

**ANALYSIS OF FACTORS INFLUENCING CHINA'S  
ACCESSION TO THE GPA.**

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Analysis of Factors Influencing China's Accession to the GPA.

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**Abstract:**

China, with a huge market in government procurement, submitted an application to join the WTO GPA and formally began the negotiating process with the other signatories to the Agreement while the current parties were revising the 1994 GPA. International trade is not simply the outcome of market forces, of relative supply and demand. Rather, it is the result of a complex and interlocking network of bargains that are partly economic and partly political. This article discusses the main factors influencing China's accession to the GPA from the perspective of trade negotiation, outlines the possible emerging problems and difficulties in the course of the accession and provides a brief recommendation to make the negotiations go on wheels.

**Legislation:** Agreement on Government Procurement (GPA)

**Subject:** PUBLIC PROCUREMENT. Other related subjects: Trade Negotiation

**Keywords:** China; Accession; GPA; Parties; influencing factors

## 1. Introduction

‘Government procurement’ generally refers to the purchasing by government bodies from external providers of the products and services these bodies need in order to carry out their public service mission.<sup>1</sup> Government procurement accounts for 10% or more of Gross Domestic Product (GDP) in most states, and practices in this area can operate as important barriers to trade. The size and nature of government markets means that government procurement has always had a great economic and political importance. On the one hand, Government uses procurement policies to achieve the best possible value for money—that is, to successfully acquire the goods, work or services needed by the government on the best available terms. On the other hand, the government’s procurement power is also frequently used to support industrial, social and environmental policies—that is, as an economic instrument, to strategically promote ‘secondary’ policies, such as supporting national industrial growth, the development of particular regions and disadvantaged ethnic groups. Thus it is not surprising that government procurement is quite substantial in most states and market access has been a subject of great interest for the World Trade Organization (WTO).

The WTO Agreement on Government Procurement (GPA), signed by most of the world’s industrialized countries at the Uruguay Round in 1994 and enforced on 1 January 1996, provides an international legal framework for the liberalization and governance of public procurement markets, which facilitated international market access and reinforced the significance of government procurement as an element of economic activity. In December 2006, negotiators for the Parties to the 1994 WTO GPA reached provisional agreement on the text of a revised Agreement to replace and supersede the existing Agreement. During the GPA coverage negotiations, China submitted an application to the WTO GPA and formally made its initial offer to join the GPA, marking the start of the negotiating process with the other signatories to the Agreement on 28 December 2007. As Susan

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<sup>1</sup> Sue Arrowsmith (2003), *Government Procurement in the WTO*, published by Kluwer Law International, *Studies in Transnational Economic Law*, vol. 16, 2003, p2.

Strange has pointed out, international trade is not simply the outcome of market forces, of relative supply and demand. Rather, it is the result of a complex and interlocking network of bargains that are partly economic and partly political. These bargains involve the trade-off for states of their security interests and their commercial interests. They involve the unequal access of trading partners to both finance and technology. They also involve domestic political bargaining over the access to be granted to national markets, and corporate decision-making regarding secure as well as profitable sources of supply.<sup>2</sup> There is no doubt that China's accession to the GPA is not simply for international trade, but also for political and economic factors. All these interacting factors have influences on the course of China's accession, making it uneven and complex.

The purpose of this article is to provide a special perspective to analyze China's accession to the GPA, in the light of the trade negotiation, including negotiating regulation, negotiating partners and China itself; to discuss the main factors influencing China's accession to the GPA; to outline the possible emerging problems and difficulties in the course of the accession; and provides a brief recommendation to make the negotiations go on wheels. For this purpose, the remainder of the article will proceed as follows: The second section provides a brief introduction to the GPA and its recent revision, and evaluates the revised GPA's influence on China's accession. The third section summarizes the situations of China, including the background of China's commitments to accede to the GPA, the state of play with regard to government procurement and the existing problems. The fourth section shows how the EU and the USA, the main GPA players and negotiating partners, play important roles on China's accession. The fifth section gives a brief recommendation and the sixth section provides concluding remarks.

## **2. Negotiating regulation— the GPA**

### 2.1 General Introduction

#### 2.1.1 Nature and features

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<sup>2</sup> Susan Strange(1994), States and Markets, Second edition1994, Published by London and Washington, 1994, P165.

The GPA which is set out in the Annex IV to the WTO was administered by the WTO, but did not belong to part of ‘package agreements’ which were compulsorily accepted and bound on all Members. So far, it still is not brought into the multilateral legal frameworks of rights and obligations of the WTO. The peculiarity of the GPA within the WTO system results from its own nature and features. The GPA is a plurilateral agreement, meaning that the agreement applies only to those WTO Members who choose to become parties to it. Although it welcomes all WTO Members to accede, membership of the GPA is quite limited, with only forty signatories. Compared with other agreements of the WTO, the effectiveness of the GPA is not only restricted to the number of parties, but also confined to the limited commitments of parties. The commitments of the GPA parties are all undertaken in the several Annexes of their respective documents of accession to the GPA, meaning that the fields not listed in the Annexes are not bound by it.

Therefore, the plurilateral nature of the GPA has three notable features: firstly, limitation of the number of GPA parties and their commitments. Secondly, the GPA should be the agreement to join of the party's own accord, all WTO members have the right to independently choose to accede it or not. Thirdly, the GPA’s disciplines apply only to governments that sign it, and then only for the entities that are listed in the Annexes of each country. The GPA parties reciprocally open the market for government procurement, and Non-parties, not bound by the GPA, are not available to the mutual reciprocity policies given by the GPA parties.

### 2.1.2 Objective and Principles

The objective of the GPA is to provide an effective and transparent multilateral framework of rights and obligations with respect to laws, regulations, procedures and practices regarding government procurement with a view to achieving greater liberalization and expansion of world trade and improving the international framework for the conduct of world trade. In brief, the primary goal is the removal of trade barriers to promote international competition and free trade by prohibiting discrimination against foreign products or suppliers in government procurement.

