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March 1, 2010

Mr. Barry O'Neill
President
CUPE BC Division
#510 – 4940 Canada Way
Burnaby, BC
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Dear Mr. O'Neill:

Re: Capital Regional District Wastewater Treatment Program;

And Re: The Agreement between Canada and the United States on Government Procurement

You have asked for my opinion about the effects of new international procurement rules on plans by the Capital Regional District (CRD) of British Columbia to establish sewage treatment works and related facilities. Those rules are set out in a procurement agreement between Canada and the US that went into effect on February 16, 2010 and are the first to require Canadian municipalities to open their procurement markets to foreign bidders.¹

In particular, you have asked for our assessment of how these new international obligations bear upon the choice of procurement options being considered by the CRD for proceeding with a wastewater treatment program (WWTP) for the Capital Region.

OVERVIEW

As of February 16, 2010 and for a period through September, 2011, the CRD is subject to the rules of a Canada-United States procurement agreement (CUPA), which is set out as a number of temporary rules that apply during this period to municipal procurement of construction and related services, including for the projects which comprise the WWTP.

¹ *Agreement Between The Government Of Canada And The Government Of The United States Of America On Government Procurement*, Feb 3, 2010.



These temporary rules impose significant constraints on the manner in which the CRD may procure such services during this period, as well on the terms of those procurements. The CRD is now considering various procurement approaches for proceeding with these projects, which range from a traditional procurement approach to a public-private partnership model under which the design, construction, financing and operation of projects would be contracted to a private consortium. The following analysis provides an overview of the CUPA, and in particular of certain temporary provisions that apply to municipalities, including the CRD procurement.

The key conclusions we draw in this assessment are as follows:

- i) The Canada-US Procurement Agreement is a remarkably one-sided agreement, under which most benefits flow to US companies seeking access to Canadian procurement markets, and this is particularly true for temporary procurement rules that require municipalities to comply with international procurement rules for the first time. Under these rules, the CRD must open procurement for construction and related services to US companies, but US states and municipalities, many of which maintain local preferences that effectively exclude Canadian companies, are under no reciprocal obligation to do the same.
- ii) The constraints imposed by CUPA on CRD procurement options go well beyond those of the Agreement in Internal Trade (AIT) and the Trade Investment and Labour Mobility Agreement (TILMA). Moreover, while the AIT and TILMA exempt procurement relating to water, water related services and the protection of the environment, CUPA rules do not.
- iii) Where CUPA rules apply, they impose significant constraints on the ability of the CRD to use procurement for WWTP projects as a means for achieving important public policy goals including those relating to economic development, environmental protection, green technology, and predictable project management. In particular the temporary agreement on procurement:
 - prohibits the CRD from requiring that construction contractors use some proportion of local or Canadian goods, services or labour in carrying out a WWTP project. This ban on local preferences or content denies the CRD the right to use the public investment in the WWTP to provide “maximum economic benefit to the CRD and British Columbia in terms of jobs and other economic benefits”;
 - prohibits the CRD from using WWTP procurement to support a market for innovative Canadian environmental or energy design and engineering, or for Canadian green technologies. Conversely, CUPA rules may constrain the ability of the CRD to derive the benefits of, or share innovations that emerge from, proceeding with the WWTP; and

- imposes significant new procedural and administrative obligations on the CRD with respect to procurement, and creates a litigation risk arising from the rights US companies have under CUPA to challenge both the method and the terms of certain CRD procurements, and which may result in the suspension of the procurement process or monetary compensation for non-compliance with CUPA rules.
- iv) If the CRD wishes to achieve the goals it has stated for the WWTP it must, where possible, preserve its options to include conditions in procurement contracts relating to sourcing the goods, services and labour needed to carry out the WWTP. To do so, it should choose the procurement approach that best obviates the application of CUPA rules. In this regard, the conventional approach to procurement offers several important advantages over a public-private partnership (P3) model, including by:
- allowing key project functions to be carried out by in-house staff or consultants retained by the CRD rather than as part of a procurement for construction and related services;
 - allowing non-construction services, such as environmental design, energy conservation, and various financial services to be hired or procured separately from any procurement of construction and related services;
 - facilitating the procurement of individual projects and services that may fall below the \$ Cdn 8.5 million threshold for the application of CUPA rules; and
 - adopting a staged approach to procurement that would allow certain construction projects to be procured beyond the September, 2011 date when CUPA expires.
- v) Conversely, because the P3 model contemplates a much larger and comprehensive procurement for WWTP services, goods and technology, it would invite the application of CUPA constraints to a broad array of services and projects that may only tangentially be related to the construction of a WWTP project.

