EMPOWERING SMALL AND MEDIUM-SIZED ENTERPRISES IN PUBLIC PROCUREMENT

by

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Abstract

With SMEs playing a vital role in the economy and society, and public procurement representing substantial market opportunities, governments increasingly recognise the importance of facilitating SME participation in public procurement. However, the design of supportive measures, referred to as SME-friendly measures, remains contested, particularly regarding their effectiveness in achieving the intended objectives and their potential trade-offs with other objectives, such as value for money, efficiency, non-discrimination, and competition in a public procurement system. This thesis examines such measures in public procurement law, analysing the barriers hindering SME participation, how effectively different measures address these barriers, and what trade-offs arise in practice.

The analysis focuses on four legally binding SME-friendly measures: dividing large contracts into lots, managing the qualification process, bid preferences, and reserved contracts. Examples are drawn from four jurisdictions where these measures have been most extensively developed: the European Union, the United States, Brazil, and South Africa. These measures are distinguished by their nature, with the first two representing facilitative approaches that reduce barriers without granting competitive advantages, whilst the latter two are preferential measures that explicitly favour SMEs in procurement procedures.

The findings reveal that whilst SME-friendly measures can effectively address certain entry barriers, their success depends critically on careful legal design and robust implementation. The thesis demonstrates that the selection and combination of measures depend on specific jurisdictional objectives and market dynamics: facilitative measures prove more effective where SMEs face procedural barriers to entry, whilst preferential measures may be more effective in markets where SMEs struggle to compete despite participation. Furthermore, this thesis establishes that SME-friendly measures do not necessarily compromise other objectives of public procurement and may enhance competition and value for money when calibrated carefully. Accordingly, the thesis identifies key considerations for legislators and policymakers, offering guidance on selecting, combining, and calibrating SME-friendly measures within specific public procurement systems.

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List of Abbreviations

BIS	Best-in-Class (US)
BBBEE	Broad-Based Black Economic Empowerment (South Africa)
CCP 2019	Code de la commande publique (Public Procurement Code) (France)
CFR	Code of Federal Regulations (US)
CMP 2006	Code des marchés publics (Public Procurement Code) (France)
CICA	Competition in Contracting Act of 1984 (US)
COC	Certificates of Competency (US)
DoD	Department of Defense (US)
EME	Exempted Micro-Enterprise (South Africa)
EU	European Union
FAR	Federal Acquisition Regulation (US)
GAO	Government Accountability Office (US)
GPA	Agreement on Government Procurement
GWAC	Government-Wide Acquisition Contract (US)
GWB	Gesetz gegen Wettbewerbsbeschränkungen (Act Against Restraints of Competition) (Germany)
HUBZones	Historically-Underutilized Business Zones (US)
IDIQ	Indefinite Delivery, Indefinite Quantity contract (US)
MAC	Multiple Award Contract (US)
MEEQR	Measure Having Equivalent Effect to Quantitative Restrictions (EU)
MSE	Micro and Small Enterprise
MSME	Micro, Small and Medium-sized Enterprise
NMR	Non-Manufacturer Rule (US)
NSBA	National Small Business Act 102 of 1996 (South Africa)
OIG	Office of Inspector General (US)

OLG	Oberlandesgericht (Germany)
OMB	Office of Management and Budget (US)
PPPFA	Preferential Procurement Policy Framework Act 5 of 2000 (South Africa)
PPA 2024	Public Procurement Act 28 of 2024 (South Africa)
QSE	Qualifying Small Enterprise (South Africa)
SAT	Simplified Acquisition Threshold (US)
SBA	Small Business Administration (US)
SDVOSB	Service-Disabled Veteran-Owned Small Business (US)
SME	Small and Medium-sized Enterprise
SPP	Sustainable Public Procurement
SUM	Spending under Management (US)
TFEU	Treaty on the Functioning of the European Union (EU)
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
US	United States
USC	United States Code
UVgO	Unterschwellenvergabeordnung (Below-Threshold Procurement Ordinance) (Germany)
VgV	Vergabeverordnung (Procurement Ordinance) (Germany)
WOSB	Women-Owned Small Business (US)
WTO	World Trade Organization

Chapter 1 Introduction

1.1 Introduction

Although levels of economic development vary across countries, most economies are characterised by a large number of small and medium-sized enterprises (SMEs), which constitute the majority of businesses.[1] The World Bank estimates that SMEs account for approximately 90 per cent of businesses and provide more than half of employment worldwide.[2] In the European Union (EU), they make up 99.8 per cent of businesses and 65.1 per cent of employment in the non-financial business sector.[3] In the United States (US), small businesses created 20.2 million net new jobs between January 1995 and June 2023, compared with 12.8 million created by large businesses.[4] Governments support SMEs for a variety of economic, political, and social reasons.[5] From an economic perspective, such support is often linked to benefits for the local or national economy, job creation, and entrepreneurship.[6] Politically, SMEs represent a broad and geographically dispersed constituency, and

[1] The definition of SMEs, or small businesses vary across countries, see Chapter 2 for a discussion on SME definition and size criteria.

[2] World Bank Group, 'Small and Medium Enterprises (SMEs) Finance': <https://www.worldbank.org/en/topic/smefinance> accessed 10 February 2022.

[3] European Commission, *Annual Report on European SMEs 2024/2025* (SME Performance Review 2024/2025, Publications Office 2025) <https://data.europa.eu/doi/10.2760/7714438> accessed 6 June 2025.

[4] US Small Business Administration (SBA) Office of Advocacy, 'Frequently Asked Questions About Small Business, 2024' (23 July 2024) <https://advocacy.sba.gov/2024/07/23/frequently-asked-questions-about-small-business-2024/> accessed 6 June 2025. While the term 'SME' is. not widely used in the US, 'small business' is a commonly used term with a specific legal definition. However, its coverage is similar to that of SMEs, as discussed in Chapter 2, Section 2.3.

[5] SME support is typically a form of national industrial policies. See Wolfram Eisner and John Groenewegen (eds), *Industrial Policies After 2000* (Springer Dordrecht 2000) 285.

[6] Anthony Flynn, 'Investigating the Implementation of SME-Friendly Policy in Public Procurement' (2018) 39 Policy Studies 422. Whether SMEs represent entrepreneurship or not is a contested issue in economics, but it is not the focus of this thesis. For further discussion, see Allan A Gibb, 'SME Policy, Academic Research and the Growth of Ignorance, Mythical Concepts, Myths, Assumptions, Rituals and Confusions' (2000) 18 International Small Business Journal 13.

their success is closely linked with local economies and electoral concerns.[7] From a social perspective, supporting SMEs is regarded as supporting individuals who own these small businesses, such as those from minority groups or those who have faced discrimination in the past.[8]

Beyond national borders, supporting SMEs is also seen as a crucial component of the broader agenda of sustainable development, which is a global endeavour to balance economic, social, and environmental priorities for present and future generations.[9] The United Nations (UN) Sustainable Development Goals (SDGs), adopted in 2015, provide a universal framework for achieving this balance.[10] Among the three pillars of sustainability: social, economic, and environmental, supporting SMEs is directly linked to the first two and indirectly linked to the environmental pillar.[11] SDG 8.3 explicitly calls for policies that promote the formalisation and growth of SMEs to contribute to inclusive economic growth and full employment, and SDG 9.2 emphasises that increasing SMEs' access to financial services and their integration into value chains

[7] Andrea Mangani, 'Bipartisan Support for Small Businesses: Statements by Politicians and Legislative Measures in Italy between 1996 and 2018' [2023] Piccola Impresa / Small Business <https://journals.uniurb.it/index.php/piccola/article/view/3439> accessed 22 June 2025.

[8] For example, in the US, the beneficiary of set-aside programmes includes women-owned small businesses, veteran-owned small businesses, historically underutilised business zones (HUBZone) small businesses, and small disadvantaged businesses. The objective of these programmes is to support individuals who own those businesses, or in the HUBZone small business case, to support the local economy where they are located. See Chapter 7 for an analysis on set-aside programmes (reserved contracts) in US federal procurement.

[9] See United Nations (UN), Transforming our world: the 2030 Agenda for Sustainable Development (21 October 2015) UN Doc A/RES/70/1; United Nations Department of Economic and Social Affairs (UNDESA), 'Micro-, Small and Medium-sized Enterprises (MSMEs) and their Role in Achieving the Sustainable Development Goals' (UNDESA 2021) <https://sdgs.un.org/sites/default/files/2020-07/MSMEs_and_SDGs.pdf> accessed 5 May 2025.

[10] ibid UN Doc A/RES/70/1.

[11] UNDESA (n 9) 4; also see Sarah Schoenmaekers, 'The Role of SMEs in Promoting Sustainable Procurement' in Beate Sjåfjell and Anja Wiesbrock (eds), *Sustainable Public Procurement under EU Law: New Perspectives on the State as Stakeholder* (Cambridge University Press 2015) 160.

and markets is essential to build a resilient infrastructure, promote inclusive and sustainable industrialisation, and foster innovation.[12]

In response to these calls, governments have implemented various measures to support the formation and performance of SMEs by helping them overcome the constraints they face.[13] Commonly adopted SME policies include improving access to finance, offering tax reliefs, or providing direct subsidies, etc. [14] These measures typically fall into two categories: direct interventions, such as grants and subsidised loans, and indirect approaches aimed at improving the business environment for SMEs, for example by simplifying regulatory procedures or offering tax incentives.[15] Direct support mechanisms have attracted criticism, particularly due to their fiscal burden and uncertain effectiveness.[16] In contrast, improving the business environment for SMEs is viewed as a more advantageous form of support as it does not directly raise large public expenditure and may yield broader structural benefits.[17]

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[12] UN (n 9) 19, see SDGs 8.3 and 9.2.

[13] Among the most common support measures are policies to enhance SME access to finance, provide then with wage subsidies, and payment deferrals, such as tax. See Vanitha Prasannath and others, 'Impact of Government Support Policies on Entrepreneurial Orientation and SME Performance' (2024) 20 International Entrepreneurship and Management Journal 1533, 1534. SMEs face more difficulties in accessing to financial resources compared with large businesses, and access to finance is deemed as an important factor in the survival and growth of SMEs. See Sasan Bakhtiari and others, 'Financial Constraints and Small and Medium Enterprises: A Review' (2020) 96 Economic Record 506.