The GPA shares its main principles with other WTO Agreements. It contains the following: the

first general principle is the non-discrimination principle, embodied by the national treatment and most favoured nation (MFN) obligation. This means each Party should not protect domestic products and suppliers or discriminate among foreign products and suppliers by preparing, adopting or applying all laws, regulations, procedures and practices regarding government procurement. It should be noted that the MFN obligation has not been applied to delimiting the Agreement's coverage in the first place. Another basic principle is the transparency rule. The GPA requires members to create transparency in their procurement procedures, in order to ensure fair and open competition among suppliers. They must open their laws, regulations, procedures and practices regarding government procurement. The GPA also comprises the principle of preferential treatment for developing countries, which is an exception to the non-discrimination principle. Taking into account the objectives of economic and social development and balance-of-payments position of developing countries, the GPA shall provide the special and differential treatment (S&DT) for developing countries, in order to favor their development, financial and trade needs.

### 2.1.3 Accession and Membership issues

Accession to the GPA is open to all WTO Members, and shall be on terms to be agreed between the acceding member and the existing GPA parties. The process of accession involves negotiations on coverage issues (This includes consideration of the entities that will be covered, relevant thresholds, the particular services and construction services that will be covered, any over-riding exclusions from coverage, etc.) and verification of the consistency of the acceding Party's national legislation with the norms and requirements of the GPA. <sup>3</sup>

An important challenge for the WTO and the existing parties to the GPA is to increase the number of participants in the open international procurement market. Currently, Membership to the GPA still remains limited: out of the total of 153 WTO Members (at 23 July 2008), 40 WTO members are covered by the GPA (if counting the 27 Member States of the EU as one, only 13 parties). They are the European Communities (including its 27 Member States); Liechtenstein,

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<sup>3</sup> Robert D. Anderson (2007), *The WTO Agreement on Government Procurement (GPA): The Process for Accession to the Agreement and Related Issues and Developments*, West Government Contracts Year in Review Conference - Covering 2007.

Switzerland, Norway, Iceland, Canada, the United States, Japan, the Netherlands with respect to Aruba, Hong Kong, China, Singapore, South Korea and Israel. Most of the parties to the GPA are developed countries and the majority of developing countries are excluded. Furthermore, the majority of developing countries that are parties to the Agreement, including Israel, South Korea, Singapore and Hong Kong, China, have "advanced economies" according to the classification of the International Monetary Fund. <sup>4</sup>

From the perspective of costs and benefits, Arrowsmith analyses the reasons for limited membership of the GPA. She considers the 'costs' that deter states from acceding to the GPA. First of all, most states seek to retain the power to use discriminatory procurement to support national industrial objectives when other policy tools are constrained by other WTO agreements, particularly for developing countries with a large state sector, in which protectionist procurement measures have more market impact. Another consideration is the desire to promote non-industrial secondary policies—such as social, environmental and human rights policies—through procurement. A third factor deterring GPA membership in some states is the fact that transparency rules curtail the possibility to award contracts for personal or political objectives; There are also a number of practical difficulties with the GPA in its current form, such as the burden of undertaking 'bilateral' negotiations, the lack of clarity in many of its rules and stringent enforcement mechanisms. On the other hand, she also considers the reasons for limited membership of the GPA from the benefits perspective. The potential benefits of GPA membership, both from a political and from an economic perspective, are limited by a number of features of the current Agreement. The 'positive list' approach adopted in relation to procuring entities and services inhibits the incentives for accession to, in particular, small countries and developing economies; Further, a major problem in relation to developing country participation in the WTO is the inability of the supply-side in those countries to respond even to opportunities that do exist; Another problem in attracting new members is the GPA's 'all or nothing' approach, which is tempered both by the possibilities for flexibility in the scope of

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<sup>4</sup> Valeria Guimaraes De Lima e Silva, *The Revision of the WTO Agreement on Government Procurement: to what extent might it contribute to the expansion of current membership*, *Public Procurement Law Review*, 2008, 2, 66.

coverage and in the possibilities for negotiating limited exemptions for covered procurement. The absence of formal recognition of a ‘tariffication’ approach or a formal structure for negotiation and gradually eliminating barriers of this kind makes it difficult for acceding states to negotiate based on this approach.<sup>5</sup>

## 2.2 The revised GPA

### 2.2.1 The objectives and outline of the revised GPA

With a view to improving the Agreement and achieving the greatest possible extension of its coverage among all parties, the 1994 GPA contained a built-in agenda for future negotiations to improve the Agreement.<sup>6</sup> The negotiations of the GPA are divided into two parts, including the negotiations of non-market access in the Agreement (the Agreement text) and the negotiations of obligation to market access (coverage negotiation). The purpose of these negotiations is three-fold: (1) to improve and update the text of the Agreement and advance in information technology and procurement methods; (2) to extend the coverage of the Agreement; and (3) to eliminate the remaining discriminatory practices. The negotiations are also intended to facilitate accession to the Agreement by additional Parties, notably developing countries.

The negotiations of the GPA have been under way for several years. The first part consists of the revision of the text of the Agreement, which was completed and agreed by the parties in December 2006. The revised Agreement is provisional in two aspects: first, it remains subject to a final legal check and verification of consistency; Secondly, the agreement on the text has been explicitly made subject to a mutually satisfactory outcome to the negotiations on coverage, which have been under way for some time but have still to be completed. Compared with the 1994 GPA, the revised text significantly improves the current GPA and has two notable changes: one is the changes of Article in the Agreement. The revised text re-orders the provisions to correspond more closely to the order in which procurements are conducted, and re-groups related provisions into a single article. As a result,

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<sup>5</sup> Sue Arrowsmith (2003), *Government Procurement in the WTO*, published by Kluwer Law International, *Studies in Transnational Economic Law*, vol. 16, 2003, p439-444.

<sup>6</sup> GPA Article XXIV.7 (b) requires the parties to review the GPA within three years of its entry into force (1995) and ‘periodically’ thereafter, with a view both to ‘improving’ the Agreement and to extending coverage.

the revised text simplifies its structure, making compliance by new Members easier. Another is the changes of content, including definitions, scope and coverage, developing countries, procurement approaches, notices, conditions for participation and qualification of suppliers, consultations and dispute settlement, electronic procurement tools and so on. The revised text improves the quality of the drafting and makes it more user-friendly by updating the GPA to take into account developments in government procurement practices, clarifying transitional measures for developing countries, and agreeing to develop arbitration procedures to resolve differences over the modification of the entities covered by the GPA.

### 2.2.2 Influence of the revised text on China's accession

Although the revised GPA improves on the existing Agreement in various significant ways, this article will mainly focus on the flaws of the revised text in its influence on the China's accession.

