product or service, which can be viewed as the successful completion of an innovation cycle.⁴⁵ Thus, the way that public procurement is viewed as transactional in law at least poses a challenge to realising such a long-term relationship.

³⁷ GPA, Article VII.2.

³⁸ GPA, Article X.7.(a).

³⁹ GPA, Article XV.5.

⁴⁰ *See, e.g.*, GPA, Article II.7.

⁴¹ *See, e.g.*, GPA, Article XIII.1.(c).

⁴² *See* GPA, Article XIII.1.(h).

⁴³ *See* GPA, Article XII.

⁴⁴ Lynn K. Mytelka & Keith Smith, *Innovation Theory and Innovation Policy: Bridging the Gap, Paper presented to the Danish Research Unit for Industrial Dynamics (DRUID) Conference(2001); supra* note 13, at 41–43.

⁴⁵ *See* Uyarra & Flanagan, *supra* note 5, at 129-32.

Another challenge emerging from this transactional nature of procurement is to effect transfer. As a strategic endeavour, procurement for innovation can only be successful if it results in transfer and sharing of knowledge and experience. Thus, procurement will only be an effective lever of innovation if there is subsequent transfer of the innovative solution in the public, and eventually the private market, that is, if a sufficient demand is generated on the back of a procurement. This of course calls for a more integrated approach to public procurement to start with, along with opportunities for sharing experiences across a broader market.

The subsequent question is whether current procurement practices, in particular the institutional arrangements set up within current regulatory landscapes, support this transfer and the potential commercial volume to be generated through such transfer. Has the modern trend not been to break the procurement function down to lower institutional levels (that is, procurement by every public entity for its own needs rather than relying on a national, centralised state tender board, and even beyond that to category management practices where particular types of procurement within an entity are conducted by distinct procurement teams)? Do these practices support essential conditions for innovation? I am not suggesting that such institutional rearrangement of the location of procurement functions are necessarily bad – category management seems to be rendering positive results⁴⁶ – but the question is, how does one achieve transfer in such a fragmented approach? In my view, this is where a meta-level of procurement regulation or procurement management becomes essential within a state and preferably at the broadest possible level. What I have in mind is a public entity that can assist in effecting transfer and transversal transacting in order to facilitate commercial volume for innovative goods and services. Such an entity should also be able to assist in coordinating approaches to procurement so that there is more coherence in the procurement market, which in itself should support transfer. In this way, sufficient demand can be generated to justify a particular innovation and both the process and the outcome of the innovation procurement can be widely shared so that subsequent formulations of need in the public service can take account of the innovative solutions generated elsewhere. The institutional structure that I am referring to does not necessarily amount to centralised procurement. A system with centralised procurement will of course automatically have the overarching regulatory framework in place to effect transfer and coordination and thus, there is

⁴⁶ See *Future Purchasing Category Management Survey 2014*, available at <http://www.futurepurchasing.com/2014-global-category-management-survey-report>; OFFICE OF GOVERNMENT COMMERCE, AN INTRODUCTION TO PUBLIC PROCUREMENT, 2008, at 7 (U.K.); Christian Husted & Nicolas Reinecke, *Improving Public-Sector Purchasing* (Aug. 2009), available at http://www.mckinsey.com/insights/public_sector/improving_public-sector_purchasing.

very little in this idea for such systems. The structure at issue here is rather of particular relevance to systems with decentralised procurement functions where the problems of fragmentation creep in, as set out above. In such systems, the introduction of an overarching coordinating or regulatory body, while retaining actual procurement at a decentralised level, should have significant value. The function of the additional entity should thus not be operational, in that it should not perform procurement itself, but should rather be regulatory in effecting coordination and transfer.

While the GPA is largely silent on the specifics of the institutional design of a procurement system, support for a centralised regulatory function can be viewed as inherent in the Agreement. Membership of the GPA involves adherence to a range of commitments, not just at a regulatory level, but also operationally within specific procurements. It is difficult to see how a party will ensure such compliance without some form of overarching regulatory function; there are numerous examples in the GPA that one can point to as typically the work of such an entity. One example is in Article IX.2 where an obligation is placed on parties to ensure that “its procuring entities make efforts to minimize differences in their qualification procedures” and “where its procuring entities maintain registration systems, the entities make efforts to minimize differences in their registration systems”. This is necessarily an ongoing function that a party will have to entrust to some entity with oversight over all its contracting authorities covered by the GPA.