In early February, the CRD published a report in which it identified criteria for choosing among various procurement options for proceeding with the WWTP. Given the advent of CUPA since that report was prepared, and in light of the significant impediments to the realization of WWTP goals engendered by this Canada-US Agreement, it would be prudent in our view for the CRD to carefully consider the constraints imposed by CUPA rules as a criterion for assessing the relative merits of the procurement options it is now considering.

THE CAPITAL REGIONAL DISTRICT WASTEWATER MANAGEMENT PROGRAM

The CRD WWTP is comprised of several elements, including a waste water collection system, two main waste water treatment plants, an energy centre for biogas, waste heat and other energy recovery projects, and resource recovery facilities for biosolids and other waste products. The CRD is now in the process of trying to finalize funding commitments by the provincial and federal governments for the project.

As noted, the CRD has recently released a report describing delivery options for proceeding with the Program (the Options Report).² The Report describes various approaches for procuring the goods, services and labour needed to carry out the WWTP. These range from a conventional design-bid-build approach to a public-private partnership model under which financing, maintenance and operational services may also be contracted for. To guide its choice among these procurement options, the CRD has developed “Preliminary Assessment Criteria”. For the purposes of this assessment, the following criteria are particularly important:

- the ability for the delivery option to provide maximum economic benefit to the CRD and British Columbia in terms of jobs and other economic benefits;
- the complexity and risks associated with the delivery option; and
- the feasibility of the procurement option for implementing CRD’s multi-year, multi-component build-out program.³

The Options Report indicates that the final business case for the WWTP will analyze each procurement method and assess each component of the Program against these and other criteria.

For reasons that are set out below, CUPA rules have a material impact on the likelihood of achieving the goals inherent in the above noted criteria, and when taken into account clearly favour the conventional approach to procurement over the P3 model or some variant thereof.

Before comparing the impact of CUPA rules on these two procurement approaches, we need first to describe how they differ. For this purpose we summarize the Options Report description of these procurement models and how the CRD might utilize them.

² Capital Regional District Core Area Wastewater Management Program Potential Program Delivery Options
January 6th, 2010

³ Idem.

Option A: the Conventional Approach

This conventional approach to procurement would involve the CRD “engaging an Engineering Consultant and Construction Manager at the early project stages to refine the concept design, develop the detailed design and prepare a comprehensive project budget and schedule. ... Construction can start on early work packages on a sequential tender bases ...”

The engineering consultant and/or construction manager prepare the design and contract documents, tender the projects, evaluate the tenders, and enter into multiple trade contracts with suppliers and sub-contractors. The construction manager would have primary responsibility for the performance of the trade contracts and subcontracts, and would be responsible for ensuring the project is brought in on budget.

Option B: the Hybrid Approach

The CRD describes this option as utilizing a variety of procurement methodologies, with the design-build (conventional) approach being used for the wastewater treatment facilities, and the P3 model (see below) for the energy centre and West Shore treatment plant. Conventional procurement is also used for the conveyance system, outfalls and tunnel, and might also be used for some of the treatment facilities.

Because the hybrid approach simply represents some combination of procurement models, the comparative analysis we carry out here only considers the two primary procurement approaches, the conventional and P3 models.

Option C: the PublicPrivate Partnership Approach

There are various forms a P3 project may take. The CRD P3 option would involve contracting for the design, construction, financing, operation and maintenance of WWTP facilities (the DBFO model). The corporate entity that typically responds to a DBFO tender is a consortium incorporated for the purpose of bidding on the project, which is usually comprised of investors; financial brokers; design, engineering and construction firms; and companies that specialize in managing and operating the facilities being contracted for. Each of these parties may have their own counterparties and subcontractors. The multi-party corporate arrangements among members of the consortium, and between the consortium and the public partner, are set out in highly sophisticated and complex contracts that routinely span decades.

CUPA rules contemplate these complex schemes by specifying that it covers procurement for government purposes of construction services “by any contractual means, including: purchase; lease; and rental or hire purchase, with or without an option to buy”.

The CRD describes the P3 option as using a DBFO approach for the treatment plants, energy centre and resource recovery facilities. The CRD further describes this option as involving “one large DBFO procurement package” for the core area components of the WWTP, with a separate

DBFO for the West Shore plant. The conveyance system, pumping stations, outfalls and tunnel would be procured using a conventional procurement model.

The Canada-US Procurement Agreement (February, 2010)

A little more than week after it was concluded, the Canada-US Procurement Agreement (CUPA) went into effect on February 16, 2010. The Agreement, which became public when it was leaked to civil society groups merely days earlier, is comprised of three elements:

- i) provincial and territorial procurement commitments under the General Procurement Agreement (GPA) of the World Trade Organization (WTO) for all provinces and territories (except Nunavut) in exchange for U.S. sub-federal GPA commitments (to which 37 states have made commitments);
- ii) temporary⁴ Canadian procurement commitments for construction projects for some provincial/territorial agencies and for a significant number of municipalities, in exchange for the U.S. exempting Canada from the “Buy American” provisions of the *Recovery Act* for seven (7) federal programs; and
- iii) a commitment to explore the scope for a long term government procurement agreement between Canada and the U.S., within the next 12 months, to deepen on a reciprocal basis, procurement commitments beyond those in the WTO GPA and NAFTA.