[14] OECD, *Framework for the Evaluation of SME and Entrepreneurship Policies and Programmes 2023* (OECD Studies on SMEs and Entrepreneurship, OECD Publishing 2023) 102. For example, in the EU, the most recent SME-related policy was published in December 2023. The relief package includes measures such as simplifying taxes, better or business-friendly regulation, tackling late payments, financial support (more favourable financing conditions), easier access to public procurement markets, easier access to sustainable finance. See European Commission, 'SME Relief Package' (Communication 12 September 2023) COM (2023) 535 final.

[15] See Prasannath and others (n 13) 1534; Lutz Preuss, 'On the Contribution of Public Procurement to Entrepreneurship and Small Business Policy' (2011) 23 Entrepreneurship & Regional Development 787.

[16] Gibb (n 6); James Curran, 'What Is Small Business Policy in the UK for? Evaluation and Assessing Small Business Policies' (2000) 18 International Small Business Journal 36.

[17] Phoebe Bolton, 'Government Procurement as a Policy Tool in South Africa' (2006) 6 Journal of Public Procurement 193, 196.

The business environment relevant to SMEs can broadly be divided into four aspects: the institutional and regulatory framework, access to markets, entrepreneurial culture, and access to resources.[18] Public procurement, the process by which public authorities purchase goods, services, and works from the private market, forms a critical part of the market environment for SMEs.[19]

Public procurement constitutes a significant part of government expenditure and economic activity.[20] In 2023, it accounted for an average of 12.7 per cent of GDP across OECD countries, with even higher figures observed in OECD-EU countries, for example, nearly 20 per cent in the Netherlands.[21] Given this scale, public procurement is governed by a complex body of legal and regulatory rules, which serve multiple purposes.[22] Some are driven by domestic objectives, such as achieving value for money, promoting efficiency, preventing corruption, or advancing industrial and social policies; others stem from external commitments, particularly the liberalisation of international procurement markets through trade agreements and multilateral frameworks.[23] Satisfying the procurement need and achieving value for money is usually considered the primary objective of a procurement system; other primary

[18] See OECD, *SMEs in Public Procurement: Practices and Strategies for Shared Benefits* (OECD Public Governance Reviews, OECD Publishing 2018) 29.

[19] For the definition of public procurement, see Sue Arrowsmith, John Linarelli, and Don Wallace, Jr. *Regulating Public Procurement: National and International Perspectives*, Kluwer Law International, 2000, 1.

[20] OECD, *Government at a Glance 2025* (OECD Publishing 2025) 147.

[21] ibid.

[22] Martin Trybus, Gustavo Piga and Tünde Tatrai, 'Colloquium' in Gustavo Piga and Tünde Tatrai (eds), *Public Procurement Policy* (Routledge 2016) 9.

[23] Arrowsmith, Linarelli, and Wallace, Jr. (n 19) 15; UNCITRAL Model Law on Public Procurement propose six objectives, including efficiency, competition, transparency, integrity, equal treatment, and promoting international trade. See *UNCITRAL Model Law on Public Procurement,* UN Doc A/66/17, annex I (adopted 2011), Preamble.

objectives include competition, efficiency, integrity, etc.[24] Specifically, value for money is achieved when a contracting authority successfully acquires the goods, services, or works needed by the government on the best available terms.[25] To obtain value for money, public procurement regulations may require transparency or the use of a competitive procurement method in the procurement process.[26]

Recognising the purchasing power of governments, public procurement has increasingly been used not only for functional objectives but also to pursue broader strategic goals, including social, environmental, and economic sustainability objectives in some jurisdictions.[27] Notably, the UN SDG 12.7 explicitly calls for public authorities to adopt sustainable public procurement (SPP) practices that ensure sustainable consumption and production patterns.[28] Although there is no universal definition of socioeconomic objectives, the UN SPP Indicator Methodology provides a reference framework for such considerations.[29] Supporting SMEs is one of these socioeconomic

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[24] Schooner identifies nine objectives frequently adopted by government procurement systems: (1) competition; (2) integrity; (3) transparency; (4) efficiency; (5) customer satisfaction; (6) best value; (7) wealth distribution; (8) risk avoidance; and (9) uniformity. See Steven L Schooner, 'Desiderata: objectives for a system of government contract law' (2002) 2 Public Procurement Law Review 103.

[25] Arrowsmith, Linarelli, and Wallace, Jr. (n 19) 28.

[26] ibid 29.

[27] See James F. Nagle, *A History of Government Contracting* (3rd edn, Government Training Inc 2012) ch 19, 108; Sue Arrowsmith and Peter Kunzlik (eds.) *Social and Environmental Policies in EC Procurement Law* (Cambridge, Cambridge University Press, 2009) 12; Willem Janssen, 'Shifting Towards Mandatory Sustainability Requirements in EU Public Procurement Law: Context, Relevance and a Typology' in Willem Janssen and Roberto Caranta (eds), *Mandatory Sustainability Requirements in EU Public Procurement Law: Reflections on a Paradigm Shift* (Hart Publishing 2023) 4.

[28] UN (n 9) 19, see SDG 12.7.

[29] In the 'SDG Indicator 12.7.1 SPP Index Calculation Methodology & Guidelines', SPP is referred to as a process whereby public organisations meet their needs for goods, services, works and utilities in a way that achieves value for money on a whole life cycle basis in terms of generating benefits not only to the organisation, but also to society and the economy, whilst significantly reducing negative impacts on the environment. See UNEP, 'SDG Indicator 12.7.1 SPP Index Calculation Methodology & Guidelines' (updated 18 June 2021) <https://www.oneplanetnetwork.org/sites/default/files/spp_index_methodology_sdg_indicator_12.7.1.pdf> accessed 08 June 2025. Article 2 (o) UNCITRAL Model Law on Public Procurement has a wide definition of socio-economic policies, which refer to 'environmental, social, economic and other policies

objectives, alongside others such as protecting human rights, promoting compliance with International Labour Organisation standards and decent work, and promoting fair trade, etc.[30] In practice, promoting SMEs is identified as one of the most frequently expressed concerns addressed in SPP implementation.[31]

Arrowsmith and Kunzlik used the term 'horizontal policies' to encompass social and environmental objectives that public authorities may wish or be required to pursue in public procurement activities. [32] These horizontal policies are not necessarily connected with the functional objectives of a procurement activity.[33] While in some jurisdictions the pursuit of socioeconomic objectives is an entrenched feature of the procurement system, their use as instruments of public policy remains contested, especially when they are embedded in legal frameworks and come into tension with primary objectives and principles, such as value for money, competition, and efficiency. [34] In practice, incorporating socioeconomic objectives can increase administrative burdens, for example, by complicating specification, selection and award criteria, and lengthening tender evaluation, thereby potentially compromising

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of this State authorized or required by the procurement regulations or other provisions of law of this State to be taken into account by the procuring entity in the procurement proceedings'. See *UNCITRAL Model Law on Public Procurement,* art 2(o) (n 23).

[30] UN, 'SDG Indicator 12.7.1 SPP Index Calculation Methodology & Guidelines' (n 29) 15.

[31] Other most popular concerns addressed in SPP implementation include the protection against human rights abuses, the promotion of decent work and compliance with ILO standards, the promotion of transparency, accountability and combating corruption. See UNEP, '2020/2021 Data Collection for SDG Indicator 12.7.1' <https://wedocs.unep.org/bitstream/handle/20.500.11822/37967/SDG.pdf> accessed 08 June 2025, 22.

[32] See Arrowsmith and Kunzlik (n 27) 13; Sue Arrowsmith, 'Horizontal Policies in Public Procurement: A Taxonomy' (2010) 10 Journal of Public Procurement 150; Arrowsmith, Linarelli, Wallace, Jr. (n 19) 237; Trybus, Piga, and Tatrai (n 22) 9.

[33] Arrowsmith and Kunzlik (n 27) 9; Steven L Schooner, 'United States: Mixed Messages: Heightened Complexity in Social Policies Favouring Small Business Interests' (1999) Public Procurement Law Review 3, CS78.

[34] Schooner (n 24) 104; Arrowsmith, 'Horizontal Policies in Public Procurement: A Taxonomy' (n 32); Nagle (n 27) 152.

efficiency of the procurement process.[35] Trybus argues that horizontal objectives shall be pursued in a balance with other objectives of public procurement, especially with value for money.[36] Similarly, Sjåfjell and Wiesbrock argue that the issue is to balance socioeconomic and environmental objectives with economic objectives rather than choosing one over the other.[37] However, achieving such a balance proves challenging in practice.[38]

Nevertheless, the difficulty does not lie in the pursuit of horizontal objectives as such, but in the choice and design of the mechanisms by which those aims are operationalised in public procurement regulations.[39] Arrowsmith proposes a taxonomy comprising nine categories of such mechanisms: (1) the decision to purchase or not to purchase, (2) the decision on what to purchase, (3) contract conditions laid down by the purchaser, (4) packaging and timing of orders, (5) set-asides, (6) exclusion from contracts for non-compliance with government policies, (7) preferences in inviting firms to tender, (8) award criteria, (9) measures for improving access to government contracts.[40] Among these mechanisms, some compromise open competition by restricting participation to specific bidder groups, whilst others can enhance competition and value for money when carefully designed [41]

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[35] ibid; also see Arrowsmith and Kunzlik (n 27) Preface, xviii.

[36] Martin Trybus, 'Beyond Competition and Value for Money: Corporate Social Responsibility in Public Procurement' (2020) 8(4-2) Kilaw Journal 217.

[37] Beate Sjåfjell and Anja Wiesbrock, 'Why should public procurement be about sustainability?' in Sjåfjell and Wiesbrock (eds) (n 11) 4.

[38] Kirsi-Maria Halonen, 'Is Public Procurement Fit for Reaching Sustainability Goals? A Law and Economics Approach to Green Public Procurement' (2021) 28 Maastricht Journal of European and Comparative Law 535, 536.

[39] Trybus, 'Beyond Competition and Value for Money: Corporate Social Responsibility in Public Procurement' (n 36).

