

23 April 1992

UNITED STATES - PROCUREMENT OF

2.2 The contract between the NSF and ASA, referred to as DPP89-22832, is a multi-year contract for an amount of US\$251 million. It covers a wide range of activities, including the construction, maintenance and operation of research, housing, logistical and transport facilities and the provision of all manner of logistical support. Its budgeted amount for the period 1 April 1990 to 30 September 1991 was \$70,084,019, of which \$38,953,244 or 56 per cent was allocated to the acquisition of services, and which included the appropriation for the sonar mapping system. In the contract the NSF states that its long-range planning encompasses a wide range of scientific goals as well as maintaining an effective presence on the Antarctic continent. Under the contract, ASA is, inter alia, responsible for procurement of project computer

will be the primary beneficiaries of the mapping system. Furthermore, according to the contract between the NSF and ASA, UNOLS is charged with co-ordinating the use of major shared-use research vessels and identifying future requirements for the oceanographic institutes, which operate these vessels. The Foundation's role in this process will be to ensure that procurement rules are followed and that there are sufficient funds for the procurement.

#### Public Law 101-302

2.7 The initial 1990 appropriation of funds for the Antarctic Research Program provided funds amounting to \$74,000,000 for the United States Antarctic Program (Public Law 101-144, dated 9 November 1989). The United States informed the Panel that part of this sum was to be allocated to the acquisition of a multibeam sonar mapping system. Subsequently, the 1990 Emergency Appropriations Act (Public Law 101-302, dated 26 May 1990) in its Section 307, placed a limit of \$2.4 million on the total cost of procurement of a multibeam sonar mapping system, and further directed that no appropriated funds could be used for procurement of a multibeam sonar mapping system manufactured outside the United States. It was further provided that this Section would not be applicable to any procurement covered by the Agreement on Government Procurement.

Section 307 of Public Law 101-302 reads as follows:

"Section 307. None of the funds appropriated by this or any other Act with respect to any fiscal year for contractual services support of the United States Antarctic Program may be obligated for procurement of a multibeam bathymetric sonar mapping system manufactured outside of the United States: Provided, that not to exceed 2,400,000 shall be available for the total cost of such procurement, including software: Provided Further, that this section shall not be applicable to any procurement covered by the GATT Agreement on Government Procurement."

According to FAR 52.203-10, entitled "Remedies for Illegal and Improper Activity", the text of which is quoted in full in the contract between the NSF and ASA, the NSF would disallow funds if ASA purchased a sonar mapping system of non-United States origin, since the purchase would be in violation of this section of Public Law 101-302 and therefore not an allowable cost.

#### Draft Contract for the Acquisition of the Sonar Mapping System

2.8 The draft of a subcontract between the ASA, as the buyer, and the eventual winning bidder for the supply of the sonar mapping system, specifically refers to the prime contract DPP89-22832 between the NSF and ASA and states that, in the performance of such a prime contract, ASA requires the manufacture of a bathymetric sonar mapping system. It repeats most of the FAR clauses incorporated in the NSF-ASA contract, by reference - with the same force and effect as if they were given in full text - including 52.225-3, "Buy American Act" (Supplies), which specifies that in case of conflicts the United States Manufacture Certification has precedence over FARs. According to information submitted by the NSF in response to a question from the Panel, clauses such as this one, or FAR 52.225-7 ("Balance of Payments") are imposed routinely on procurements which are not covered by the Agreement, both on prime and subcontracts. Additional clauses include 52.249-2, entitled "Termination for Convenience of the Government" which allows the NSF to terminate the subcontract if it were in the interest of the Government to do so. The draft subcontract also includes a Certificate of United States Manufacture, which needs to be signed by the company manufacturing the required item(s) for the procurement of a bathymetric sonar mapping system. The subcontract furthermore contains an assignment clause which allows the Buyer (ASA) to assign this subcontract to any joint venture member and/or its subsidiaries, to the NSF, or to any party selected by the NSF.