The temporary agreement is particularly important because until now provincial and municipal governments have not had to comply with international procurement rules. Provinces/territories have declined to undertake such obligations because of concerns regarding the U.S. carve-out for mass transit and highway projects, and U.S. federal set-asides for small and minority business, both of which impede Canadian access to U.S. procurement opportunities.⁵ Remarkably, and as noted below, these U.S. exclusions under international procurement rules are essentially unaltered by the CUPA.

The commitment to future negotiations is also relevant to municipal governments, but for present purposes our focus is on the temporary procurement commitments Canada has made because these now apply to municipalities, including the CRD, and have already gone into effect.

⁴ The temporary Canadian procurement offer was scaled back to construction services only to counter the effect of the time delay in reaching agreement with the U.S. on the scope of *Recovery Act* program exemptions and that, in some of the programs, a significant portion of the contract dollars have already been issued.

⁵ See the Backgrounder to CUPA that accompanied the deal at the time of its release.

Temporary Canadian Procurement Commitments

Part B of CUPA sets out the terms of the Temporary Agreement on Enhanced Coverage (TAEC). Article 6 of this scheme provides that:

1. *Canada shall provide access to sub-federal procurement of construction services to the United States in accordance with Appendix C of this Agreement. For greater certainty, this includes all U.S. iron, steel and manufactured goods used in a construction project, unless otherwise noted.*
2. *This Article shall remain in force through September 30, 2011.*

Appendix C sets out the scope of the temporary regime, which covers construction services contracts with a value greater than \$ Cdn 8,500,000. Part B of the Appendix sets out certain exceptions for measures relating to aboriginal peoples and for promoting development in distressed areas.⁶ It also list the provincial entities to which the Agreement will apply, and in this regard British Columbia has gone further than any other province or territory is providing that:

All Crown Corporations and all municipalities are covered.

Part B also sets out the substantive obligations and procedures of the procurement regime to which municipalities must now adhere. These preclude according favourable treatment to local contractors or those providing goods and services to such contractors. Governments are also prohibited from seeking “offsets”, even where these are imposed on an entirely non-discriminatory basis.⁷

An offset in government procurement is:

*. . . a measure used to encourage local economic development by means such as domestic content requirements or the obligation to set aside some portion of the procurement contract for local services or labour.*⁸

As noted below, offsets and set-asides are in widespread use in the United States, and they will largely remain in force against Canadian suppliers and service providers under CUPA. Thus,

⁶ Subsections 2 and 3 of App. “C” Part A also set out several exceptions to these obligations, none of which are relevant to the RD present project.

⁷ S. 6 stipulates that: *With regard to covered procurement, provinces and territories will not seek, take account of, impose or enforce any offset.*

⁸ “Offset” is defined by App. “C” Art. 23 to mean “any condition or undertaking that encourages local development such as the use of domestic content, the licensing of technology, investment, counter-trade and similar action or requirement”.

under these rules the CRD cannot require, for example, that the successful bidder for a construction contract hire or source goods and services locally.

In return for these Canadian commitments under TAEC the US agrees to remove certain “buy American” conditionality to US stimulus spending. Article 7 provides:

The United States shall modify its Annex 3 of Appendix I of the GPA by listing seven programs under List C and providing that with respect to those programs, the domestic purchasing requirement of section 1605(a) of the American Reinvestment and Recovery Act of 2009 will not be applied as a condition of financing those programs with respect to Canadian iron, steel, and manufactured products in procurement above the Annex 3 threshold for construction services through September 30, 2011. The United States shall include such modifications in its notification to the WTO Committee on Government Procurement, as set out in Appendix B to this Agreement.

The One-sided Nature of the CUPA

It may not be readily apparent from these provisions how truly one-sided the TAEC bargain is. According to an uncontroverted assessment carried out by the Canadian Centre on Policy Alternatives (the CCPA), even if taken at face value, Canadian companies will gain access to only a small portion of US stimulus spending under CUPA.⁹ In return, Canada offers US companies unfettered access to many times the value of Canadian public procurement. By the CCPA assessment, Canadian suppliers have a brief opportunity to compete for an estimated \$US 4–5 billion of federally funded stimulus projects, representing less than 2% of the approximately \$US 275 billion of procurement funded under the *Recovery Act*,¹⁰ but even then subject to several qualifications and exclusions that greatly reduce even this modest access to US procurement.