[40] Arrowsmith, 'Horizontal Policies in Public Procurement: A Taxonomy' (n 32) 152.

[41] ibid.

The objective of supporting SME can be pursued through the above-mentioned mechanisms, each carrying distinct implications for other procurement objectives. Such measures may be categorised according to procurement stages as SMEs face barriers at different stages of the procurement process.[42] Prior to bidding, contracting authorities may limit competition exclusively to SMEs. In a call for tenders, authorities may divide large contracts into smaller lots to accommodate SME capacity limitations.[43] At the qualification stage, legislation may impose caps on minimum turnover requirements typically used to evaluate bidders' financial capacity.[44] Finally, at the award stage, price evaluation preferences may be provided for SMEs.[45] SME support can extend beyond contract award to performance and payment stages, including requirements for prime contractors to subcontract specified percentages to SMEs, or prompt payment obligations.[46]

Jurisdictional approaches vary significantly: some explicitly incorporate measures in public procurement law, requiring contracting authorities to consider or even prioritise SME interests, while others grant discretion to contracting authorities.[47] These

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[42] Donor Committee for Enterprise Development (DCED), 'Technical Report: Policies that Promote SME Participation in Public Procurement' (Business Environment Working Group September 2017, the World Bank Group) <https://www.enterprise-development.org/wp-content/uploads/DCED-BEWG-SME-Procurement-Report.pdf> accessed 28 April 2025, 18.

[43] Arrowsmith (n 32) 162; also see Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC [2014] OJ L94/65, art 46; For a discussion on the division into lots regime, see Chapter 4.

[44] Directive 2014/24/EU, art 58. For a discussion on managing the qualification process to facilitate SME access to procurement, see Chapter 5.

[45] For a discussion on providing bid preferences for SMEs at the award stage, see Chapter 6.

[46] The US Federal Acquisition Regulation (FAR) incorporate rules to support small businesses in both prime contracting and subcontracting, codified in Chapter 1 of Title 48, Code of Federal Regulation (CFR). See FAR, 48 CFR ch 1 (2024), pt 19.

[47] In the US, the Small Business Act explicitly require a certain share of government procurement contracts shall be awarded to small businesses. Similarly, in Brazil, preferential treatment to micro and small enterprises is laid down in Constitution. See Chapters 6 and 7 for the detailed discussion. For an overview of SME-friendly measures adopted by different jurisdictions, see DCED (n 42) 19.

jurisdictional differences raise important questions regarding measure design and implementation within procurement systems. Termed SME-friendly measures, these initiatives explicitly account for SME interests and range from facilitating their access to procurement opportunities to providing preferences in tender evaluation.[48] This thesis examines such measures in public procurement law, analysing the barriers hindering SME participation, how effectively different measures address these barriers, and what trade-offs arise with respect to other procurement objectives such as value for money, competition, non-discrimination, and efficiency.

1.2 Objectives and Significance of this Thesis

The involvement of SMEs in public procurement has attracted sustained academic attention across disciplines, including law, economics, and management.[49] The term 'involvement' refers to the whole process of SMEs, from searching for information about bidding opportunities, preparing and submitting bids, to being awarded and performing contracts.[50] Another term that will be frequently used in this thesis is 'participation', which refers only to the process where SMEs submit bids in procurement procedures, without them necessarily being awarded contracts. The distinction between participation and contract award is important because, as will be shown, some jurisdictions set more SME participation as an objective on its own, whereas others set spending targets to ensure that SMEs are awarded a particular

[48] Martin Burgi, 'Small and Medium-Sized Enterprises and Procurement Law - European Legal Framework and German Experiences' (2007) 4 Public Procurement Law Review 284.
[49] See Anthony Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (2025) Journal of Purchasing and Supply Management (in press, corrected proof) <https://doi.org/10.1016/j.pursup.2025.101052> accessed 31 July 2025.
[50] ibid 6.

share of contracts.[51] Both approaches have advantages and disadvantages, as will be discussed in this thesis.[52]

A recent literature review by Flynn revealed that scholars have examined SME involvement in public procurement from multiple angles, but mainly focussed on five themes: (1) systemic barriers facing SMEs, (2) policy and practice interventions, (3) SME capacity, (4) SME performance, and (5) sustainability in the public sector.[53] These themes encompass the empirical and policy-friendly concerns that dominate the existing literature, especially in economics and management. However, Flynn's review does not account for the legal dimension of SMEs in public procurement, as it draws on the databases ProQuest and EBSCO, which incorporate limited legal scholarship.[54] Legal research, while intersecting with these themes, often addresses different questions, such as the rationales for SME support in procurement regulations and the potential tensions such support may create with primary objectives and principles of procurement systems.[55] This section, therefore, seeks to situate this research within the broader interdisciplinary discourse by examining the rationales typically advanced to justify SME-friendly measures and the ongoing academic debates surrounding their legitimacy, design, and impact.

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[51] See Chapter 7, Section 7.3.5.

[52] A comparison of SME-friendly measures analysed in this thesis is presented in Chapter 8.

[53] See Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (n 49).

[54] ibid 2.

[55] Martin Trybus and Marta Andrecka, 'Favouring Small and Medium Sized Enterprises with Directive 2014/24/EU?' (2017) 12 European Procurement & Public Private Partnership Law Review 224.

1.2.1 The rationales for SME-friendly measures in public procurement

Access to markets and the opportunities to sell their products and services are essential to the survival and growth of SMEs.[56] As a major purchaser, the government can shape the market dynamics in which SMEs operate through its procurement activities.[57] From the SMEs' perspective, public procurement can be used to support them not only through increasing their revenue but also by helping them build capacity and professionalism through the bidding and contract execution processes.[58] Ferraz et al have found that winning at least one contract in a given quarter increased company growth by 2.2 per cent, with continued growth for at least two years after winning the contract.[59] More importantly, this effect is more significant on younger and smaller businesses.[60]

Apart from the benefits of acquiring public procurement contracts for SMEs, it is argued that more SME participation is also beneficial for the governments.[61] Firstly, more SME participation represents enhanced competition in public procurement markets.[62] An increasing number of SMEs in the supplier pool can reduce the risk of

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[56] There are studies identifying demand deficiency as the main hindrance to small firm growth. See Ronald W Mcquaid, 'Entrepreneurship and ICT Industries: Support from Regional and Local Policies' (2002) 36 Regional Studies 909, 915.

[57] See Sue Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (3rd edn, Sweet & Maxwell 2014) para 4-106.

[58] Anthony Flynn and Paul Davis, 'The Policy-Practice Divide and SME-Friendly Public Procurement' (2016) 34 Environment and Planning C: Government and Policy 559, 561.

[59] Claudio Ferraz, Frederico Finan and Dimitri Szerman, 'Procuring Firm Growth: The Effects of Government Purchases on Firm Dynamics' (National Bureau of Economic Research 2015, w21219) <http://www.nber.org/papers/w21219.pdf> accessed 22 May 2025.

[60] ibid 20.

[61] OECD, *SMEs in Public Procurement* (n 18) 9.

[62] For a discussion on how public procurement regulations and practices could be a source of market failure, see Albert Sanchez-Graells, *Public Procurement and the EU Competition Rules* (2nd edn, Bloomsbury 2015) 60; also see Casady CB, Petersen OH, Brogaard L, 'Public Procurement Failure: The Role of Transaction Costs and Government Capacity in Procurement Cancellations' (2023) Public Management Review <https://doi.org/10.1080/14719037.2023.2231945> accessed 11 July 2025

contracting authorities being 'locked in' by large businesses.[63] Even if SMEs do not win more public procurement contracts, their presence in the competition will reduce the risk of collusion among large businesses.[64] Moreover, emerging evidence suggests that SMEs may demonstrate relative resilience in public procurement participation during periods of moderate to high inflation.[65]

Although the benefits of SMEs participating in public procurement are well recognised, they are regarded as underrepresented compared to large businesses in public procurement markets across jurisdictions.[66] Piga conceptualises the difference between SMEs' share of total gross value added (GVA) and their share of public procurement as a form of discrimination index against SMEs in public procurement.[67] Between 2009 and 2011, this 'discrimination index' averaged 29 across the EU Member States, indicating widespread underrepresentation of SMEs in public procurement, at least in above-threshold procurement.[68] The view that SMEs are

[63] Temidayo O Akenroye and others, 'One Size Does Not Fit All: Deciphering the Interdependence between Barriers Hindering SMEs' Involvement in Public Sector Procurement' (2024) 37 International Journal of Public Sector Management 935, 949.

[64] Martin Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (2018) 43 European Law Review 313.

[65] Luka Klimavičiūtė, Marco Schito and Egidijus Barcevičius, 'Do Firms Submit Fewer Tender Bids with High Inflation? An Analysis of Firms' Participation in Public Procurement in the EU' (2024) 24 Journal of Public Procurement 478, 492.

[66] See OECD, *SMEs in Public Procurement* (n 18) 32; PwC, ICF GHK and ECORYS, *SMEs' Access to Public Procurement Markets and Aggregation of Demand in the EU* (Study commissioned by European Commission, DG Internal Market and Services, February 2014) 5; also see Andreas Herbert Glas and Michael Eßig, 'Factors That Influence the Success of Small and Medium-Sized Suppliers in Public Procurement: Evidence from a Centralized Agency in Germany' (2018) 23 Supply Chain Management: An International Journal 65.

[67] Gustavo Piga, 'Centralization vs. Bundling: The Victory of an Italian David against an Italian Goliath' (2018) 1 European Journal of Public Procurement Markets 62, 65.