First of all, the MFN obligation in government procurement is a conditional most favoured nation treatment. That is, the commitments which the party obtains through negotiations cannot be applied to other parties automatically and unconditionally. Although a MFN obligation is clearly provided in the GPA (1994 GPA Article III and the revised text Article V) for covered procurement, the MFN rule is not the basis for the negotiation to decide which entities and types of procurement contract are covered on the first place. The implementing MFN is derogated by the fact that coverage in relation to categories of products, services and entities was based mainly on strict reciprocity. As Arrowsmith notes, most parties have in fact provided for very extensive derogations from MFN, as a result of which [with regard to coverage commitments] the GPA has the appearance more of a series of bilateral agreements than a multilateral agreement.<sup>7</sup> To reduce the disadvantages for developing countries in coverage of negotiations as previously mentioned, the revised text adds the extension of the MFN principle to developing countries upon their accession to the Agreement.<sup>8</sup> However, the implementing of MFN is still subject to the negotiations between that Party and the developing country. This means that the application of the MFN obligation to developing countries is still a

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<sup>7</sup> Sue Arrowsmith (2003), *Government Procurement in the WTO*, published by Kluwer Law International, *Studies in Transnational Economic Law*, vol. 16, 2003, p111.

<sup>8</sup> See the revised text Art.IV.2.

conditional most favoured nation treatment, and remains uncertain. Therefore, the revised text still does not restrict parties' discretion to make various types of party-specific derogations departing from MFN, nor does it change the situation in nature. For China's accession, departures from the MFN principle would have the influences on the following: firstly, it will not be allowed to take the benefit of a MFN rule without reciprocal concession, meaning the potential benefits of China's accession are limited; secondly, China must spent much time and money to come to a series of bilateral agreements, meaning increasing the costs of accession; thirdly, the MFN principle to developing countries is restricted to the negotiations between the parties and developing countries, so the real gains of developing countries from the MFN rule remains much doubt; finally, it will add the political tensions that can arise when countries give different treatment to different foreign states.

In the next place, the merits and demerits of provision on S&DT for developing countries should be further analyzed. To encourage developing countries to join the Agreement and facilitate the accession process, the revised text has clarified concerns about special and differential treatment for developing countries, providing the legal basis for developing countries adopting special and differential treatment. However, we should note the following points: firstly, the regulations of transitional measures narrowly circumscribe the compensating scope, only adopting four measures listed in the Article; secondly, the application of transitional measures must be based on developing countries' specific needs and negotiations with the Parties. This means that the transitional measures are potentially available, if the developing countries can fully enjoy privileges are mainly subject to negotiations. At the same time, the Article also regulates that the developing country must use the measures agreed during a transition period. The facts that the benefits of transitional measures are provided on a transitional basis and are not determined by any objective terms in the Agreement, but rather depend on the consent of GPA parties, raises uncertainties for developing countries on the level of the implementation that will be given to this provision;<sup>9</sup> thirdly, the revised text cancels the regulation which allows developing countries to apply exclusions from the rules on national

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<sup>9</sup> Valeria Guimaraes De Lima e Silva, *The Revision of the WTO Agreement on Government Procurement: to what extent might it contribute to the expansion of current membership*, *Public Procurement Law Review*, 2008, 2, 84

treatment to certain entities, products, or services, and adds the MFN principle to them upon their accession to the Agreement. As we know, most parties of the GPA do not strictly abide by the MFN rule, and the application of the MFN rule in developing countries finally depends on argy-bargy in the negotiations. Therefore, it should further be considered whether developing countries would gain more benefits from either the MFN rule or exclusions from the national treatment rule; finally, the revised GPA contains a provision on technical co-operation that the parties shall give due consideration to requests by developing countries for technical co-operation or capacity building related to accession or implementation of the Agreement.<sup>10</sup> According to Article IV: 9, the Committee may develop procedures for the implementation of this Article. That means the enforceability of the Article is dependent on whether and how the Committee will address the current omissions on enforcement. So far, it does not clarify how this provision shall be implemented. The S&DT provisions established are more defensive than offensive in nature, in the sense that they allow for additional protection, on a transitional basis, of the markets of developing countries, but do not offer them a significantly improved access to the market of other GPA parties.<sup>11</sup>

In the end, the revised text contains in uncertainties in some rules, hindering the accession course. Because of the lack of clarity in many of its rules, GPA accession also brings costs in terms of uncertainty, which affects both important national policy issues and the day-to-day conduct of procurement. Apart from exacerbating the practical difficulties of implementation, this uncertainty means that national policy makers and individual purchasers and suppliers cannot be confident that the rules that they apply are fully GPA-compliant.<sup>12</sup> As for the influences on China's accession, uncertainties in the revised text mainly embody the following: first of all, the draft decision of the revised text indicates that not all parties to the 1994 GPA may become parties to the revised GPA, and sets rules for the co-existence between both Agreements. It means that current parties to the 1994

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<sup>10</sup> The revised GPA: Article IV: 8.

<sup>11</sup> Valeria Guimaraes De Lima e Silva, *The Revision of the WTO Agreement on Government Procurement: to what extent might it contribute to the expansion of current membership*, *Public Procurement Law Review*, 2008, 2, 98.

<sup>12</sup> Sue Arrowsmith (2003), *Government Procurement in the WTO*, published by Kluwer Law International, *Studies in Transnational Economic Law*, vol. 16, 2003, p441.

GPA may maintain their status quo by not acceding to the revised version, and newly acceding Members will most probably join the revised GPA. In that case, the new acceding parties will not be able to fully benefit from the expanded coverage nor from the S&DT provisions provided by the revision, since these will not be enforceable against the parties to the GPA 1994. Therefore, the potential market access gains of China could be significantly reduced and might not compensate for the effort and costs involved in accession; secondly, the revised text has introduced an arbitration procedure to address the difficulty for a party in withdrawing a covered entity. However, the details of such a procedure and a common understanding of what constitutes government control remain to be developed through negotiation. Because the new arbitration procedure and the indicative criteria remain to be adopted by the WTO Committee on Government Procurement in the future, it remains unclear under the revised GPA whether the competitive market environment of an enterprise may qualify as a criterion demonstrating the effective elimination of government control over that entity, and whether the new arbitration procedure will be able to deter any unilateral action of the party proposal for withdrawal. Thus the difficulty of withdrawing a covered entity is likely to discourage countries with a large state sector from tabling an extensive entity offer covering their state enterprises since such enterprises cannot easily be withdrawn later.<sup>13</sup> There is no doubt that the uncertainties would largely affect China's entity offer; thirdly, the revised text introduces a new definition of 'covered procurement', including two new elements: (1) for governmental purposes; (2) not procured with a view to commercial sale or resale. However, the revised text does not construe the commercial procurement exclusion narrowly and with procedural guarantees. Since the term 'governmental purposes' is not further defined, a second problem is that this ambiguous new qualification makes it difficult to ascertain the exact scope of covered procurement. Furthermore, according to the foregoing statement, some rules of the revised text remain unclear, lacking the related procedures to implement provisions such as the S&DT. All these uncertainties would bring about many obstacles to China's accession.