Another important regulatory step in countering a potentially adverse impact on innovation of the institutional dispersal of the procurement function is the harmonisation and standardisation of procurement methods and discourse. This can also play a vital role in facilitating the bridge view of procurement between the public need and the innovator. If contracting authorities between themselves as well as innovative suppliers and public service providers speak the same procurement language, there is much better chance of linking them up and transferring experience in one context to another. Instruments such as the United Nations Standard Products and Services Code, the EU Common Procurement Vocabulary⁴⁷ and perhaps also the European Single Procurement Document⁴⁸ are thus very important tools in this respect. International regulatory instruments like the GPA are of course also of high value in this regard. Not only do these instruments support greater harmonisation in how procurement is conducted, but they invariably call for the use of standard terms and conditions. Thus the GPA,

⁴⁷ Caroline Nicholas, *Developing Countries, Innovative Procurement Strategies & Challenges*, PROCUREMENT WK. (Inst. Competition and Procurement Studies) 2015, at 46.

⁴⁸ Article 59 of the new EU Directive on Procurement, Directive 2014/24/EU of the European Parliament and of the Council of 26 Feb. 2014.

for example, calls for the use of international standards in the formulation of technical specifications for goods and services.⁴⁹

C. *Procurement as a policy tool*

A third area of regulatory challenge in procurement for innovation is the well-worn issue of procurement as a policy tool. A full assessment of the debate about using procurement as a policy tool falls far beyond the scope of this article. It is, however, important to note that procurement for innovation is as much using procurement to achieve a horizontal policy objective as any other social or industrial policy objective in procurement such as gender equality, wealth distribution, job creation, local industrial development, social cohesion, environmental aims or anti-corruption agendas, to name a few.

The pursuit of horizontal policies in public procurement is not unproblematic under the GPA.⁵⁰ This is despite the fact that the GPA itself can be viewed as an instrument whose main aim is the pursuit of a horizontal policy objective in public procurement, namely free international trade.⁵¹ Priess & Pitschas take the strict

⁴⁹ GPA, Article X.2.(b).

⁵⁰ See Arwel Davies, *The National Treatment and Exceptions Provisions of the Agreement on Government Procurement and the Pursuit of Horizontal Policies*, in THE WTO REGIME ON GOVERNMENT PROCUREMENT: CHALLENGE AND REFORM 429 (Sue Arrowsmith & Robert D. Anderson eds., 2011); John Linarelli, *The Limited Case for permitting SME Procurement Preferences in the Agreement on Government Procurement*, in THE WTO REGIME ON GOVERNMENT PROCUREMENT: CHALLENGE AND REFORM 444 (Sue Arrowsmith & Robert D. Anderson eds., 2011); Phoebe Bolton & Geo Quinot, *Social Policies in Procurement and the Agreement on Government Procurement: A perspective from South Africa*, in THE WTO REGIME ON GOVERNMENT PROCUREMENT: CHALLENGE AND REFORM 459 (Sue Arrowsmith & Robert D. Anderson eds., 2011) [hereinafter Bolton & Quinot]; Hans Joachim Priess & Christian Pitschas, *Secondary criteria and their compatibility with EC and WTO procurement: The case of the German Scientology Declaration*, 9 PUB. PROCUREMENT L. REV. 171 (2000)[hereinafter Priess & Pitschas]; Christopher McCrudden, *International Economic Law and the Pursuit of Human Rights: A Framework for Discussion of the Legality of 'Selective Purchasing' Laws Under the WTO Government Procurement Agreement*, 2 J. INT'L ECON. L. 3 (1999); Dragos & Neamtu, *supra* note 27, at 314-315.

⁵¹ As Sue Arrowsmith puts it, the *raison d'être* for the GPA is “to prevent support for national industry against foreign competition.” Sue Arrowsmith, *National and International Perspectives on the Regulation of Public Procurement: Harmony or Conflict?*, in PUBLIC PROCUREMENT: GLOBAL REVOLUTIONS 17 (Sue Arrowsmith & Arwel Davies eds., 1998) [hereinafter Arrowsmith, *National & International Perspectives*]. Priess & Pitschas similarly state that “[i]n principle, the justification for an international public procurement agreement is therefore entirely an economic one. In accordance with this rationale, the overall aim of the GPA is said to be to open up public procurement contracts to international competition

view that “it is doubtful, whether the pursuit of secondary policies when awarding public contracts is compatible with the GPA”.⁵² Their view is *inter alia* based on the argument that the incorporation of various secondary policy objectives in national procurement systems would undermine the very reason for the GPA, which is to create a global standard framework for public procurement that will facilitate free cross-border public procurement transactions. Particularly, this may occur when one country views the use of procurement for a specific policy objective, e.g. in support of innovation, as beneficial, while other countries do not. Under such circumstances, the commonality between public procurement systems, that the GPA aims to generate, will fail. However, there is also a more pragmatic view on the use of public procurement for secondary policy purposes under the GPA. In this view, a secondary policy will only be problematic when it in fact results in discrimination between suppliers of different countries.⁵³ It is thus not secondary policies *per se* that is incompatible with the GPA, but the discriminatory effect that a particular policy may have.