[68] See de Bas P and others, *Analysis of the SMEs' Participation in Public Procurement and the Measures to Support It - 697/PP/GRO/IMA/18/1131/10226: Final Report* (European Commission, October 2019) 96. Although this approach draws attention to possible disparities, its underlying assumptions and data limitations must be considered. Notably, this underlying data includes only contracts above the EU thresholds, whereas SMEs are known to participate more actively in lower-value contracts. From 2011-2017, they accounted for between 56 per cent and 94 per cent of the value

underrepresented in public procurement motivated the incorporation of SME-friendly measures in the 2014 EU public procurement directives, such as dividing contracts into lots, or limiting the minimum turnover requirement, etc.[69] In the US, the participation of small businesses in government procurement is in a similar situation.[70] Based on the data from the SBA Office of Advocacy, small businesses have consistently contributed to more than 40 per cent of the total GDP, whereas the proportion of federal procurement contracts awarded to them accounts for only 27 per cent.[71]

The extant literature frequently takes these disparities as evidence of systemic barriers faced by SMEs in accessing public procurement markets, and barriers faced by SMEs have gathered more research interest than any other topic related to SMEs in public procurement.[72] Although the definition and scope of the term 'barriers' remain unclear,[73] scholars commonly concur on categorising these barriers into two distinct types: those necessitating intervention from the public sector (external factors) and

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of below-threshold procurement contracts in the EU. However, comparisons based solely on above-threshold data may overstate the extent of SME underrepresentation.

[69] Directive 2014/24/EU; see Trybus and Andrecka (n 55); see Chapter 4 for an analysis of the division into Lots and Chapter 5 for managing the qualification process.

[70] See Chapter 2 for the definition of small businesses and its difference with SMEs.

[71] See US SBA Office of Advocacy (n 4).

[72] See Chapter 3 on barriers faced by SMEs in public procurement. See Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (n 49) 6; also see Mazzucato, M., Spanó, E., and Wainwright, D., 'Rethinking the economics of public procurement: towards a mission-friendly economic approach' (UCL Institute for Innovation and Public Purpose, Working Paper Series IIPP WP 2025-08) <https://www.ucl.ac.uk/bartlett/publications/2025/jun/rethinking-economics-public-procurement-towards-mission-oriented-approach> accessed 14 June 2025, 15; Kim Loader, 'Small- and Medium-Sized Enterprises and Public Procurement: A Review of the UK Coalition Government's Policies and Their Impact' (2018) 36 Environment and Planning C: Politics and Space 47, 48.

[73] Barriers faced by SME gathered the most research interests than any other topic related to SMEs in public procurement. See Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (n 49) 9-10; Jamie Thomas, 'A Working Definition of "Barriers" to Small Business in Public Procurement:' (2023) 18 European Procurement & Public Private Partnership Law Review 77, 79.

those requiring proactive measures from SMEs (internal factors).[74] The former category includes pro-large-business (risk-averse) attitudes, large contract size, administrative burden, etc.[75] The latter category includes barriers such as a lack of appropriate resources, poor completion of bids, a lack of required standards, etc.[76]

Similarly, Thomas has recognised the difference between natural disadvantages and barriers.[77] Natural disadvantages refer to conditions that may place businesses at a disadvantage, such as size, experience, or geographic location, and they do not warrant regulatory intervention.[78] Barriers are defined as structural impediments arising from procurement rules or practices that may make it disproportionately more difficult for SMEs to bid for or win public contracts.[79] While this categorisation offers conceptual clarity, it may understate how certain natural disadvantages can be intensified by the design of procurement systems, thereby blurring the distinction between natural disadvantages and barriers in practice.[80] Hence, the discussion of barriers facing SMEs in public procurement raises the question of whether public

[74] Kim Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (2013) 31 Environment and Planning C: Government and Policy 39; 46. UNDP, New Playbook on Inclusive Public Procurement' (*Business Call to Action*, 21 September 2022) <https://www.businesscalltoaction.org/news/now-online-new-playbook-on-inclusive-public-procurement> accessed 31 October 2023.

[75] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74) 44-46.

[76] ibid 46.

[77] Thomas (n 73) 81.

[78] ibid.

[79] Thomas (n 73).

[80] For example, SMEs consistently report that the procurement process is too complex to navigate, which is a challenge that large businesses may also face, but it is more severe to SMEs as they often lack certain financial and human resources to deal with the complex procurement process.

procurement law is genuinely supplier-neutral or inherently favours larger businesses.[81]

Across jurisdictions, these debates are addressed through divergent legal approaches. Some regimes permit preferences or reservations for SMEs as a corrective to structural barriers they confront in the procurement system.[82] Public procurement systems often unintentionally favour larger businesses through mechanisms such as contract aggregation, administrative complexity, and stringent qualification requirements.[83] Others prohibit preferential treatment and rely on access-enhancing tools such as dividing contracts into lots, proportionate selection criteria, grounded in a strict reading of equal treatment.[84] A third group adopts hybrid models that allow reserved contracts under certain thresholds and also use access-enhancing tools.[85] Building on this, the following section outlines the main types of SME-friendly measures adopted in public procurement systems and the key objectives they pursue. It sets the stage for later chapters that will explore how the design of such measures influences their effectiveness in practice, and what trade-offs emerge between the goal of supporting SMEs and core procurement objectives such as value for money, competition, and efficiency.

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[81] 'Supplier-neutral' denotes a public procurement system that neither advantage nor disadvantage economic operators on the basis of their size.

[82] A prominent example of such systems is the United States. See Sandra M Anglund, 'Policy Feedback: The Comparison Effect and Small Business Procurement Policy' (1999) 27 Policy Studies Journal 11.

[83] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).

[84] A prominent example is the European Union, see European Commission, 'Promoting SME Participation in Public Procurement in the Community' (Communication) COM (90) 166 final.

[85] An example of the third approach is Brazil, incorporating both preferential and facilitative measures. For a discussion on jurisdictional approaches, see Chapter 8, Section 8.3.

1.2.2 The objectives and classification of SME-friendly measures in public procurement

As mentioned earlier in Section 1.1, SME-friendly measures are defined as measures designed specifically to enhance SME involvement in public procurement markets, irrespective of whether the measure is facilitative, preferential, or symbolic.[86] SME-friendly measures are often tasked with multiple objectives, and the scope and extent of these measures are contingent upon a government's priorities and institutional frameworks.[87] Some objectives fall within the scope of public procurement, such as increasing SME participation or contract awards. In contrast, others extend beyond it, including supporting SME development, boosting the local economies in which they operate, and promoting the inclusion of SME owners, such as women or minority entrepreneurs.[88] The broader and more numerous the objectives of a measure, the more complex the task of evaluating its effectiveness becomes.[89]

As Storey argued, SME policies that pursue multiple objectives warrant caution in evaluation, as the fulfilment of a single aim may be regarded as evidence of overall success.[90] This concern is particularly relevant in jurisdictions where SME-friendly measures in public procurement are tied to broader economic policy goals, such as SME development, entrepreneurship, or local economic growth. These objectives, while important, are often diffuse and difficult to evaluate within legal frameworks. In such cases, the degree of governmental commitment to these goals can often be

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[86] See Section 1.1.

[87] Burgi (n 48) 284.

[88] See Chapter 6, Section 6.4; also see Chapter 7, Section 7.2.

[89] David J Storey, 'Six Steps to Heaven: Evaluating the Impact of Public Policies to Support Small Businesses in Developed Economies' in Donald L. Sexton, Hans Landström (eds), *The Blackwell Handbook of Entrepreneurship* (Blackwell 2000) 176.

[90] ibid 179.

discerned through the language used in relevant provisions, which may signal whether these measures are intended as enforceable tools or symbolic affirmations. For example, 'supporting', 'promoting', and 'protecting' represent a more proactive attitude, whereas 'facilitating' and 'encouraging' represent a more neutral stance. In the EU, the Commission used the term 'promoting' and argued that fuller SME participation will bring the benefits of 'mobilisation of new resources, increased competition and stimulus to entrepreneurship'.[91] However, in the currently effective public procurement framework, Directive 2014/24/EU adopts a more neutral approach by using the terms 'facilitating' and 'encouraging' regarding SME-friendly measures.[92] For example, Recital 78 Directive 2014/24/EU mentions that contracting authorities shall be encouraged to refer to the soft law Code of Best Practices published in 2008, which introduced multiple SME-friendly measures in public procurement, ranging from ensuring access to relevant information, setting proportionate qualification levels and financial requirements, to ensuring timely payments.[93] Recital 78 sets out that 'to that end [facilitate SME participation] and to enhance competition, contracting authorities should in particular be encouraged to divide large contracts into lots'.[94] Moreover,

[91] See European Commission, COM (90) 166 final I.2. This rationale is supported by Article 173 (1) TFEU, where it stresses that to support the competitiveness of the EU's industry, 'an environment favourable to initiative and to the development of undertakings throughout the Union, particularly small and medium-sized undertakings' shall be encouraged. See Consolidated Version of the Treaty on the Functioning of the European Union (TFEU) [2012] OJ C326/47, art 173 (1). Originally, SME favouring policies existed in the EU and they were considered to be successful. However, these policies were abolished since the start of the Single Market in 1992 because they were strongly related to regional developments. See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 239; also see Christopher Bovis, 'The Regulation of Public Procurement as a Key Element of European Economic Law' (1998) 4 European Law Journal 220, 236.

[92] See Directive 2014/24/EU, recitals 2, 120, 124. The only provision used the term 'SME support' is Recital 120 where it mentions SME support in the context of specific SME support programmes such as Joint European Resources for Micro to Medium Enterprises.

[93] See European Commission, 'European Code of Best Practices Facilitating Access by SMEs to Public Procurement Contracts' (Commission Staff Working Document, 25 June 2008) SEC (2008) 2193.

[94] Directive 2014/24/EU, recital 78.

Recital 124 Directive 2014/24/EU explicitly states that it is not appropriate to impose an obligation on national governments to guarantee a specific share of success for SMEs.[95] This reveals that the objective of SME-friendly measures in Directive 2014/24/EU is to facilitate the participation of SMEs, and it should not be interpreted as a spending target or a binding mandate on contracting authorities.[96]

In contrast, the US adopts a more proactive and target-driven approach to SME-friendly measures in public procurement. The Small Business Act, as amended (15 U.S.C. 631), sets out an explicit policy that the federal government should 'aid, counsel, assist, and protect' the interests of small businesses to preserve free competitive enterprise.[97] The phrasing indicates that the objective is to safeguard and assist small enterprises, rather than merely enhancing their involvement in federal procurement. As will be discussed in Chapter 7, this proactive approach is coupled with legally binding targets and obligations on contracting authorities to reserve contracts for small businesses.[98]

The jurisdictional differences have attracted scholars to categorise SME-friendly measures into different approaches. Most literature categorises SME-friendly measures based on their objectives, and some are based on the effects of the measure. Burgi divides measures into SME-fair and SME-favouring.[99] SME-fair measures aim to 'counteract the difficulties and disadvantages' that SMEs face and create equal opportunities for them, whereas SME-favouring measures aim beyond

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[95] Directive 2014/24/EU, recital 124.