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<sup>13</sup> Wang Ping (2007), *Coverage of the WTO'S Agreement on Government Procurement :Challenges of Integrating China and Other Countries with a Large State Sector into the Global Trading System*, Journal of International Economic Law, 1–34, Oxford University Press 2007.

## 2.3 Negotiations on coverage

### 2.3.1 Introduction

The second part of the negotiations of the GPA is the negotiations of obligation to market access (coverage negotiation), which refers to which types of procurement contract and procuring entities and thresholds are covered. Since there are no common rules on the coverage, GPA coverage negotiations are conducted bilaterally based on the principle of reciprocity which means that markets are opened in return only for equivalent concessions by trading partners.<sup>14</sup> For entity coverage, the GPA mainly adopts the 'positive list' approach which only those entities listed in Appendix I to the Agreement are covered.

The agreement on coverage is more difficult to reach, since it depends on mutually acceptable requests and offers about market access by the parties to the GPA. Thus negotiations on coverage are taking longer to complete than negotiations on the revised text. Although the overall negotiations were scheduled to be completed by the end of 2007, the negotiations are still ongoing so far. The negotiations on market access are in a stiff and pivotal phase. Not all the parties to the negotiations have submitted initial offers so far. Moreover the European Community has made clear its dissatisfaction with the level of ambition reflected in other major Parties' offers and threatened to reduce its own offers if other parties' offers do not improve substantially. Synchronously, US negotiators are under pressure to ensure that international trade instruments relating to government procurement do not call into question the viability of related US national policies. In this context, it remains to be seen how the coverage negotiations will unfold from here.<sup>15</sup>

### 2.3.2 Difficulties for acceding countries with a large state sector

The coverage negotiations closely are related to the revised text, and they are mutually influenced. Some flaws in the revised text also hinder the advance of coverage negotiations. (As explained in 2.2.2, the following will not discuss the related detail)

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<sup>14</sup> Sue Arrowsmith (2003), *Government Procurement in the WTO*, published by Kluwer Law International, *Studies in Transnational Economic Law*, vol. 16, 2003, p109.

<sup>15</sup> Robert D. Anderson, *Renewing the WTO Agreement on Government Procurement: progress to date and ongoing negotiations*, *Public Procurement Law Review* 2007, 4, 270-271.

As noticed by Wang, transitional economies with a large state sector, such as China, might face difficulties in their coverage negotiations. He points out a number of issues relevant to their GPA accession: The first problem in negotiations for countries with a large state sector is the current GPA approach to the entity coverage negotiation. In particular the principle of reciprocity rather than the MFN will make it difficult for these countries to decide which state enterprise to offer in order to secure reciprocal treatment. A second problem is the difficulty in preparing the offer of entity coverage due to the lack of unified practice with respect to listing entities under different Annexes of Appendix I. This lack of formal coherence and unified terminology will make it difficult for acceding countries such as China to decide where to list their public institutions and state enterprises. The third problem is the difficulty of withdrawing a covered entity and its impact on preparing the offer of entity coverage by countries with a large state sector.<sup>16</sup>

### 2.3.3 Ongoing negotiations among existing parties

Final agreement on the revision of the GPA requires a mutually satisfactory outcome in the market access negotiations to open up additional government procurement to international competition under the GPA. Since coverage negotiations among the existing parties have not been completed according to schedule, the negotiating results remain uncertain. It would influence two aspects of China's accession. On the one hand, the revised GPA cannot be enforced until there is a satisfactory outcome. When the existing parties reach an agreement the position will remain unclear, for the possibility for negotiation of mutually acceptable concessions would be limited by the fact that negotiations are based mainly on sectoral reciprocity, without scope for cross-sector trade-offs. Therefore, China's accession would face a dilemma as to which rules (either 1994 GPA or the revised GPA) should be applied; On the other hand, China's accession probably takes longer than it would normally, since the accession process has become intertwined with the GPA expansion negotiations occurring at the same time. The situation is the same as with Korea's accession to the GPA, in which

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<sup>16</sup> Wang Ping, Coverage of the WTO'S Agreement on Government Procurement :Challenges of Integrating China and Other Countries with a Large State Sector into the Global Trading System, Journal of International Economic Law, 1–34, Oxford University Press 2007

Korea was participating in the GPA expansion negotiations along with the existing signatories of the GPA under the GATT. Because of the lack of other parties' offers, the accession brings costs in terms of uncertainty, which directly affect the initial offer. Korea's experience was to make only a limited offer before seeing the other's offers, because it would be very difficult to withdraw any part of the initial offer list once the others had seen it. Thus Korea's first offer list was very conservative, including a minimum number of local government entities and public corporations.<sup>17</sup> Korea's strategy was to start with a minimum offer list and then make adjustments depending on the responses from other parties. China also follows this strategy because the other parties are preparing their offer lists during the GPA expansion. Therefore, it is no wonder that China's initial offer is so narrow and limited.

### **3. The negotiator---China**

#### **3.1 The background on China's accession and commitments**

WTO members tried to persuade China to join the GPA at the same time as the WTO. However, China, in the course of its accession to the WTO in 2001, only committed itself to joining the GPA 'as soon as possible'. In its Protocols of Accession to the WTO, China undertook the following commitments: first, China intended to become a Party to the GPA; second, China would become an observer at the GPA upon accession to the WTO Agreement and initiate negotiations for membership in the GPA by tabling an Appendix 1 offer as soon as possible; third, China would conduct their procurement in a transparent manner, and provide all foreign suppliers with equal opportunity to participate in that procurement pursuant to the principle of MFN treatment.<sup>18</sup> Under constant pressure from its major trade partners, China made the first move towards fulfilling that commitment in April 2006: as an outcome of the ongoing Sino-US trade dialogue, China committed to table an

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<sup>17</sup> Inbom Choi. Long and Winding Road to the Government Procurement Agreement: Korea's Accession Experience. The WTO and Government Procurement, edited by Evenett, Simon J. and Hoekman, Bernard, Published by Edward Elgar Publishing, Inc, 2006. p502.