### III. MAIN ARGUMENTS

#### (i) Summary

3.1 The European Community argued that the procurement of the sonar mapping system fell under the Agreement on Government Procurement because it was a direct product procurement, above the threshold, by an entity covered by the Agreement, notwithstanding the fact that the system was to be procured through an upstream product procurement contract between a private company (ASA) and the supplier of the system and that the prime contract was a service contract. Accordingly, the application to the procurement of a "Buy American" requirement, resulting in the exclusion of potential foreign suppliers, was contrary to Article II:1 of the Agreement on Government Procurement.

3.2 In normal circumstances such an upstream contract between two private companies would not be regarded as government procurement and would fall outside the scope of the Agreement on Government Procurement. In such a case the application of the "Buy American" requirement might be held to be inconsistent

(ii) Detailed Arguments

3.6 Article I:1(a), whose interpretation is dealt with in the arguments of the two parties, reads as follows:

"This Agreement applies to:

- (a) any law, regulation, procedure and practice regarding any procurement of products, through such methods as purchase or as lease, rental or hire-purchase, with or without an option to buy, by the entities subject to this Agreement. This includes services incidental to the supply of products if the value of these incidental services does not exceed that of the products themselves, but not service contracts per se."

The relationship between the NSF and ASA

3.7 The European Community argued that the procurement of the sonar mapping system was covered by Article I of the Agreement because, notwithstanding the fact that in contractual terms it was to be effected through a subcontract between two private companies, in reality an entity covered by the Agreement (the NSF) was effecting the procurement of a product, whose value was above the threshold of SDR 130,000. The fact that this was done through an upstream contract between two private companies, which was linked to a service contract between the NSF and ASA, was irrelevant.

3.8 In normal circumstances an upstream contract between two private companies would not in principle be regarded as government procurement and would fall outside the scope of the Agreement

for its acquisition, thereby setting special conditions of origin for the procurement of the system. As a result, a company originating in the Community was denied the opportunity to bid, which it had sought.

3.10 Finally, according to a specific clause (H.6) in the NSF-ASA contract, the contract for the purchase of the system could only be concluded with a United States firm and any teaming through subcontracting had to be between United States firms. Therefore, even without a "Buy American" requirement imposed by United States Congress, ASA would have been bound by the contract with the NSF to exclude non-United States offerers from the tender for the system. Whatever the ultimate source of the obligation, it could not be contested that the procurement of the system was subject to a "Buy American" provision.

3.11 All these factors were indications of the direct government grasp on the procurement of the sonar mapping system and pointed to the fact that the acquisition of the system was in reality a direct and distinct government procurement - through an intermediary - of a good above the threshold.

3.12 The European Community put forward as a further argument in favour of the separation of the purchase of the good from the rendering of the service that the sonar mapping system was physically separable from the provision of the service; in other words the system was not consumed in rendering the service and would be recoverable when the service was completed.

3.13 The United States responded that the procurement of the sonar mapping system was being made as part of the service contract between the NSF and ASA, and therefore fell outside the scope of the Agreement, pursuant to the exclusion contained in Article I:1(a). The language of Article I:1(a) indicated quite clearly that all aspects of a service contract, including product procurement elements in the c

3.16 Finally, the assignment clause appeared in the subcontract for the purchase of the sonar mapping system as a matter of routine. These clauses were always used in long-term subcontracts. They were designed to provide continuity in the provision of products or services by a subcontractor if the prime contract was terminated or expired before the subcontract was completed. The legal significance of the clause depended on whether the assignment had been accepted by another party. In answer to a question from the Panel, the NSF stated that in case funds were cut off by Congress, ASA could not avoid its contractual responsibilities to the sonar mapping supplier by assignment.

3.17 The United States observed that the EC's interpretation of clause H.6 of the NSF-ASA contract was incorrect, because H.6 applied solely to the "nationality" of the entity that ASA could team with through subcontracting. It did not restrict the origin of products that could be supplied by a subcontractor. Rather, it concerned only personnel working on the United States Antarctic Program. The clause was included in the contract so that the Program would be staffed by United States citizens, pursuant to the directive of the Executive Order requiring the NSF to maintain a United States presence in Antarctica.