[96] These SME-friendly rules include dividing large contracts into lots, a cap on minimum turnover requirement, ESPD, direct payment to subcontractors. See Trybus and Andrecka (n 55).

[97] 15 United States Code (USC) §631 (2021).

[98] Chapter 7 in this thesis will explore the effectiveness of reserved contracts in the US federal procurement.

[99] Burgi (n 48).

providing equal opportunities and improving SMEs' situation directly by favouring them in the award procedure.[100] Similarly, Loader divides approaches that governments may take into interventionist and level playing field approaches.[101] The interventionist approach involves active support for SMEs, including reserved contracts and spending targets, while the level playing field approach only aims to achieve a level playing field where SMEs are not adversely treated, such as dividing large contracts into lots or improving access to tender information.[102] However, both adverse treatment and a level playing field are contestable and difficult to define in practice. For instance, a turnover requirement set at three times the contract value may be viewed by a small business as exclusionary, while a medium-sized enterprise may consider it proportionate.[103] In another scenario, when a large contract is divided into small lots, large businesses may claim that they are adversely treated as they cannot leverage economies of scale, which is usually their advantage.[104] Moreover, the idea that all businesses can be placed on an equal footing through legal intervention is aspirational rather than realistic.[105] SME-friendly measures inevitably affect different types of firms

[100] ibid 288.

[101] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74) 50. More broadly, Loader argues that there are two approaches, government support and SME self-help approach. More literature focuses on the government support, but not SME self-help approaches, which include, for example, SMEs developing their knowledge and skills about public procurement procedures or forming consortia to bid for large procurement contracts.

[102] ibid.

[103] See Chapter 5, Section 5.2.1 for a discussion on financial requirements.

[104] See Thomas (n 73). Thomas argued that sometimes a large contract should be justified as it is not suitable for SMEs to undertake. Also see chapter 6 for a detailed discussion on trade-offs in division into lots.

[105] A level playing field refers to a situation that is fair because everyone has the same chance of succeeding. See Cambridge University Press, 'Level playing field' (Cambridge Business English Dictionary, Cambridge University Press 2011) <https://dictionary.cambridge.org/dictionary/english/level-playing-field?q=level+playing> accessed 16 June 2025.

in different ways, and the use of certain terms, such as level playing field, may obscure rather than clarify the actual trade-offs involved.

Based on the effects of those programmes on competition in procurement markets, Kirkwood adopts a typology of facilitative and preferential small business programmes. [106] Preferential programmes artificially add restrictions to the procurement marketplace by providing small businesses with preferences, whereas facilitative programmes seek to help SMEs without distorting the competitive marketplace.[107] Both Burgi and Kirkwood argue that SME-favouring measures (Burgi) or preferential programmes (Kirkwood) have negative impacts on competition in public procurement markets. Trybus and Andrecka have also pointed out that measures which favour SMEs would compromise the main objectives of competition, non-discrimination, and value for money in the EU.[108] However, the concept of 'competition' needs to be more specifically defined. [109] As discussed in Chapter 4, although reserving contracts exclusively for SMEs is an exception to the principle of open competition, it does not necessarily reduce actual competition in public procurement procedures.[110] Interestingly, a facilitative measure for SMEs does not interfere with the principle of open competition, but it may have a negative impact on the actual competition in tendering, such as dividing contracts into lots, which might discourage

[106] William Kirkwood, 'The Evolution of Small Business Preferences in the United States and Selected Lessons Learned for the European Union' (2016) 11 European Procurement & Public Private Partnership Law Review 311, 312.

[107] ibid 312. Under this definition, facilitative measures include loan guarantees, simplified procedures, dividing contracts into lots, restricting bundling, and preferential measures including set-aside programmes (reserved contracts), bid advantages etc.

[108] Trybus and Andrecka (n 55) 224.

[109] See Trygve Harlem Losnedahl, 'Five Meanings of "Competition" in EU Law', (2025) 11(2) *Oslo Law Review* 1. As Harlem Losnedahl pointed out, there are more than one meaning of 'competition' and a rigorous analysis shall be clear about which meaning of the competition is referred to.

[110] See Chapter 7 on reserved contracts.

large businesses from submitting bids.[111] Thus, whether competition is compromised or not is not an appropriate criterion to categorise SME-friendly measures.

While classifications of SME-friendly measures help to conceptualise different approaches, they do not always capture the nuances of individual measures. Moreover, the actual impact of a measure often depends not on its classification but on its detailed rule design and legal enforceability. For these reasons, this thesis does not rely on a classified framework but examines specific measures on their own terms. However, the distinctions discussed above help illuminate why some measures may face greater legal or practical challenges than others, which is an issue explored further in Chapters 6 (bid preferences) and 7 (reserved contracts), and returned to in the Conclusions.

1.2.3 The effectiveness of SME-friendly measures

The effectiveness of SME-friendly measures is subject to an ongoing debate in the law, economics, and management literature.[112] 'Effective' is usually used to define a measure as being successful and working in the intended manner, and effectiveness refers to the extent to which something is effective.[113] In fact, this question includes two parts, one if contracting authorities have implemented these measures as legislators intended on the one hand, and if these measures can achieve their

[111] See Chapter 4 on division into lots.

[112] The discussion of existing empirical evidence on the effectiveness of SME-friendly measures is incorporated in Chapters 4-7.

[113] Longman Business Dictionary, 'effective' (Longman Business Dictionary, LDOCE online) <https://www.ldoceonline.com/Law-topic/effective> accessed 24 June 2025; Cambridge University Press, 'effectiveness' (Cambridge Dictionary, online) <https://dictionary.cambridge.org/dictionary/english/effectiveness> accessed 24 June 2025.

stipulated objectives if implemented properly on the other hand. A further inquiry is the trade-offs such measures incur with other objectives in public procurement systems.

Trybus has examined the division into lots regime stipulated in Article 46 Directive 2014/24/EU and found that it would be challenging to achieve its intended objectives, which is to increase SME participation, due to the fact that contracting authorities can easily choose not to divide a large contracts into lots, unless there is an obligation to divide contracts into lots.[114] Flynn and Davis have found that there is a policy-practice divide in SME-friendly public procurement, with little evidence showing that contracting authorities are implementing these measures.[115] This could be due to a risk-aversion attitude of contracting authorities, which is a recognised barrier in itself.[116] In fact, Flynn and Davis have observed that the division into lots regime has the lowest level of compliance among public buyers.[117] This will be further discussed in Chapter 4.[118]

Even when SME-friendly measures are implemented by contracting authorities according to the law, there is mixed evidence about their effectiveness. Hoakman and Taş found that dividing contracts into lots is associated with higher participation of SMEs but their chance of being awarded the contract does not increase, unless the value of the lots is lower than EUR 25,000.[119] However, Nemec has found the opposite, that dividing a contract into lots does not increase SME participation in public works contracts but seems to increase their chances of being awarded the contract.[120] There

[114] See Chapter 4 on division into lots.
[115] Flynn and Davis (n 58)
[116] Akenroye and others (n 63) 949.
[117] Flynn and Davis (n 58) 565.
[118] See Chapter 4; also see Chapter 8, Section 8.4.3.
[119] Bernard Hoekman and Bedri Kamil Onur Taş, 'Procurement Policy and SME Participation in Public Purchasing' (2022) 58 Small Business Economics 383.
[120] Peter Nemec, 'Contesting the Public Works Domain: Examining the Factors Affecting Presence and Success of SMES in Public Procurement' (2024) 67 Empirical Economics 2135, 2158.

are more concerns about SME-favouring measures than SME-fair measures, as the former type of measures tends to create reliance of SMEs on those preferences and compromises the open competition principle.[121]

Despite sustained academic interest, much of the existing literature on SME-friendly public procurement remains segregated within disciplinary boundaries. Economic and management research tends to focus on the impact of barriers and SME support measures on bidder performance, often attempting to quantify associated costs and benefits. Legal scholarship, by contrast, typically addresses the legitimacy and legal implications of SME-friendly measures within a specific jurisdictional context, with less attention to cross-jurisdictional comparisons or empirical evaluation. Critics of SME-friendly measures caution that they may conflict with the value for money principle and introduce inefficiencies.[122] Measures which aim to secure a share of public procurement (reserved contracts) for SMEs have been regarded as a form of state support intended to address insufficient market demand for SMEs.[123] When SMEs are awarded contracts through SME-friendly measures and their offers do not represent the best value for money, it is expected that government funds are used to absorb the resulting inefficiencies.[124] Advocates for more proactive SME-friendly measures counter that a level playing field does not naturally exist, SMEs face inherent disadvantages, such as limited resources, less bidding experience, etc, and that procurement rules can be adjusted to legitimately offset those disadvantages.[125]

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[121] Hoekman and Taş (n 119).

[122] See OECD, *SMEs in Public Procurement* (n 18) 89.

[123] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74); also see Christopher Yukins and Gustavo Piga, 'Dialogue', Gustavo Piga and Steen Treumer (eds) *The Applied Law and Economics of Public Procurement* (Routledge 2013) 321.

[124] Storey (n 89) 178.

[125] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).

Moreover, Nicholas and Fruhmann argue that SME policies in public procurement should not be exempt from the general requirements of public procurement systems, such as transparency, objectivity, integrity, and value for money.[126]

These debates illustrate that SME support in procurement is neither universally accepted nor uniformly implemented. What remains underdeveloped in the literature is a comprehensive, interdisciplinary approach that examines SME-friendly measures as legal and policy instruments in their own right, grounded in national examples and situated within specific jurisdictional contexts. This thesis focuses on how particular SME-friendly measures are designed and applied within individual legal frameworks, and how they operate alongside broader procurement principles and objectives.