Consider, for example, that under Article 7 of CUPA, the US only agrees to modify its WTO procurement commitments by:

*“listing seven programs ... and providing that with respect to those programs, the domestic purchasing requirement of section 1605(a) of the American Reinvestment and Recovery Act of 2009 will not be applied as a condition of financing those programs with respect to Canadian iron, steel, and manufactured products in procurement”*¹¹
[emphasis added]

⁹ CCPA, “Buy American Basics” Feb. 2010.

¹⁰ Ibid, p. 1.

¹¹ Sec. 1605. Use of American Iron, Steel, and Manufactured Goods.

(a) None of the funds appropriated or otherwise made available by this Act may be used for a project for the construction, alteration, maintenance, or repair of a public building or public work unless all of the iron, steel, and manufactured goods used in the project are produced in the United States.

In other words, under CUPA the US is only agreeing to remove the stipulation that as a condition of federal funding states and local governments must only purchase US iron, steel and manufactured products. But most US offsets, set-asides and local preferences are established at the state and local level, and as noted under CUPA, these would remain in place.¹²

This means that while the US has agreed to remove domestic purchasing requirements as a condition for funding under the 7 federal programs, it does not commit to have state and local governments remove their own barriers to Canadian bids on the very projects funded by the seven listed federal programs referred to, and state level restrictions on Canadian bids are often more onerous than those set out in the federal programs.

In other words, while Canadian provinces and municipalities are obliged to open their procurement markets to US bidders for construction services, US states and municipalities are under no reciprocal obligation. This means that a construction company based in Seattle, Portland, Anchorage, or anywhere else in the US is entitled to bid for CRD procurement for construction but Canadian companies have no similar rights to bid on US projects.

Moreover, as stipulated in attachments to CUPA, even the limited waiver it offers with respect these seven federal programs would apparently not apply to projects carried out by governments in thirteen states that have made no commitments under the WTO, including Alaska.¹³ But most

(b) Subsection (a) shall not apply in any case or category of cases in which the head of the Federal department or agency involved finds that—

- (1) applying subsection (a) would be inconsistent with the public interest;
- (2) iron, steel, and the relevant manufactured goods are not produced in the United States in sufficient and reasonably available quantities and of a satisfactory quality;
- or
- (3) inclusion of iron, steel, and manufactured goods produced in the United States will increase the cost of the overall project by more than 25 percent.

(c) If the head of a Federal department or agency determines that it is necessary to waive the application of subsection (a) based on a finding under subsection (b), the head of the department or agency shall publish in the Federal Register a detailed written justification as to why the provision is being waived.

(d) This section shall be applied in a manner consistent with United States obligations under international agreements.

¹² Under CUPA, the US would not modify State or municipal commitments under the WTO procurement agreement, and under that agreement states have preserved their rights to impose local preferences and offsets, and 13 states have made no commitments under the WTO GPA.

¹³ Except as specified otherwise in this Appendix, procurement in terms of U.S. coverage does not include non-contractual agreements or any form of government assistance, including cooperative agreements, grants, loans, equity infusions, guarantees, fiscal incentives, and governmental provision of goods and services to persons or governmental authorities not specifically covered under U.S. annexes to this agreement.

importantly for the sake of this comparative analysis, US municipalities are simply not subject to international procurement rules under NAFTA, the WTO, or CUPA.

Yet another asymmetry between US and Canadian obligations under CUPA is that the US has committed to removing federal purchasing preferences for iron, steel and other manufactured products. Canada, on the other hand, has committed to opening its procurement markets to all construction contracts, including the goods (iron, steel and other products) and the services related to these contracts.

Finally in this regard, Canada must establish dispute and judicial review procedures to provide US companies with a remedy, including the right to claim compensation, should they believe that the CRD or other Canadian government has failed to comply with CUPA requirements. The US is under no similar or other obligation to establish dispute procedures for the purpose of providing an aggrieved Canadian company with recourse if their putative rights to bid on US contracts is frustrated or denied.

British Columbia's US Neighbours

To illustrate the practical reality under CUPA, consider for example Oregon procurement rules that establish a number of mandatory procurement preferences for Oregon goods and services, including the following:

(2) For the purposes of awarding a public contract, a contracting agency shall:

(a) Give preference to goods or services that have been manufactured or produced in this state if price, fitness, availability and quality are otherwise equal; and

(b) Add a percent increase to the bid of a nonresident bidder equal to the percent, if any, of the preference given to the bidder in the state in which the bidder resides.¹⁴

Washington State allows a premium to be paid for local goods and services, and while it has established reciprocity with respect to procurement in relation to other States, this reciprocity does not apply to Canada, and the State has no obligation to match Canadian concessions under the temporary rules of CUPA.¹⁵

Alaska maintains a broad array of local preferences for lumber, fisheries products and other goods harvested or produced in the State. It also imposes other preferences and restrictions on most state procurement. For example, the following general rule applies to state contracts:

¹⁴ Oregon Revised Statutes 2007 <http://www.leg.state.or.us/ors/home.htm>
Volume 7. Title 26. Public Facilities, Contracting and Insurance Chapter 279A. Public Contracting - General Provisions.