3.18 The United States furthermore argued that for all practical purposes the sonar mapping system would probably be exhausted at the end of the contract. The NSF/ASA contract could run up to as much as ten years and six months, by which time in all likelihood the system would be technologically obsolete. Furthermore, the sonar mapping system could only be removed from the research vessel by placing the vessel in a dry dock and cutting open the hull. According to the NSF, technological advances during the life of the contract would probably reduce the value of the sonar mapping system to less than the cost of its removal. In any case there was no basis in the Agreement to make "separability" or "exhaustibility" of the product element of a service contract a determining factor in the question of coverage under the Agreement. Moreover, the exhaustibility of a product was not a useful test because it would be quite problematic to define the concept of exhaustibility in the procurement context. Finally, the United States argued that it was impossible to believe that, as the Community implied, the Agreement would require procurement officers to separate certain parts of contracts - essentially making them separate transactions - without guidance or specific requirements to do so.

3.19 The United States noted further that the European Community had referred to the subcontract for the procurement of the sonar mapping system as an "upstream contract", a term which did not appear in the Agreement and whose use in this context was misleading, since it appeared to suggest that the subcontract was created subsequent, or as an afterthought, to the prime contract. In fact the requirement to provide instrumentation ~~property~~ which covered the purchase of the sonar mapping system, was provided for in the prime contract from the outset: it was an intrinsic part of the services which ASA contracted to provide to the NSF. This structure was a continuation of the way the NSF had structured its procurement of such services since long before the Agreement on Government Procurement came into being and it was not a pretext to evade the terms of the Agreement.

3.20 The European Community responded that it was not clear that the conclusion of a subcontract for the acquisition of a sonar mapping system was required by the terms of the prime contract between the NSF and ASA, which made no specific reference to the sonar mapping system, in contrast to some other goods, such as the research vessel, whose procurement was specifically mentioned in the prime contract. In the only place where there was reference ~~to property~~ to a sonar mapping system, it was said that this "will be provided" on the ship, which seemed to indicate that the NSF was to provide it, presumably as government furnished property. In an 214.32 Tm/F8 11 Tf(sonr 1 0 0 1 357.36 162.48 Tmproperty.) TjETBT 1

3.21 The Community, in this context, referred to a case which was linked to this one and had been considered in the past by the Committee on Government Procurement, viz. the question of the procurement of an Antarctic research vessel with ice-breaking capability. ASA had been charged by the NSF with making the necessary arrangements for the construction of such an Antarctic vessel. In the Request for Proposal for the research vessel and in the replies provided by ASA's predecessor, the sonar mapping system was indicated as government furnished property. This, in combination with the fact that in the current NSF-ASA contract a modern suite of oceanographic equipment was to be provided - presumably by the NSF - including swath mapping and multi-channel seismic systems, showed that it was the original intention to have the system purchased directly by the government (NSF) - which would have implied that the government made a direct government procurement, outside any service contract. This was confirmed by



3.25 The United States stated that it was not true that the United States Government had referred to the sonar mapping system as government furnished property. The sole reference to the sonar mapping system as government furnished property appeared in answers prepared by ASA to questions submitted by potential bidders in connection with ASA's request for proposals for procurement of the sonar mapping system. That reference in the ASA document, which was neither prepared nor reviewed by the NSF or any other United States Government agency, was erroneous. Under United States procurement law, government furnished property was "property in the possession of, or directly acquired by, the government and subsequently made available to the contractor" (FAR 45.101). The sonar mapping system did not meet this criterion. Consequently, under United States law the sonar mapping system was contractor-acquired property, i.e. "property acquired or otherwise provided by the contractor for

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all other conditions imposed, upon the intermediary. The Community noted that, in the present case, it might be argued that the United States had done just that.

Article III of the General Agreement on Tariffs and Trade

3.36 The European Community took the position that should the Panel not be able to follow its thesis that the procurement of the sonar

part of a service contract and was therefore excluded by virtue of the exclusion of "service contracts per se" contained in Article I:1(a), second sentence. The full text of Article I:1(a) is as follows:

"This Agreement applies to:

- (a) any law, regulation, procedure and practice regarding any procurement of

4.7 While not intending to offer a definition of government procurement within the meaning of Article I:1(a), the Panel felt that in

- B. Is the procurement, although a government procurement under Article I:1(a), first sentence, nonetheless excluded from the scope of the Agreement by virtue of Article I:1(a), second sentence?