1.3 Research Questions of this Thesis

While public procurement holds significant potential for supporting SME development, the effectiveness of SME-friendly measures depends heavily on careful rule design by legislators and robust implementation by contracting authorities. Although existing legal research has examined the compatibility of some SME-friendly measures with the other objectives of public procurement systems,[127] and economic research has

[126] Caroline Nicholas and Michael Fruhmann, 'Small and Medium-Sized Enterprises Policies in Public Procurement: Time for a Rethink?' (2014) 14 Journal of Public Procurement 328, 352.

[127] For a discussion of the four SME-friendly measures in Directive 2014/24/EU and if they interfere with the primary objectives of public procurement rules in the EU, see Trybus and Andrecka (n 55). For a detailed discussion of the division into lots regime in the EU and its Member States, see Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64). For a discussion on if reserved contracts is consistent with principles of EU law, see Dorthe Kristensen Balshøj, 'Can Affirmative Action be Allowed in EU Procurement Law? – SMEs to be Positively Discriminated?' (2021) 32 European Business Law Review 9'.

evaluated the effectiveness of certain SME-friendly measures,[128] there remains a gap in understanding such measures in a comprehensive and integrated manner. This thesis aims to fill this gap by providing a critical analysis of four prominent SME-friendly measures, drawing on jurisdictional examples selected for their experience with particular measures in order to illustrate variations in legal design and practical implementation. On this basis, the thesis addresses three interrelated research questions:

Firstly, what barriers limit SME participation in public procurement? The literature discusses various challenges facing SMEs but often conflates structural barriers preventing market access with competitive disadvantages at the award stage, or with factors that reflect perceptions rather than genuine barriers. This thesis develops a clear definition of barriers and examines which commonly cited challenges constitute entry barriers requiring regulatory intervention. This research question will be discussed and answered in Chapter 3.

Secondly, how effective are the selected SME-friendly measures, namely dividing contracts into lots, managing the qualification process, providing bid preferences, and reserving contracts, in addressing the specific barriers faced by SMEs in public procurement?[129] Each measure targets a different stage of the procurement process: division into lots addresses contract size, management of qualification processes addresses excessive eligibility requirements, whilst bid preferences and reserved

[128] See Hoekman and Taş (n 119); Justin Marion, 'Are Bid Preferences Benign? The Effect of Small Business Subsidies in Highway Procurement Auctions' (2007) 91 Journal of Public Economics 1591; Alessandro Ancarani and others, 'A Comparative Analysis of SME Friendly Public Procurement: Results from Canada, Hungary and Italy' (2019) 42 International Journal of Public Administration 1106; Benjamin V Rosa, 'Affirmative Action Subcontracting Regulations in Dynamic Procurement Auctions' (2020) 72 International Journal of Industrial Organization 102657.

[129] See Section 1.4.1 for a discussion on the rationales for selecting these measures.

contracts operate at the award stage to enhance SME competitiveness or ensure contract awards. This research question will be explored in Chapters 4 through 7, with each chapter examining one measure in detail.

Lastly, what trade-offs arise from the implementation of SME-friendly measures in public procurement, particularly with respect to other procurement objectives such as value for money, competition, non-discrimination, and efficiency?[130] This question addresses both the legal design of these measures and their practical implications, including potential effects on market competition and the administrative or financial burden on contracting authorities. The trade-offs incurred by SME-friendly measures can be framed as their respective advantages and disadvantages. However, what is perceived as an advantage in one jurisdiction may be regarded as a disadvantage in another, depending on legal constraints and policy priorities. For example, international obligations under the WTO Agreement on Government Procurement (GPA) can significantly influence the adoption of specific SME-friendly measures.[131] This research question will be addressed throughout Chapters 4 through 7 and synthesised in Chapter 8.

These three interrelated research questions frame the analysis of SME-friendly measures in public procurement law, enabling a comprehensive examination of their

[130] The focus on these objectives reflects their prevalence across procurement systems, though their relative priority varies by jurisdiction, and this will be discussed in each chapter. In this regard, the EU presents particular considerations. In the EU, the fundamental objective is supporting the Internal Market through non-discrimination, whilst value for money and competition remain important at Member State level. See Trybus, 'Beyond Competition and Value for Money: Corporate Social Responsibility in Public Procurement' (n 36) 219.

[131] See Chapter 4. WTO, *Agreement on Government Procurement* (GPA) (adopted 30 March 2012, entered into force 6 April 2014) GPA/113, art IV.

design, implementation, effectiveness, and trade-offs with other procurement objectives.

1.4 Methodology of this Thesis

To answer the research questions outlined in the preceding section, this thesis uses a doctrinal legal research methodology with a multi-jurisdictional illustrative approach, supported by empirical evidence where available. Doctrinal legal analysis forms the foundation of this research, involving a detailed examination of primary legal resources (legislation, regulations, case law) and secondary resources (policy documents and academic literature) to understand how SME-friendly measures are legally structured and implemented.[132] This approach involves identifying, interpreting, and evaluating relevant legislation and case law to elucidate the formal rules and underlying principles governing SME participation in public procurement. The doctrinal analysis serves to establish a coherent legal framework and clarify the conceptual foundations underpinning SME-friendly measures in each of their jurisdictional backgrounds.

This thesis goes beyond pure doctrinal analysis in two important ways:

First, it adopts a multi-jurisdictional illustrative approach that examines how specific measures operate across different legal systems. This thesis is not a comparative legal study in the traditional sense; it does not undertake a systematic comparison of how different legal systems facilitate SMEs to participate in public procurement.[133]

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[132] For an introduction to doctrinal legal research and its various research methods, see Terry Hutchinson and Nigel Duncan, 'Defining and Describing What We Do: Doctrinal Legal Research' (2012) 17 Deakin Law Review 83.

[133] For an analysis of comparative legal research methodology, see Mark Van Hoecke, 'Methodology of Comparative Legal Research' [2015] Law and Method 1.

Rather, it uses targeted jurisdictional examples to analyse each measure in depth where that measure has been most extensively developed. This thesis also offers preliminary observations on why certain measures are prominent in particular jurisdictions. For example, it explains why division into lots became the primary EU approach, whilst reserved contracts dominate US small business policy.[134] These explanations emerge from the detailed analysis of each measure's legal framework and implementation, rather than from systematic comparative analysis.

Second, the thesis integrates empirical evidence regarding the effectiveness of SME-friendly measures. This includes quantitative studies on SME participation rates, qualitative research on barriers faced by SMEs, and evaluation reports on specific measures. The availability of such evidence varies significantly across jurisdictions and measures, but where available, it provides crucial insights into whether legal provisions achieve their intended objectives. This interdisciplinary dimension, drawing on economic and policy analysis alongside legal analysis, is essential because the research questions concern not merely what the law provides but whether it works. This approach explicitly acknowledges and examines trade-offs inherent in reconciling core procurement objectives, such as value for money, with the goal of empowering SMEs. This thesis does not provide an economic analysis of law,[135] but it represents economically informed legal research, which is legal research with an assessment of the economic implications of legal rules, and insights from economic theory.[136]

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[134] See Chapter 8, Section 8.3.

[135] Classic economic analysis of law research, or law and economics research will evaluate the economic efficiency and effects of legal rules, such as the effect on resource allocation, incentives and social welfare. See Robert Cooter and Thomas Ulen, *Law and Economics* (6th edn, Pearson 2016) 3.

[136] Albert Sanchez-Graells, 'Economic Analysis of Law, or Economically Informed Legal Research' in Dawn Watkins and Mandy Burton (eds), *Research Methods in Law* (Taylor & Francis Group 2017) 173.

1.4.1 Scope of the research

This thesis has a focused scope by limiting its analysis to hard-law mechanisms, which are legally binding measures embedded within public procurement law that have enforceability. [137] More specifically, it concentrates on SME-friendly measures incorporated in public procurement law, which impose obligations on contracting authorities, including dividing contracts into lots, managing the qualification process, providing bid preferences, and reserving contracts for SMEs.[138] Soft-law measures, such as capacity-training programmes and voluntary guidance, fall outside the scope of this thesis.[139] Capacity training is a different mechanism that aims to enhance SMEs' capabilities to help them overcome the barriers, whereas legally binding measures are primarily intended to tackle the structural barriers through adjusting rules governing the public procurement system.[140]

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[137] Trybus identified the distinction between hard-law and soft-law approaches in SME-friendly measures. Hard-law measures impose binding obligations on contracting authorities, and soft-law approaches, such as policies or recommendations, which lack enforceability but have practical effects. See Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64). For a discussion on soft law, see Linda Senden, *Soft Law in European Community Law* (Hart Publishing 2004) 112; also see David M Trubek, Patrick Cottrell and Mark Nance, '"Soft Law," "Hard Law," and European Integration: Toward a Theory of Hybridity' (Jean Monnet Working Paper 02/05, NYU School of Law 2005) <https://jeanmonnetprogram.org/archive/papers/05/050201.pdf> accessed 18 June 2025.

[138] Although these measures can also be adopted in soft law, this thesis select jurisdictional examples where these measures are legally binding.

[139] For instance, while consortium bidding is often recognised as an important strategy for enabling SMEs to access larger contracts, it primarily operates through the discretion of economic operators rathe than as a mandated obligation on procuring entities. Public procurement law does not typically mandate or require contracting authorities to promote or accept consortium bids, but it may facilitate such arrangements through specific legal provisions. For instance, rules on qualification criteria may allow members of a consortium to aggregate their economic and financial capacity to meet financial criteria, thereby easing access to participation. This will be further discussed in Chapter 5.

[140] The definition and scope of barriers confronting SMEs in the public procurement system will be explored in Chapter 3.

The focus on hard-law measures is also shaped by the methodology of the thesis, which combines doctrinal analysis with available empirical evidence. The binding and enforceable nature of hard-law measures facilitates the examination of their implementation and effects, whereas the discretionary and context-dependent character of soft-law measures limits the availability and reliability of empirical evidence. To critically assess the practical effectiveness and broader implications of SME-friendly measures in procurement laws, this thesis incorporates empirical data and evidence from government reports and academic literature in economics and management.