¹⁵ Government of Canada, U.S. State Procurement Preferences <http://www.canadainternational.gc.ca/sell2usgov-vendreaugouvusa/opportunities-opportunitites/opportunities-debouches.aspx?lang=eng>

(b) The procurement officer shall award a contract based on solicited bids to the lowest responsive and responsible bidder after an Alaska bidder preference of five percent, an Alaska products preference, and a recycled products preference In this subsection, "Alaska bidder" means a person who

- (1) holds a current Alaska business license;*
- (2) submits a bid for goods, services, or construction under the name as appearing on the person's current Alaska business license;*
- (3) has maintained a place of business within the state staffed by the bidder or an employee of the bidder for a period of six months immediately preceding the date of the bid;*
- (4) is incorporated or qualified to do business under the laws of the state, is a sole proprietorship and the proprietor is a resident of the state, or is a partnership and all partners are residents of the state; and*
- (5) if a joint venture, is composed entirely of ventures that qualify under (1) - (4) of this subsection.*

None of these qualifications and restrictions maintained by British Columbia's US neighbours are affected by CUPA, even though Canadian municipalities are prohibited from adopting similar measures. Moreover, because Alaska has made no commitment under the WTO procurement agreement, even the limited waiver of federal "buy American" provisions would not apply to projects in Alaska carried out with federal funding.

Buy America vs. AIT and TILMA procurement rules

It is beyond the scope of this opinion to provide a detailed comparison of TILMA, AIT and CUPA obligations, but there are many significant differences between these regimes, some of which are relevant to the choice of procurement options for the WWTP. We note these briefly here.

Reciprocity

First, while all three regimes apply to municipal procurement of construction services, TILMA and AIT rules are reciprocal. This means, for example, that municipalities in Alberta have the same obligation to open their procurements markets to BC companies, as do BC local governments to solicit tenders for Alberta companies. As we have seen, this is not the case under CUPA.

Preferences for Canadian Companies and Workers

Second, under both the AIT and TILMA,¹⁶ the CRD would be able to restrict procurement to Canadian companies, or if allowing US companies to bid, establish a preference for Canadian goods and services. As framed by AIT rules such a preference is permitted in this manner:

Canadian Content

1. Entities covered by this Annex may accord a preference for Canadian value-added, provided that the preference is no greater than 10 percent.

2. An entity covered by this Annex may limit its tendering to Canadian goods or suppliers, provided the procuring entity is satisfied that there is sufficient competition among Canadian suppliers and the requirement for Canadian content is no greater than necessary to qualify the procured good as a Canadian good.¹⁷

Exceptions:

Both TILMA and the AIT allow exceptions for measures established to achieve a “legitimate objective”, a term defined under these domestic agreements¹⁸ to include measures for:

- (d) protection of the environment;*
- (e) consumer protection;*
- (f) protection of the health, safety and well-being of workers; ...*

CUPA includes no similar exceptions.

¹⁶ TILMA of course establishes reciprocal procurement obligations only in favour of companies from those two provinces.

¹⁷ AIT Annex 502.4

¹⁸ See Article 404 which defines “legitimate objective” to mean any of the following objectives pursued within the territory of a Party:

- (a) public security and safety;
 - (b) public order;
 - (c) protection of human, animal or plant life or health;
 - (d) protection of the environment;
 - (e) consumer protection;
 - (f) protection of the health, safety and well-being of workers; or
 - (g) affirmative action programs for disadvantaged groups;
- considering, among other things, where appropriate, fundamental climatic or other geographical factors, technological or infrastructural factors, or scientific justification.

Most important for present purposes, however, is the exception in TILMA and AIT for “water, and services and investments pertaining to water”.¹⁹ In our view, this exception would include waste water management or treatment services as services “pertaining to water”. There is no similar exemption in CUPA temporary agreement rules for water related services.

CUPA also has more onerous dispute procedures which not only allow for monetary sanctions, but also interim orders suspending the procurement process. Finally, BC can extricate itself from the commitments it has made under the AIT and TILMA by invoking the provisions of those agreements that empower provincial governments to retreat from their obligations. But CUPA contains no similar provision, and provincial governments have no constitutional authority to rescind international treaty obligations which the federal government may make on their behalves.