<sup>18</sup> Report of the Working Party on the Accession of CHINA, WT/ACC/CHN/49, paragraphs from 339 to 341, 1 October, 2001. <http://www.wto.org>.

offer of GPA coverage by the end of 2007.<sup>19</sup> China kept its promise and submitted its initial offer on time.

There is a lack of interest in most developing countries in joining the GPA, and China is no exception. Armenia, Croatia, Mongolia, the Former Yugoslav Republic of Macedonia and Saudi Arabia are also expected to join the Agreement as a result of the commitments undertaken in their respective Protocols of Accession to the WTO. Although, the GPA should be the agreement to join of the party's own accord, nowadays the accession to the GPA represents either a pre-condition by some of the Members of the GPA, imposed on all states that want to accede to the WTO during the negotiation process, or by the European Communities as a condition for states that intend to become one of its Members.<sup>20</sup> Therefore, in nature, the motive for China's accession is not a self-imposed task, lacking incentives. That is, China's commitments to accede to the GPA were a pre-condition of acceding to the WTO during the negotiation process, imposed by some of the Members of the GPA. We should note that the objectives of international trade organizations are set by the most powerful state in the group or on the basis of a bargain between two or more powerful states. International trade organizations' role and impact have consequently tended to reflect the concerns of their most powerful member state or group of states rather than interests of those developing countries.<sup>21</sup> As Arrowsmith analyses above, the reasons that most developing countries lack in joining the GPA interest are very clearly from the 'costs and benefits' perspective.

### 3.2 The existing problems in government procurement

From a historical perspective, the government procurement system in China remains in its founding stages, there are many problems and difficulties can be expected in the course of accession to the GPA and its implementation.

First of all, the government procurement system is still defective. The Ministry of Finance

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<sup>19</sup> The U.S.-China Joint Commission on Commerce and Trade (JCCT) Outcomes on U.S. Requests, 11 April, 2006., Available at [http://www.commerce.gov/NewsRoom/PressReleases\\_FactSheets/DEV01\\_005280](http://www.commerce.gov/NewsRoom/PressReleases_FactSheets/DEV01_005280), visited on 15 Aug 2008.

<sup>20</sup> Valeria Guimaraes De Lima e Silva, The Revision of the WTO Agreement on Government Procurement: to what extent might it contribute to the expansion of current membership, *Public Procurement Law Review*, 2008, 2, 66.

<sup>21</sup> Susan Strange (1994), *States and Markets*, Second edition 1994, Published by London and Washington, 1994, p186.

promulgated the Interim Regulations on Government Procurement in April 1998, and the Government Procurement Law of China was implemented in 2003. So, Chinese government procurement framework is relatively young and has some teething conditions and problems. For example, there is no uniform law to regulate the government procurement in China. Different ministry and local government have their own regulations to manage related government procurement. Especially, existing laws adapted in government procurement have conflicts. The construction projects in government procurement which should be regulated by the Government Procurement Law are currently covered by Invitation and Submission of Bids Law which is a procedural law. However, it is very difficult that different interest groups negotiate amendments to both laws for any amendment will involve complicated bureaucratic procedures. In the next, the Government Procurement Law is simply and principled, and lacks detailed regulations and judicial explanations to implement and consolidate. Thus implementations of government procurement are non-standard and optional in practice. Most importantly, the process of accession shall ensure the verification of the consistency of the acceding Party's national legislation with the norms and requirements of the GPA. However, there are many discrepancies between Chinese law and international rules, such as legal objective and principles, coverage scope, procurement approaches and procedures, notices, qualification of suppliers. Thus, the main task of the government should consider how to reform and improve the systems to meet the need of internal reform of economic and political systems and the requirements of the GPA. But it is very difficult and complicated work.

In the next, administrative system in government procurement is currently very complicated, and involves in many departments, resulting in the confusion of responsibility and the inaccuracy of function. All these result in little effectiveness of implementing procurement and confusion of implementation. On the other hand, the administrative institutions of government procurement including supervision and relief are still not perfect. These will influence and hinder the implementing of government procurement.

Thirdly, government procurement is a systemic and professional work and needs professional institution and personnel to implement. Since government procurement system remains in its

founding stages, the personnel of government procurement in China mostly come from the financial department. They lack the professional knowledge including bidding, market investigation and procuring production, the GPA, having the large gap between the demands of government procurement. Currently, their ability and knowledge cannot fully adapt to the professional work and the demand of accession to the GPA.

As the reform further progresses, China remains far behind the developed countries. As we have seen the Chinese realities, such as its government functions, legal system, administrative system, government procurement personnel, have many problems and difficulties. It will take a long time for the system to be established and perfected, and the practices to be popularized and regulated.

### 3.3 A sticking point—the large state sector

The large state sector remains the ‘backbone’ of Chinese economy, therefore, the operation of the state sector gives rise to the enormous importance and special characteristics of government procurement market in China. On the other hand, the current parties cannot easily give up the large state sector which is a huge market in government procurement. It can be expected whether China's state sectors should be covered by the GPA is a sticking point in the trade negotiation.

For China, a large state sector including airports, energy, communications and water supply play important roles in economic development, even involving in economic security. The government must consider the risk of opening market. Thus, from the point of view of both politics and economic analysis, it is very difficult to choose among the entities that it will offer in exchange for reciprocal concessions from GPA parties. In the next, Chinese state-owned enterprises (SOEs) are not listed as “procuring entities” in China's Government Procurement Law. Chinese SOEs procure according to Invitation and Submission of Bids Law only when there's a construction project. But Appendix I of the GPA describes qualifying procuring entities, and includes public utilities, SOEs, monopolies etc. therefore, in foreign countries, construction projects such as bridges and power stations are all procured by the government, while in China, such procurement is covered by bidding law. Thirdly, it is difficult for China to obtain reciprocal concessions on sectors of interest, since most of the GPA parties have a limited number of state enterprises due to their large degree of privatisation. China has

far more and bigger state-owned firms than those in the current parties. If all are counted, other parties to the Agreement are not able to make reciprocal offers in exchange. Therefore, China cannot list too many state sectors according to its cost and the reciprocal principle. Moreover, the government will consider the difficulties of withdrawing the coverage entities. Finally, there is very equivocal and inaccurate in how to fix on the character of the sectors in China. Since China's domestic framework and administrative system is not enough clear, it is hard to distinguish the character of institution between state-owned sectors and non state-owned, remaining uncertain and fuzzy. Thus, it cannot clearly mark off the sectors covered by government procurement in some cases. Moreover, some institutes in China are in the course of the reform and adjustment, and their characters and function cannot be certain currently. These will result in the confusion of management and implementation.