The four SME-friendly measures that this thesis focuses on can be further distinguished by the extent of support they provide. Reserved contracts and bid preferences exemplify explicit preferential (SME-favouring) measures in procurement procedures, which are government interventions designed to grant SMEs competitive advantages.[141] By contrast, dividing contracts into lots represents a facilitative measure, which does not grant SMEs a competitive advantage, but aims to tackle a significant barrier faced by SMEs, the large size of public procurement contracts.[142] Managing the qualification process also does not provide SMEs with a preference but facilitate their participation by prohibiting disproportionate qualification criteria and simplifying the procurement process, which is also an example of facilitative measures.[143] The selected measures collectively cover a broad spectrum of means to adjust public procurement law to facilitate or support SME participation.

[141] See Chapter 7 for reserved contracts and Chapter 6 for bid preferences.
[142] See Chapter 4.
[143] See Chapter 5.

1.4.2 Selection of jurisdictions and their roles

This thesis focuses primarily on the measures themselves rather than on the jurisdictions. Each of the four measures examined is analysed in depth, with examples drawn from jurisdictions where these measures have been most extensively developed and implemented. This approach allows for a thorough examination of how each measure operates in practice whilst acknowledging that the legal, economic, and political contexts differ significantly across jurisdictions. Importantly, it must be emphasised that these jurisdictions are not examined equally or systematically across all chapters.

In Chapter 4 (division into lots), the EU is selected due to its long-standing engagement with SME participation in public procurement since the early 1990s, and the introduction of division into lots in Directive 2014/24/EU has generated wide discussion regarding its effectiveness and limitations.[144] Since Article 46 Directive 2014/24/EU adopts a default 'divide or explain' approach to the division into lots, Member States retain considerable discretion in how the measure is transposed in national law.[145] The analysis therefore examines both the EU-level legal framework and its transposition and implementation at the national level. Germany and France are selected as case studies due to their long tradition of supporting SMEs and their extensive use of division into lot prior to the adoption of Directive 2014/24/EU. In fact, this measure is not an innovation introduced by the European Commission, but rather a practice

[144] See Chapter 4.

[145] Directive 2014/24/EU, art 46 (4).

embedded in German and French procurement systems.[146] The case studies further illustrate differing legal designs of lot division, such as rules on lot bundling and limits on the number of lots awarded, and their respective effects on SME participation.[147]

In contrast to dividing contracts into lots, managing the qualification process targets the qualification stage of procurement procedures, which encompasses multiple elements that may pose difficulties for SMEs, such as financial capacity requirements, past experience criteria, and shortlisting practices.[148] These elements can be adjusted to facilitate SME participation without granting explicit preferences over large businesses. In Chapter 5 (managing the qualification process), the EU and the US federal procurement regimes are selected because they represent two influential and well-developed approaches to managing the qualification process, supported by extensive guidance and administrative practice. Both regimes have engaged explicitly with the challenge of balancing risk management by contracting authorities against the need to avoid disproportionate exclusion of SMEs, making them particularly suitable for examining how qualification criteria can be calibrated to improve SME access. In Chapter 5, the analysis on the EU side is confined to Directive 2014/24/EU, rather than extending to Member States. Unlike the division into lots, the SME-friendly measures in the qualification process leave relatively limited discretion to Member States, for example, the caps on minimum turnover requirements.[149] While Member States may adopt more lenient approaches to facilitate SME participation, they are not permitted to exceed the cap set in Article 58(3) Directive 2014/24/EU.[150] As a result, the EU-

[146] ibid.
[147] See Chapter 4, Section 4.3.
[148] See Chapter 5.
[149] See Chapter 5, Section 5.2.1
[150] Directive 2014/24/EU, art 58(3).

level framework provides a relatively complete basis for analysing the legal design of managing the qualification process, without the need for a separate Member State-level examination.

Bid preferences are not widely used across the jurisdictions selected in Chapters 4 and 5. In order to understand how bid preferences operate in practice as an SME-friendly measure, it was therefore necessary to examine jurisdictions in which they are incorporated in public procurement law. Chapter 6 (bid preferences) accordingly draws on examples from Brazil, South Africa, and the US, each of which illustrates a distinct approach to the design and implementation of bid preferences.[151]

Brazil is selected as it has developed an innovative form of bid preference for micro and small enterprises (MSEs), fictitious-tie preferences, which seek to enhance MSE participation without increasing contract prices.[152] This design allows for an assessment of whether bid preferences can be structured to mitigate concerns about value for money, which is a critical question given that such concerns often motivate opposition to preferential measures.[153] Moreover, Brazil implemented bid preferences relatively early (2006), providing sufficient time to observe their implementation and effects on MSEs.[154]

South Africa offers a fundamental different model through its point-based preferential procurement system.[155] Whilst South Africa's framework was designed primarily to support historically disadvantaged individuals (HDIs) and advance broad-based black

[151] See Chapter 6.
[152] ibid, Section 6.2.
[153] See Section 1.2.
[154] See Chapter 6, Section 6.2
[155] See Chapter 6, Section 6.4.

economic empowerment (BBBEE), rather than SME specifically, it remains highly relevant to this research for several reasons.[156] First, SMEs owned by or employing HDIs can qualify for preferential points, meaning SMEs are often beneficiaries even if not the primary target. Second, South Africa's mathematically sophisticated points system represents a distinct design approach that differs from Brazil's fictitious-tie bid preferences. Third, the system has been extensively litigated and revised, culminating in the 2024 Public Procurement Act, providing rich material for analysing how bid preferences can be structured, challenged, and reformed.[157] South Africa thus provides a valuable case for examining how bid preferences function as an SME-friendly measures within a broader redistributive procurement framework, rather than merely as a market access tool for SMEs.

The US presents yet another model, characterised by more restrained use of bid preferences within a procurement system that relies heavily on reserved contracts (examined in Chapter 7) as its primary small business support mechanism. At the federal level, price evaluation preferences exist primarily for HUBZone small businesses, businesses located in historically underutilised business zones, representing a geographically targeted preferential measure with specific developmental objectives, However, this federal bid preference mechanism is implemented on a much narrower scope than reserved contracts and lacks substantial empirical evidence regarding its effectiveness. To understand the effectiveness of bid preferences for small businesses with stronger empirical grounding, Chapter 6 therefore also examines California's state-level small business bid preferences. California was selected specifically because substantial empirical evidence exists

[156] ibid.
[157] See Chapter 6, Section 6.4.

regarding the effectiveness of its price preference system, including econometric studies analysing its impact on small business awards and competition. This evidence base permits meaningful evaluation of whether and how bid preferences affect small business participation and the trade-offs between supporting small businesses and procurement outcomes. California's preference also differs from the federal HUBZone model in applying to small businesses generally rather than to a specific subcategory, enabling assessment of how preferences operate when applied more broadly. The inclusion of both federal and state examples thus illustrates how bid preferences can be calibrated differently depending on policy objectives (geographic development versus broad small business support) whilst also demonstrating the methodological value of examining measures where empirical evidence permits robust evaluation.

Together, these three jurisdictions provide instructive examples of how bid preferences can be designed under varying legal and policy contexts. The diversity of approaches examined enables identification of common design challenges and effectiveness questions that transcend specific jurisdictional contexts, whilst also illustrating how preferences can be adapted to serve different policy objectives, from enhancing market access for SMEs to promoting geographic development or addressing historical economic exclusion.

Lastly, Chapter 7 (reserved contracts), by contrast, focuses exclusively on the set-aside programmes for small businesses in US federal procurement.[158] This focused approach differs from the multi-jurisdictional examination in previous chapters and requires explanation. Within all the measures analysed in this thesis, the US federal set-aside programmes have been implemented for the longest time, with origins dating

[158] See Chapter 7.

back to the Small Business Act of 1953. This extensive implementation history provides the richest body of legal materials, empirical evidence, and practical experience for analysing how reserved contracts operate. Although reserved contracts also exist in other jurisdictions discussed in this thesis, their scope is considerably more limited. In the EU, the reserved contracts regime under Article 20 Directive 2014/24/EU applies only to sheltered workshops and social enterprises, not to SMEs generally.[159] Brazil incorporated a mandatory reserved contracts rule to support MSEs in Contemporary Law 147/2014 (LC 147/2014), but its scope is limited by a rather low threshold, and contracting authorities retain substantial discretion to avoid reserving contracts. [160] South Africa adopted reserved contracts under the new Public Procurement Act 2024, but this provision is not yet in force and therefore cannot be evaluated based on implementation experience.[161]

Chapter 7 (reserved contracts) therefore focuses exclusively on the US federal procurement system. The analysis is confined to the federal level for two reasons. First, US states operate under different public procurement laws with no unification of state procurement rules, making comprehensive state-level analysis impractical. Second, and more importantly, reserved contracts for small businesses in public procurement were stipulated at the federal level through the Small Business Act of 1953, and state-laws have subsequently drawn upon federal models when developing their own small business support measures.[162] The federal system therefore represents both the

[159] Directive 2014/24/EU, art 20.
[160] LC 123/2006 (Brazil); also see Chapter 6, Section 6.2.
[161] PPA 2024 (South Africa); also see Chapter 6, Section 6.4.
[162] Small Business Act 1953, 15 USC § 631 et seq; also see Chapter 7, Section 7.2.

origin and the most comprehensive framework for reserved contracts, making it the natural focus for in-depth analysis of this measure.

Whilst this research does not undertake systematic comparative analysis of different jurisdictions' legal systems, political economies, or administrative cultures, it does identify and explain the prominence of particular measures in specific jurisdictions.[163] For instance, division into lots emerged as the primary EU approach due to the EU's fundamental principle of non-discrimination, which precludes preferential measures for SMEs. Similarly, reserved contracts (set-asides) developed as the cornerstone of US small business policy within the federal procurement system. These preliminary observations on jurisdictional approaches are developed in the concluding chapter based on the detailed analysis of how each measure operates within its legal framework.