There are also important distinctions between these regimes that allow the CRD greater latitude for action under CUPA than is the case for its domestic analogues. The two most important of these are that i) CUPA is limited to construction and related services, and ii) the monetary threshold for engaging the application of CUPA rules is much higher. For the reasons set out below, both of these differences bear upon the choice of procurement option for the present CRD project.

In sum:

For present purposes, the most significant distinction between CUPA and domestic procurement rules is that only the former applies to water related services, which in our view would include the wastewater management services that comprise the CRD plan. However, even if we are wrong in this point, there are several significant points of departure of between CUPA and AIT and TILMA rules. While higher CUPA thresholds allow greater procurement flexibility for smaller projects, where all three regimes apply, CUPA obligations are far more constraining of government procurement authority than is the case under domestic Canadian procurement rules.

ANALYSIS

From the preceding description of CUPA rules, it may already be apparent that their unalloyed application to procurement for WWTP projects will make it very difficult for the CRD to achieve some of its stated objectives, while at the same time creating new risks for the procurement process. Fortunately, there are ways to mitigate some of the risks associated with the application of CUPA rules. To underscore the importance of adopting strategies to mitigate CUPA risks, it is important to understand how CUPA rules are likely to undermine the achievement of important WWTP goals. Accordingly, we begin with that.

¹⁹ PART V Exceptions To The Agreement and see AIT 1102(3).

CUPA rules preclude procurement preferences that are key to maximizing WWTP economic benefits to the CRD and BC

As noted, the CRD has identified maximizing local and provincial economic benefits as a criterion for choosing among the delivery options available to it. As noted, however, CUPA rules prohibit the CRD from requiring that bidders agree to source services or hire workers from within the province or Canada. In the jargon of international trade agreements, this prohibition on seeking local economic benefits is expressed as a ban on offsets which the CRD is not permitted to “seek, take account of, impose or enforce ...”²⁰

Yet the use of local procurement preferences to stimulate economic development is one of the most important public policy tools used by government for creating jobs and stimulating the economy. This is, of course, the rationale for the “buy American” provisions of US state and federal laws which CUPA was ostensibly negotiated to remove but which, as we have seen, it almost entirely fails to do.

Nevertheless, the Temporary Agreement prohibits the CRD from adopting such preferences, thereby denying it what is arguably the most effective means at its disposal for ensuring that implementation of the WWTP provide “maximum economic benefit to the CRD and British Columbia in terms of jobs and other economic benefits”.

It is important in this regard to appreciate the scope of the measures that are prohibited under the CUPA scheme. As noted, “offset” is defined to mean:

any condition or undertaking that encourages local development such as the use of domestic content, the licensing of technology, investment, counter-trade and similar action or requirement. [emphasis added]

The list of prohibited measures set out by this definition is illustrative not comprehensive. The key phrase (underlined) explicitly prohibits *any* government action that encourages local development – not just economic development, but any development. Certainly any preference for local or Canadian companies, service providers, materials, or workers would run afoul of this prohibition. But measures that have no discriminatory intent might also offend this prohibition if they effectively put a US supplier in a less advantageous position than a Canadian competitor. For example, a preference for recycled building materials might favour BC sources if such materials could not readily be imported to Canada and therefore offend the prohibition on requiring materials to be locally sourced. Similarly, requirements relating to energy efficiency or the use of renewable energy could be assailed for favouring BC power producers.

²⁰ CUPA, App. “C”, Part A:6.

In fact, the prohibition on offsets of any kind or description is problematic if CRD goals relating to environmental sustainability are to be realized. We consider some aspects of this problem next.

CUPA Rules as an Impediment to Realizing CRD Goals Concerning Environmental Innovation

A related problem exists with respect to CRD goals that the WWTP fosters and serve as a model for environmental innovation with respect to the management of wastewater.²¹ In this regard, the WWTP is seen by the CRD as an important means for “integrating wastewater management into sustainable water, stormwater, solid waste and energy planning for the community.” For practical applications of wastewater treatment resources, the possibilities are endless.”²²

As we know, public procurement has often been used to promote domestic innovation, and this is certainly the case for Canadian high tech industries, including green energy technology. Thus the WWTP could provide a means to maximize economic benefits to the CRD, the Province and Canada by providing a market for innovative Canadian environmental and energy engineering services and technologies.

But as noted, under CUPA rules, the CRD is prohibited from including “offsets” in construction procurement contracts for the purpose of encouraging local development “such as the use of domestic content, ... [or] licensing of technology...” This rule clearly precludes procurement terms that would require any bidder to source environmental engineering services or technologies from Canadian providers.