#### 3.4 The limitation in implementation of secondary objectives

As a policy instrument, procurement regulation is merely a reflection of general government policy and ideology and that is apt to be used effectively to pursue a number of social and political goals, which is a distinct character different from commercial procurement. Most states seek to use discriminatory procurement to support national industrial objectives and promote non-industrial secondary policies such as social and environmental policies. There is no exception to China. Chinese Government Procurement Law regulates preemption of national production as a procurement principle. In 2006, The Ministry of Finance drafted a policy of government procurement to support independent innovation industries, exerting the policy function of government procurement. At the same time, it advocated the 'green procurement' in government procurement and also constituted related policy to protect environment, save energy sources and maintain public interests through government procurement. Therefore, there is a practical significance of pursuing secondary policies through government procurement in China. However, the GPA limits secondary uses of procurement based on the following reasons. First, the discriminatory policies such as support domestic industry are in general prohibited by the national treatment rule; Second, secondary objectives can affect transparency. Finally, some measures including offsets, qualifications and technical specifications

also restrict trade, which may also affect secondary policies. Therefore, these measures are prohibited under the GPA rules.

In this area, the Chinese government faces a dilemma on basis of their situation. The economic developments in China largely depend on the public investment and finance of the government. The government procurement plays an important role in favour of secondary objectives while other policy tools such as quotas, duties, or subsidies are constrained by other WTO agreements. Without the protection and support of procurement policy, the national industries may be at a fall. On the one hand, the manufactures that now make up the bulk of internationally traded goods are mainly imported and exported by the industrialized countries. Despite faster growth-rates in developing countries, this domination of world trade by the developed market economies has been a consistent trend. Especially, opportunities for developing countries to participate in services markets (including construction) are limited by significant restrictions on the movement of natural persons. On the other hand, the holistic competitive powers of national industry in China remain lower level and the development of market fall far behind, the level of management of corporation should further be improved, lacking the experience of international competition. Once when opening the market in government procurement, it will make a strong impact on the national industries. Moreover, the government procurement not only is related to industrial objectives, but is related to non-industrial secondary policies. The limitation in implementation of secondary objectives means that the government loses an important policy instrument to protect the environment and improve employment.

### 3.5 Domestic politics matters

International trade negotiation refers to not only international interests, but also domestic interests. Domestic politics matters are generally involved with citizen, interest group and government. The foreign trade policy-making process is generally torn by conflicting objectives of national interest-groups. Industry associations, labor unions, regional authorities, consumer lobbies,

and government agencies all interact in determining the policy outcome.<sup>22</sup> Although greater emphasis on the economic impact of trade policies would be very beneficial, many governments are unlikely to support such initiatives without strong domestic political support in favour of this change.<sup>23</sup>

For China, the potential benefits of GPA concessions are in any case limited, whatever the approach to negotiation. Even when the economic benefits are accepted, political pressures mean that China may continue to protect industry through procurement, particularly since other policy tools are constrained by WTO rules. So far, the benefits of GPA membership have not generally been sufficient to overcome these constraints.<sup>24</sup> With the progress of democracy, the public in China begin to exert an influence on the government by the public voice. Government procurement is related to public expenditure, domestic industry, and social policies which can easily attract the public's attention. The risk of opening market and great concession in the negotiation may probably make the public dissatisfied with the trade policy of government, against the opening market in government procurement. It goes without saying that interest groups will play a more important role in foreign trade policy-making process. Governments procure considerably more manufactured goods and services which are developed countries' comparative advantage than agricultural goods which developing countries specialize in producing. This creates a larger scope for lobbies and resistance to the liberalisation of the local procurement market by domestic groups, which has a high level of political interference. During the course of investigation on the influence of the GPA on China,<sup>25</sup> domestic suppliers were very worried about the market opening and lobbied the government not to join the GPA, seeking to maintain their competitive advantage in the procurement market. More importantly, owing to the particularity of government procurement, accession to the GPA will have a large influence on

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<sup>22</sup> Bernard Hoekman and Michel Kostecki(1995), *The Political Economy of the World Trading System: from GATT to WTO*, Oxford university press, p23-24.

<sup>23</sup> Bernard Hoekman and Michel Kostecki(1995), *The Political Economy of the World Trading System: from GATT to WTO*, Oxford university press, P274.

<sup>24</sup> Sue arrowsmith, reviewing the GPA: the role and development of the plurilateral agreement after Doha, *Journal of International Economic Law* (2002) 761-790., oxford University Press.

<sup>25</sup> The institute of public market and government procurement at university of international relations undertook the project on the influence of accession to the GPA on China.

the government. On the one hand, once China joins the GPA and opens the market in government procurement to the world, it could probably have a strong impact on domestic industry and even national economic security may be damaged. The policy maker must consider this kind of aftermath and its political risk. Moreover, negotiation risk which failure to extract reciprocal concessions may mean losing political support for the agreement. On the other hand, the government must procure goods or services through a transparent, equal and open manner, and cannot protect domestic products and suppliers or discriminate among foreign products and suppliers. This means that the behavior of government is restricted by international organization and foreign government. Therefore, the government would face a new challenge while China joins the GPA.

#### **4. The negotiating partners---- the main GPA parties**

This basic asymmetry between the power of governments in developed and developing countries to ensure their own economic security through trade arrangements and regulations, and between associations of manufacturers and primary producers to do the same, is yet a feature of the world's trade structure as it exists in the real world.<sup>26</sup> The EU and the USA, two leading players in the world trade system, play important roles in urging China to join the GPA through their power in trade organization.

##### **4.1 The reasons of the parties to advance China's accession**

First of all, a huge market in government procurement in China is the main reason pushing the current parties urgently calling upon China to join the GPA. According to official sources, China's procurement market reached a total of 350 billion RMB (US \$46 billion) in 2006.<sup>27</sup> With the transition of government function and the foundation of a public financial management system, the scale and proportion of procurement expenditure would be improved step by step. According to the EU Commission estimates, public purchase (widely speaking) will represent up to 25% of China's

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<sup>26</sup> Susan Strange (1994), *States and Markets*, Second edition 1994, published by London and Washington, 1994, p176.