4.14 The Panel then considered whether the procurement of the sonar mapping system, found to be within the scope of Article I:1(a), first sentence, was excluded from the Agreement by virtue of Article I:1(a), second sentence. The Community had advanced two propositions: first, that the procurement of the sonar mapping system was a direct or separate product procurement, not in reality or for practical purposes part of the service contract between the NSF and ASA; and secondly that, even if it were held to be part of the service contract, it would still be subject to the disciplines of the Agreement, since the exclusion of "service contracts per se", contrary to the view of the United States, did not extend to products procured under such contracts.

4.15 The Panel noted that if the second of these propositions is true, the first is irrelevant; if the sonar mapping system procurement is covered by the Agreement even if part of a service contract, there is no need to demonstrate that it is not part of such a contract. Conversely, if the first proposition were true it would be unnecessary to consider the meaning of the exclusion of service contracts per se.

4.16 Because this was the primary thesis of the Community, and in order to satisfy itself that it was essential to address the second proposition above, the Panel examined in detail all the arguments, set out in paragraphs 3.9 to 3.12 and paragraphs 3.20 to 3.24, advanced by the Community in support of the view that this was a direct product procurement and not part of the service contract. The Panel accepted that there were a number of considerations which attested to the close and direct interest of the NSF in the process of acquisition of the sonar mapping system; most of these are referred to in paragraphs 4.8 to 4.12, since they were also raised in relation to the question whether this was in fact a case of government procurement at all. On the other hand, one ~~relation~~ argument put forward by the Community - that the sonar mapping system might in fact be property furnished by the government to the contractor - was not persuasive; the Panel accepted the explanation of the United States that the reference to government furnished property in a document issued by the contractor was merely an error. Furthermore, the Panel was unable to set aside the fact that there is a service relationship between ASA and the NSF in the purchase of the sonar mapping system; carrying out the purchase is a service rendered to the NSF by ASA. The Community disputed whether the services relating to the sonar mapping system were part of, or entailed by, the prime contract between the NSF and ASA; the United States maintained that they were so entailed by virtue of the ASA's system

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4.21 It would also seem anomalous that while even products below the threshold can be brought within coverage by the inclusion of the value of services incidental to their supply - which attests the Agreement's objective of securing wide product coverage - products of much greater value should be excluded because the preponderant value of the contract is for services. The Panel found it more difficult to accept that these anomalies were consistent with the intent of the text than to imagine that it included a redundant phrase. It also recalled the general principle that in the interpretation of agreements, exceptions provisions should normally be construed narrowly rather than broadly.

4.22 In the present case, if the sonar mapping system were to be purchased directly from its manufacturer by the NSF, there would be no doubt that the NSF's obligations under the Agreement would apply; but it was suggested that because the NSF had chosen to employ ASA to carry out the procurement as part of a large service contract these obligations were no longer applicable. It was not disputed that

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ANNEX 1

Commission of the European Communities

Geneva, 31 July 1991

AIDE MEMOIRE

Multibeam sonar mapping system

The facts

By a tender notice published in the Commerce Business Daily of 27 February 1991, Antarctic Support Associates (ASA) announced its intention to purchase a sonar mapping system. It was indicated that "Buy American" provisions would apply to the purchase.

By letter of 30 May 1991, ASA informed potential suppliers that it was seeking "a company

The contract (referred to throughout by ASA as "the sub-contract"), which incorporates clauses from the Federal Acquisition Regulations (FAR) provides for assignment of the contract "at any time ... to the Foundation (the NSF), or to any party selected by the Foundation".

The purchase is financed by public funds provided through the NSF.

The sonar mapping system will become the property of the NSF.

NSF is a covered entity under the Government Procurement Agreement.

There is no exception under the Agreement on Government Procurement for purchase of a sonar mapping system.

The value of the sonar mapping system is clearly above the threshold of the Agreement