Furthermore, this prohibition would arguably also preclude any requirement that a US bidder transfer or share intellectual property or technology that arises from the procurement. Yet the CRD is promoting its wastewater treatment program as offering an important opportunity for it to “demonstrate leadership in the field of wastewater treatment and beneficial reuse, and also aim for carbon neutrality,” and to share the lessons it learns. It puts that commitment this way:

The CRD is following an open and transparent process with all research, analysis and methodologies available to the public and other governmental agencies through the CRD project website at www.wastewatertreatment.ca/media/archived-documents. This website includes extensive archival libraries of helpful analysis. CRD has also hosted other public sector agencies interested in implementing similar types of wastewater

²¹ As noted by the CRD business case “... the CRD is committed to implementing a large number of sustainability initiatives in these Programs. The CRD will demonstrate leadership in the field of wastewater treatment and beneficial reuse, and also aim for carbon neutrality.” [G.5 Resource Recovery And Carbon Neutrality - business case]

²² <http://www.wastewatertreatment.ca/environment/benefits.htm>

*projects, including parties from the USA. The CRD is committed to sharing its research with all interested parties.*²³

The openness that has characterized CRD planning to date is very likely to be impeded where CUPA rules are engaged. For example, the process of innovation often generates intellectual property in the form of new design and technology. If the CRD and other communities are to benefit from these advances, technological developments that arise from the project must be transferable.

For these reasons, the prohibition on any procurement condition that seeks to foster economic development, including measures relating to technology licensing, can certainly be seen as an impediment to realizing CRD goals related to using the WWTP to foster environmental innovation in Canada. In this regard, it is important to recall that unlike the AIT and TILMA, TAEC includes no exception for measures relating to environmental protection.

CUPA Rules Increase the Complexity and Costs of the Procurement Process

As noted, CUPA rules impose a number of procedural and substantive requirements on the CRD with which it would have no experience. Among these are requirements that the procurements be posted in manner that provides US bidders with equal access to CRD tenders. Tender documents must be formulated to conform with detailed CUPA rules, and the CRD is likely to be called upon to assess a greater number of proposals from US construction companies.

CUPA rules also require the Province to establish dispute procedures for US suppliers that wish to complain a Canadian government failed to comply with its obligations under the Agreement. S.16 provides:

Provinces and territories will provide a timely, effective, transparent and non-discriminatory administrative or judicial review procedure through which a U.S. supplier may challenge a covered procurement for failure to conduct a covered procurement in accordance with this Appendix, in which the U.S. supplier has, an interest. (s. 16)

Under these rules, the CRD is obliged to accord timely and impartial consideration to any complaint, and will generally also be required to respond in writing and disclose all relevant documents to the administrative or judicial body that has authority to determine such complaints and the authority to order corrective action or compensation where procurement rules have not been observed. The provincial government is also obliged to establish interim measures to preserve the interests of a US bidder, including the suspension of the procurement process.

²³ *Business Case in Support of Funding Under the Infrastructure Canada Building Canada Fund - Major Infrastructure Component*, December 9, 2009, p. 38.

CUPA RULES: CONVENTIONAL vs. P3 PROCUREMENT

As we have seen, the application of CUPA rules imposes serious constraints on the ability of the CRD to establish procurement terms and the relationships that are needed to achieve important WWTP goals. In light of these constraints, the CRD must obviously consider CUPA rules in deciding among procurement options for proceeding with WWTP projects.

As the following analysis reveals, when CUPA rules are taken into account, it is clear that the conventional approach to procurement allows the CRD much greater scope for structuring WWTP procurement to avert the application of the constraints imposed by this Canada-US agreement. In doing so, the CRD can maintain its prerogatives to fashion the terms of a procurement contract to achieve the economic and environmental goals it has identified for the WWTP.

We should point out, however, that averting the application of CUPA rules does not mean the CRD would necessarily close procurement to US bidders. It might, for example, decide to open procurement for construction or other services to US companies, but stipulate that certain materials, technologies, services or workers be sourced or hired in BC or Canada. Obviating the application of CUPA rules simply allows the CRD flexibility to structure and/or condition procurement as it considers best for achieving its objectives.

Direct Employment/Retainers vs. Procurement

The conventional approach allows key project functions to be carried out directly by CRD staff or by individuals it may hire or retain for that purpose. For example, the CRD Options Report explains that under a conventional procurement approach, an engineering consultant and/or construction manager would be responsible for creating an overall project design, tendering for its various components, and overseeing the project as it proceeds.

The Options Report describes two variations of this approach:

The CMAR [Construction Management at Risk] approach would involve the CRD engaging an Engineering Consultant and Construction Manager at the early project stages to refine the concept design, develop the detailed design and prepare a comprehensive project budget and schedule. Through a competitive process the owner would hire a construction manager on a fee basis to work with the engineer to provide preconstruction services including constructability, innovation, schedule and cost estimating input as the design progresses. Construction can start on early work packages on a sequential tender bases ...