<sup>27</sup> China, Ministry of Finance, Report on the implementation of the central and local budgets for 2006 and on the draft central and local budgets for 2007, Fifth Session of the 10th National People's Congress on March 5, 2007, <http://www.china.org.cn/english/government/203405.htm> [Accessed March 19, 2007].

GDP - that is about € 500 billion! <sup>28</sup>

Secondly, government procurement boasts a history of over 200 years in western developed countries whereas it remains a new thing in China. The current parties hold sound legislation, a mature system and rich experience in practice. Moreover, they have a strong power of competition in manufactured goods and services. We should note the fact that governments procure considerably more manufactured goods and services in comparison to agricultural goods. Due to developing countries' comparative advantage in producing agricultural goods and developed countries specialisation in the production of manufactured goods, it can be seen that developed countries would get more benefits than developing countries from the opening market in government procurement.

Finally, China's accession to the GPA would be a good model for developing countries, facilitating the expansion of membership to the Agreement. Increased membership is of interest for GPA parties not only for the purpose of expanding the share of the government procurement market subject to the WTO system, but also because it will eventually lead to the desired multilateralisation of the GPA, which would ultimately legitimise the principles and rules of the Agreement in the international sphere. <sup>29</sup> China will be the first major economy with a large state sector negotiating GPA accession, if the negotiation is successful, it will encourage other economies mentioned earlier 'at the doorstep' of the GPA to take further action to fulfill their commitments. For Anderson points out, China's very recent initiation of its GPA accession process may well mark a watershed in the evolution of international regulation of public procurement markets. Clearly, China's accession will enhance the importance of the Agreement over time. <sup>30</sup>

#### 4.2 Taking actions on China's accession

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<sup>28</sup> Peter Mandelson, European Commissioner for External Trade, market access newsletter, Issue 7 – 31 March 2008, available to [http://trade.ec.europa.eu/doclib/docs/2008/march/tradoc\\_138475.pdf](http://trade.ec.europa.eu/doclib/docs/2008/march/tradoc_138475.pdf), 18 Aug, 2008.

<sup>29</sup> Valeria Guimaraes De Lima e Silva, The Revision of the WTO Agreement on Government Procurement: to what extent might it contribute to the expansion of current membership, *Public Procurement Law Review*, 2008, 2, 98.

<sup>30</sup> Robert D. Anderson (2007), the WTO Agreement on Government Procurement (GPA): The Process for Accession to the Agreement and Related Issues and Developments, *West Government Contracts Year in Review Conference - Covering 2007*.

The EU and the USA, the main negotiating partners of China, successfully urged China to commit to joining the GPA when China acceded to the WTO. Nowadays, they are hammering at making China keep its promise by a series of actions together or solely. On the one hand, the EU committee and the USA government take the same standpoint on the benefits of open market in government procurement, and take combined action to expedite the progress in negotiations and membership expansion. At the 2005 EU-U.S. summit, recognizing the benefits of open and competitive procurement markets, the EU and U.S. declared to reinforce their co-ordination and co-operation with a view to fostering progress in plurilateral negotiations on government procurement, both via the GPA and via expansion of GPA membership.<sup>31</sup> Next, at the 2006 U.S.-EU Summit, the United States and EU declared to take steps to ensure that negotiations on all pending accessions to the GPA were accelerated and to respect all countries that took commitments to start negotiations for accession to the GPA.<sup>32</sup> Again, at the 2007 U.S.-EU Summit, the United States and EU agreed to work together to complete market access negotiations and reach final agreement on the revision to the GPA. They would cooperate to expand membership in the Agreement, in particular to expedite China's accession to the GPA.<sup>33</sup> It can be seen that China's accession to the GPA has been a very important interest focus in government procurement in the EU and the U.S.

On the other hand, the EU and U.S. respectively take actions to foster the course of China's accession. In November 2005, the EU and China signed together the Memorandum of understanding that established a dialogue on government procurement between China and the EU. Later on, in May 2006, they formally launched the first EU-China regulatory dialogue on government procurement in Beijing. The EU also agreed to organise a study tour of Chinese officials from various Chinese ministries around Europe. Since 2005 and with the help of the EU-China WTO technical assistance program, EU-China have organised four conferences on government procurement. The U.S. also

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<sup>31</sup> The European Union and United States Initiative to Enhance Transatlantic Economic Integration and Growth, which is the Press Release on the EU-US Summit, 20 July,2005.

<sup>32</sup> Government Procurement in 2006 U.S.-EU Summit Progress Report on the Economic Initiative.

<sup>33</sup> See Procurement of Key Accomplishments in 2007 U.S.-EU Summit Economic Progress Report.

played an active role in China's commitment to table its initial offer by the end of 2007. In April 2006, after long prodding from the United States, and shortly before Chinese President Hu Jintao met with U.S. President George W. Bush, China announced a number of trade concessions, including a commitment to launch negotiations for China to join, potentially, the GPA.<sup>34</sup>

#### 4.3 Main claims and following step

China's initial offer lists the limited scope and high thresholds, and does not cover procurement by sub-central government entities and state owned enterprises like transportation, infrastructure and the utilities sector. Both the EU and the U.S. are very disappointed by China's initial offer, and push China to improve it.

Aiming at China's initial offer, the current parties mainly present the following claims. First of all, they are disappointed at the widening gap between the initial offer and their expectation. They claim that China should lower the thresholds to a reasonable level, add the procurement entities including sub-central government entities and state sector, and expand the opening of goods, services and construction. One issue of key interest is procurement by the large state and whether or not they should be subject to government procurement rules. On this, the EU stresses that, public entities that exercise a non-commercial activity for the specific purpose of meeting needs in the general interest or public undertakings that operate in a utility sector which has not been liberalized are indeed covered by government procurement legislation. Therefore their view is that China should provide a similar coverage of entities in the forthcoming GPA negotiations. Similarly, the US says all the state-owned, public-interest-oriented enterprises in the US are considered government procurement entities. And due to their engagement in public welfare undertakings, even some private firms are included. According to the Agreement, enterprises whose senior management is appointed by the government, whose annual revenues are reported to the government, and whose businesses are subject to government intervention should be included in the list. In the next place, they think China is not a developing country and should not apply for the special and differential

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<sup>34</sup> U.S. Department of Commerce, U.S. Issues Fact Sheet on Joint Commission on Commerce and Trade Talks with China, U.S. Federal News, July 11, 2005, 2005 WLNR 10906001.

treatment such as trade offset. Therefore, they request that China tables the offer in the light of the level of market opening of the current parties. Finally, they asked China to submit its information of government procurement as soon as possible, in order to facilitate the negotiations.