Fortunately this is a space that seems to be opening up and acceptance of the role of policy objectives in procurement has steadily increased over the last few years.⁵⁴ Whether those policy objectives need to be linked to the procurement at hand and how closely those linkages must be, remain topics of debate in many regulatory systems and certainly also arise in the innovation context. In this respect procurement for innovation will have to deal with the same set of questions regarding a balance between price or cost and the achievement of innovation objectives. This will include, for example, the question of what the award criteria will look like to achieve this balancing act and the very difficult questions of quantification behind those criteria.

From the perspective of the GPA, the pursuit of innovation through public procurement may thus not be problematic where the focus is on the innovation itself and obtaining innovative goods or services to fulfil the contracting authority’s needs. However, public procurement of innovation may become more problematic under the GPA if it forms part of a domestic innovation policy aimed at generating innovation within the particular country; for example in support of economic

under equal commercial conditions free of any national preferences.” Priess & Pitschas, *supra* note 50, at 190.

⁵² Priess & Pitschas, *supra* note 50, at 190.

⁵³ Arrowsmith, *National & International Perspectives*, *supra* note 51; Bolton & Quinot, *supra* note 50, at 479–80; Dragos & Neamtu, *supra* note 27, at 315.

⁵⁴ Dragos & Neamtu thus, for example, state in respect of the new EU 2014 Procurement Directives that “[w]e can state that with the new 2014 Directives, the sustainability paradigm is almost taking over the realm of public procurement.” Dragos & Neamtu, *supra* note 27, at 302.

growth. Such a policy would necessarily have to favour local innovation to be effective, which may very well translate into procurement preferences for local suppliers.

The use of procurement as an innovation policy tool also raises questions about the role of procurement officials in developing, implementing and assessing innovation criteria. Is it appropriate and realistic to expect procurement officials to accept responsibility for driving the innovation agenda, either generally or in a particular subject field? Or will there be a subsequent need to design some parallel regulatory process such as green- or eco-labelling,⁵⁵ source of origin certification⁵⁶ or, as in the South African social policy of addressing inequalities, Broad-based Black Economic Empowerment status level certificates,⁵⁷ to provide the basis for innovation assessment in procurement? Under the GPA, the use of such third-party certification schemes may cause significant challenges given that such schemes will in most instances be national (or at best regional) ones. Contracting authorities will thus be obliged to accept equivalent forms of certification, that is certification of the particular characteristic at issue in the procurement (such as environmental credentials or innovation) by processes or agencies other than national or regional ones, in order to adhere to the non-discrimination principles of the GPA. The result is a potential proliferation of certification schemes which may again undermine the very purpose of relying on third-party certification, namely to remove the need for public procurement officials to have to adjudicate on the horizontal policy objectives in each particular procurement.⁵⁸ It is also evident that the introduction of third-party certification schemes will add a layer of complexity to public procurement with consequent costs, which must be discounted in terms of both the innovation agenda and the public procurement objective of value for money.

⁵⁵ See Dragos & Neamtu, *supra* note 27, at 329–30; Totis Kotsonis, *Commission v. Netherlands (C-368/10): Environmental and Fair Trade Considerations in the Context of a Contract Award Procedure*, 21 PUB. PROCUREMENT L. REV. 234 (2012); Dan Wilsher, *Reconciling National Autonomy and Trade Integration in the Context of Eco-Labelling in SOCIAL AND ENVIRONMENTAL POLICIES IN EC PROCUREMENT LAW* 408 (Sue Arrowsmith & Peter Kunzlik eds., 2009).

⁵⁶ For eg., reliance is placed in South Africa on the South African Bureau of Standards approved technical specification number SATS 1286:2011 used to calculate local content for sectors where preference for domestic goods are mandatory. See Department of Trade and Industry, *Guidance Document for the Calculation of Local Content*, available at http://www.dti.gov.za/industrial_development/ip.jsp (S. Afr.).

⁵⁷ See Geo Quinot, *Promotion of Social Policy through Public Procurement in Africa*, in PUBLIC PROCUREMENT IN AFRICA 399 (Geo Quinot & Sue Arrowsmith eds., 2013).

⁵⁸ Dragos & Neamtu, *supra* note 27, at 330; Abby Semple, *Reform of the EU Procurement Directives and WTO GPA: Forward Steps for Sustainability?*, at 12-13 (June 22, 2012), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2089357.

IV. CONCLUSION

There seems to be strong evidence and subsequent growing consensus that public procurement can be a significant factor in supporting broad-based innovation. Public procurement is thus increasingly viewed as a promising tool that states have available to support innovation. The sheer volume of public procurement, along with the possibility of tailoring that significant buying power towards innovative outcomes, results in a powerful demand-side measure in support of innovation. This is a mechanism that any economy that is serious about innovation cannot ignore. However, from a regulatory point of view there are numerous questions that will have to be carefully considered in order to calibrate a procurement system to achieve maximum innovation policy objectives. In some respects these are fairly fundamental questions about how we conceptualise the procurement function in law and how we subsequently design the institutional framework within which this function operates.