The construction manager would tender each package and enter multiple trade contracts with suppliers and sub-contractors ...

Under a design bid build approach the CRD engages an engineering consultant to prepare the design and contract documents. The consultant tenders the project, evaluates

tenders and administers the construction contract. Under this arrangement the Owner assumes risks for unknowns or design omissions. [emphasis added]

What is key to these approaches is that either lends itself to the consulting engineer and/or construction manager being hired or retained outside a procurement framework. This would allow the CRD various options not permitted under CUPA, including the right to hire BC residents familiar with the local construction industry, services and/or workforce for these positions. The CRD would also be free to give direction that in carrying out their work, these professionals should endeavour to optimize economic benefits to the region and Province, and do so in a manner that promotes innovative environmental and energy design and technology.

By contrast, under the P3 approach the work of the engineering consultant and construction manager would simply be constituent elements of “one large procurement package” for the construction of WWTP facilities and therefore subject to CUPA constraints.

Isolating Non- construction Services

Another advantage of conventional procurement is that it allows non-construction services to be isolated from construction contracts²⁴ so they can be carried out or procured outside the CUPA framework. This is important because under the heading *National Treatment and Non-Discrimination* Article 4 provides:

With respect to any measure regarding covered procurement, provinces and territories will accord immediately and unconditionally to the goods and services of the United States that are included in a procurement of construction services and to the suppliers of the United States offering such goods or services that are included in a procurement of construction services, treatment no less favourable than the treatment provinces and territories accords to domestic goods, services and suppliers. [emphasis added]

A DBFO P3 would include a variety of non-construction services such as environmental and energy consulting services, project management and operational services, and various financial services. Under the conventional procurement model, none of these services, or the goods and subcontracts associated with them, would be subject to CUPA rules. However bundled together in a P3 scheme, all would likely to be considered “goods and services ... included in the procurement of construction services...” and therefore subject to CUPA rules.

For example, if the CRD was to stipulate in a tender call for an energy centre that certain environmental design work be carried out by a BC or Canadian firm, it would be exposed to a

²⁴ Construction services are defined under CUPA as “a contract which has as its objective the realization by whatever means of civil or building works, in the sense of Division 51 of the Central Product Classification. For greater certainty, this includes all U.S. iron, steel and manufactured goods used in a construction project, unless otherwise noted.”

complaint that it had effectively discriminated against a US construction company that was part of the DBFO P3 proposal for that facility.

It is certainly unclear how expansively the provisions of CUPA will be construed, but underestimating the application of these rules could be very costly because under the regime the CRD could be obliged to compensate an unsuccessful bidder for running afoul of CUPA rules. Therefore, the prudent course would be to assume that one large DBFO procurement package would invite the application of CUPA rules to all the goods, services and labour involved, whether relating to overall project management, design, construction, insurance, financing, energy and resource recovery, or facility operations.

Increasing the number of Procurement Contracts With a Value of Less Than 8.5 Million

The threshold for application of TAEC rules is \$Cdn 8.5 million. As noted, under the conventional model, the construction manager would “tender each package and enter multiple trade contracts with suppliers and subcontractors ...” Given the diversity of services and number of projects involved, many of these contracts may be for amounts below the CUPA threshold. A large P3 contract would not, and even in the hybrid scenario the value of the diverse services necessarily involved in a DBFO P3 would inevitably exceed the \$8.5 million.

Staging Procurement for Elements to Fall Outside the CUPA Window

The Temporary Agreement expires on September 30, 2011. The conventional approach to procurement lends itself to staging WWTP projects in manner that could delay tendering for some construction services beyond this CUPA termination date. As noted, under the conventional procurement approach, the CRD describes construction projects proceeding on a “sequential tender bases”. By contrast, P3 project implementation would take place under “one large DBFO procurement package ... for the core area components ...”

Here again the conventional approach to procurement allows the CRD flexibility with respect to planning for the implementation of the Program in a manner that mitigates the application of CUPA rules.

CONCLUSION

Having summarized our key conclusions in the introduction to this opinion, we will not repeat that exercise here. Our analysis of the CUPA agreement and its impacts on municipal procurement describes some of the serious constraints imposed by the regime on the authority of local governments to use public spending as a tool for fostering community economic development or for achieving environmental, resource conservation and other important goals.

Fortunately, the direct impact of CUPA rules on municipal procurement authority is limited to construction services and expires in September, 2011. We trust that this assessment will underscore the need for the utmost due diligence before any further international procurement commitments could be responsibly considered.

Please let us know if you have any questions.

Sincerely,



Steven Shrybman

SS/lbr