On the basis of information that has been publicly disclosed, the Government Procurement Advisory Team established by the EU Commission, Member States and European business fully supported the Commission's efforts to substantially improve the Chinese offer in particular in view of extending the coverage (entities and sectors), lowering thresholds (especially for construction), and shortening the 15 years transitory period. They will play a central role in pressing China to improve its offer, speed up public procurement reform process and allow better market access to EU companies, to make sure China finally makes a real market access offer and that its internal government procurement legislation conforms to the GPA. The GP Advisory Team will meet regularly to discuss the best way to persuade China to improve its GPA offer. In parallel, Commission services have already started using existing tools (such as the EU-China regulatory dialogue on government procurement) to engage with the Chinese authorities in cooperation activities and regulatory dialogue so as to encourage them to speed up their Public Procurement reform process and allow better market access to EU companies.<sup>35</sup> In addition, the current parties may probably impose their influences and pressures on China through other relevant political or economic issues. For example, the EU continually pressed China to start-up accession negotiations after China's accession to the WTO through linking the opening market of government procurement with granting China the status of market economy.<sup>36</sup>

## **5. A brief recommendation**

This article analyses the related factors influencing China's accession from trade regulation, the parties and China itself. Hence, a brief recommendation will be given from these three perspectives.

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<sup>35</sup> Peter Mandelson, The "Government Procurement Advisory Team" in China: one of the MAP tools to influence WTO Government Procurement Agreement negotiations European Commissioner for External Trade, market access newsletter, Issue 7 – 31 March 2008, available to [http://trade.ec.europa.eu/doclib/docs/2008/march/tradoc\\_138475.pdf](http://trade.ec.europa.eu/doclib/docs/2008/march/tradoc_138475.pdf).

<sup>36</sup> Owing to referring to significant interests, the analysis of the current parties is confined to the limited information available.

First of all, for the GPA, there is an urgent need to consider how the benefits of accession can be enhanced and the costs minimized. The current improvements to the GPA make it more operational and appear to benefit the current parties more than stimulate further accessions. It can be suggested that there is a need to offer a more flexible approach to developing countries, allowing them to adopt defensive measures for a longer transitional period while at the same time conferring offensive S&DT to enable their increased access to foreign procurement markets. If the GPA does not provide the overspread benefit of the potential gains from the Agreement, it might also not become successful in obtaining overspread adhesion.<sup>37</sup>

In the second place, China should seriously study the negotiating regulation and the requests of the main parties. On the basis of weighing the benefits and costs of accession to the GPA, the government should duly adjust and revise its initial offer to meet the parties' demand. Next, China should revise or adjust the Government Procurement Law to accord with the GPA, and mainly focus on perfecting domestic review procedures for supplier challenges. On the other hand, the government also considers the unification between Government Procurement Law and Invitation and Submission of Bids Law, and constituting detailed regulations related to implementing the government procurement system. Finally, the government should expedite the course of reforming the government procurement regime, and maturing domestic industry during the transition period, and cultivate the professionals, in order to prepare opening the market in government procurement.

Finally, the parties should fully consider the situation and practices of China, and the GPA is a voluntary agreement which leave much room for negotiations. The essential ingredient is the survival of the nation-state as a distinct entity, as autonomous as possible in its international political and economic relations and the conduct of its domestic affairs. Thus it could not finally resolve problems and reach a satisfactory outcome if the parties bring pressure without compromise on the Chinese government in the negotiations. The parties should not only evaluate the benefits of China's accession to the GPA from their own interests, but also consider the costs of accession from China's

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<sup>37</sup> Valeria Guimaraes De Lima e Silva, *The Revision of the WTO Agreement on Government Procurement: to what extent might it contribute to the expansion of current membership*, *Public Procurement Law Review*, 2008, 2, 98.

point of view, giving enough inducements and benefits to facilitate China's accession.

## **6. Concluding remarks**

China's accession to the GPA is inevitable tendency; however, negotiating an international agreement is a long and trying process. China's initial offer is only the first step in the process of accession to the GPA, coverage negotiations will be a hard work, and bring disagreements and difficulties which may probably result in encumbrances to the course of negotiations.

China's accession to the GPA is not simply a trade issue. Rather, it is the result of a complex and interlocking network of bargains that are partly economic and partly political. With respect to the GPA, although the negotiable Articles in the GPA endow the negotiator with stated flexibility, the ambiguities of the Agreement also block the course of negotiations. Especially, if a large state sector of China should be covered by the GPA, this would be a focal problem and most probably main divergence, easily resulting in the stagnation of negotiations. For China, the government would, first of all, weigh the benefits of acceding to the GPA, which must be sufficient to outweigh any costs. China would also insist on the status of developing countries in joining the GPA, of which Israel, South Korea, Singapore and Hong Kong, China, joining the GPA as developing countries, are all good examples. Moreover the government may probably be cautious and conservative based on consideration of the domestic situation and other political and economic factors. As for the main parties, the EU and the USA would use a carrot-and-stick policy to continually strive for more concessions from China by together or solely imposing pressure and influence on China. They may probably connect government procurement with other economic or political issues, such as imposing influences by dint of a political topic for discussion, such as granting China the status of market economy, human rights and the Taiwan issue.

For Susan Strange, "It is the false impression that it is the trade 'regime'—the rules and arrangements agreed between governments—that is a prime determinant of what actually happens. Instead, so-called 'rulebooks' are in reality a rather peripheral influence, reflecting the interests and

bargaining power of the most powerful states on the conduct of the most effective traders.”<sup>38</sup> This is the reason why this article discusses the influencing factor on China’s accession to the GPA from different perspectives, not only from trade regulation. The solution of the problem is to find that balance of interest and power that allows a working set of bargains to be hammered out and observed.

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<sup>38</sup> Susan Strange (1994), *States and Markets*, Second edition 1994, Published by London and Washington, 1994, p166.

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