1.5 Limitations of this Thesis

While this thesis aims to provide a rigorous and contextualised examination of how legal frameworks shape the design and effectiveness of these measures, certain limitations must be acknowledged. First, this thesis relies on existing empirical evidence rather than original data collection. It draws on available academic research and official evaluation reports to assess the implementation and effectiveness of SME-friendly measures. This thesis does not conduct empirical research through interviews

[163] Comparative legal analysis signifies the systematic application of the comparative technique to the field of law, involving the research in law through systematic comparison of two or more legal system. See WJ Kamba, 'Comparative Law: A Theoretical Framework' (1974) 23 The International and Comparative Law Quarterly 485, 486; P Ishwara Bhat, 'Comparative Method of Legal Research: Nature, Process, and Potentiality' in P Ishwara Bhat, *Idea and Methods of Legal Research* (Oxford University Press 2020).

with contracting authorities or SMEs, or econometric analysis. This has two implications: first, the analysis is constrained by the quality and scope of existing studies; second, where robust empirical evidence exists, more confident claims about effectiveness can be made; where evidence is limited or contradictory, the analysis is necessarily more tentative.

Second, language and literature availability affect the depth of analysis across jurisdictions. This research relies primarily on English-language materials, with some French and German sources where relevant to the analysis. Whilst primary legal sources from all four jurisdictions are available in English, the volume of secondary sources, such as academic literature and official reports, is considerably greater for the EU and the US than for Brazil and South Africa. This affects the depth of contextual and evaluative analysis possible, with the analysis of Brazil and South Africa necessarily relying more heavily on legislative frameworks and official documents than on extensive scholarly debate or independent empirical evaluation.

Third, based on the analysis of how different measures operate across jurisdictions, Chapter 8 identifies key considerations for policymakers and legislators developing or reforming SME-friendly measures. Whilst these principles are grounded in the detailed legal and empirical analysis of specific measures in specific jurisdictions, they are formulated at a level of generality that makes them potentially applicable across different legal and institutional contexts. This is both a strength and a limitation: the principles provide valuable guidance for jurisdictions developing or reforming SME-friendly measures, but they require adaptation to specific circumstances. Because this research examines measures where they are most developed rather than undertaking systematic comparative analysis of how different jurisdictions approach the full range

of measures, the principles represent thematic guidance derived from cross-measure patterns rather than jurisdiction-specific prescriptions. Policymakers and legislators would need to consider their particular legal framework, market conditions, and policy objectives when applying these principles.

In light of these limitations, the thesis makes its primary contribution by examining the legally binding SME-friendly measures in one place, providing a comprehensive overview that has not previously been available in the literature. By examining four distinct measures with specific jurisdictional examples, this thesis enables understanding of the regulatory options available to governments seeking to support SME participation as prime contractors and identifies key considerations for policymakers when selecting, combining, and calibrating these measures.

1.6 Overview of Subsequent Chapters

The thesis is organised in three parts, the first part provides the background for the later analysis of measures (Chapters 2-3), the second part is the main analytical part of the thesis, which examines the effectiveness and limitations of four frequently used SME-friendly measures in public procurement law, consisting of Chapters 4-7. The third part (Chapter 8) synthesises the findings and answers the research questions, comparing the four measures and presenting key considerations for policymakers.

As the first part, Chapters 2-3 provide the conceptual and analytical foundations for the subsequent analysis. Chapter 2 analyses SME definitions and size standards across the four jurisdictions, serving two purposes: delineating the scope of beneficiaries for SME-friendly measures and enabling interpretation of participation

data across different contexts. Chapter 3 addresses the first research question by developing a definition of barriers and examining commonly cited challenges facing SMEs, distinguishing structural barriers requiring regulatory intervention from other factors such as perceptions or competitive disadvantages. This framework underpins the evaluation of measure effectiveness in subsequent chapters.

Building on the conceptual and analytical foundations established in Chapters 2-3, Chapters 4-7 examine four legally binding SME-friendly measures in public procurement. Chapters 4 and 5 analyse two facilitative measures that reduce barriers to participation: division into lots and management of qualification processes.[164] Chapters 6 and 7 examine two preferential measures: bid preferences, which enhance SME competitiveness at the evaluation stage, and reserved contracts, which restrict competition to SMEs only.[165] Each chapter analyses a measure's legal design, implementation, and effectiveness in addressing specific barriers, whilst examining potential trade-offs with other procurement objectives such as value for money, competition, and efficiency.

As the concluding chapter, Chapter 8 synthesises the findings and addresses the research questions. The chapter first evaluates each measure's effectiveness in addressing barriers and enhancing SME participation. It then compares the four measures across three dimensions: contract value, SME eligibility criteria, and implementation incentives. The chapter also offers preliminary observations on jurisdictional patterns, identifying factors that shape measure selection across the EU, the US, Brazil, and South Africa. Building on this analysis, the chapter presents key

[164] See Chapters 4 and 5.
[165] See Chapters 6 and 7.

considerations for policymakers when selecting, combining, and calibrating SME-friendly measures.

Chapter 2 Defining the beneficiary of SME-friendly measures: The Definitions of SMEs

2.1 Introduction

SMEs are often described as the backbone of national economies across countries.[166] However, the criteria for what constitutes an SME vary significantly across different legal systems, reflecting the characteristics of the economic, social and regulatory environment.[167] As introduced in Chapter 1, some SME-friendly measures aim to facilitate SME access by removing the entry barriers facing them, and some explicitly grant them a bid evaluation preference in the bidding process.[168] Regardless of the legal design of such measures, the scope of the beneficiary needs to be clarified and delimited first. Ambiguity in the definition of SMEs may hinder the implementation and practical effectiveness of those measures.[169]

In general, there are two types of criteria used to define SMEs: quantitative criteria and qualitative criteria.[170] Most jurisdictions adopt a combination of both types of indicators to define SMEs.[171] Quantitative criteria include indicators such as the

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[166] For example, see European Commission, 'Entrepreneurship and small and medium-sized enterprises (SMEs)' <https://single-market-economy.ec.europa.eu/smes_en> accessed 08 June 2025; International Labour Organization (ILO), 'MSMEs: The backbone of economies and the world of work' <https://www.ilo.org/resource/msmes-backbone-economies-and-world-work> accessed 08 June 2025.

[167] Meghana Ayyagari, Thorsten Beck and Asli Demirguc-Kunt, 'Small and Medium Enterprises across the Globe' (2007) 29 Small Business Economics 415.

[168] See Chapter 1, Section 1.2.2.

[169] The lack of a clear definition may cause variabilities and inefficiencies in SME public policies. See Adil El Madani, 'SME Policy: Comparative Analysis of SME Definitions' (2018) 8 International Journal of Academic Research in Business and Social Sciences 103.

[170] Martin Senderovitz, 'How Are SMEs Defined in Current Research', (Regional Frontiers of Entrepreneurship Research 2009: 6th International Australian Graduate School of Entrepreneurship AGSE Entrepreneurship Research Exchange, February 2009) 985; also see Gentrit Berisha and Justina Shiroka Pula, 'Defining Small and Medium Enterprises: A Critical Review' (2015) 1 Academic Journal of Business, Administration, Law and Social Sciences 17.

[171] See Berisha and Shiroka Pula (n 170) 21.

number of employees, the total assets and annual turnover or revenue.[172] Qualitative criteria mainly refer to independent ownership and non-dominance in the relevant market.[173] The criterion of independent ownership differs between SMEs and subsidiaries of large businesses.[174] While most jurisdictions combine both, the relative emphasis varies: some rely principally on quantitative thresholds, others place greater weight on qualitative conditions.[175] Compared to qualitative criteria, quantitative criteria are more often adopted due to their convenience in application and for dividing subcategories.[176] The number of employees is the most frequently used indicator, but the thresholds vary significantly across countries.[177] For example, in the United States (US), enterprises with fewer than 2,000 employees are considered small in some industries.[178] However, in the European Union (EU), the upper limit of staff headcount is 250.[179] A small business in the US may be classified as a large one in the EU.

This chapter provides a clear understanding of the term 'SMEs' and lays the groundwork for the following chapters on SME-friendly measures in public procurement law. The following chapters focus on specific SME-friendly measures across different jurisdictions, including the division into lots in the EU, with Germany and France selected to demonstrate the transposition at the Member State level;

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[172] ibid. The term 'revenue' is more frequently used in the US, in Europe the equivalent term is annual turnover.

[173] Berisha and Shiroka Pula (n 170) 22.

[174] J E Bolton, DSC, 'Small Firms: Report of the Committee of Inquiry on Small Firms, Cmnd 4811 (1971).

[175] Berisha and Shiroka Pula (n 170) 21.

[176] Senderovitz (n 170) 986; also see Susanne Durst, Samuel Foli and Ingi Runar Edvardsson, 'A Systematic Literature Review on Knowledge Management in SMEs: Current Trends and Future Directions' [2022] Management Review Quarterly 1.

[177] Adil El Madani (n 169).

[178] See Section 2.3.

[179] Khrystyna Kushnir, 'A Universal Definition of Small Enterprise: A Procrustean Bed for SMEs?'(11 August 2010) <https://blogs.worldbank.org/psd/a-universal-definition-of-small-enterprise-a-procrustean-bed-for-smes> assessed 10 February 2022

managing the qualification process is based on both Directive 2014/24/EU and Federal Acquisition Regulations (FAR) in the US; bid preferences are supported by evidence in Brazil, the US, and South Africa; reserved contracts are based on the experience in US federal procurement. Each of these jurisdictions defines SMEs differently: the EU uses the term 'SMEs' consistently in legislation and policies, although in some Member States, SMEs might be understood differently, for example, Germany, which will be discussed in Section 2.2.2. The US uses the term 'small businesses', without recognising medium-sized enterprises separately.[180] Brazil and South Africa use the term 'micro and small enterprises (MSEs)' instead of SMEs. To facilitate the discussion in this thesis, 'SMEs' is used generally to refer to the target group of SME-friendly measures, 'small business' is used only in the US context, and 'MSEs' in the contexts of Brazil and South Africa.

This chapter does not attempt to propose a uniform SME definition, recognising that contextual factors, including market structure, economic development, and policy objectives, necessarily inform jurisdictional approaches to SME definition and classification. Nevertheless, this chapter compares different definitions of SMEs across the jurisdictions selected for this thesis and assesses which legal framework defines SME status most expansively, i.e. which jurisdiction extends SME-friendly measures in public procurement to the largest enterprises in relative terms. While SMEs are often described as comprising over 99 per cent of enterprises globally, this statistic is arguably circular, since it derives directly from the legal definitions established by each jurisdiction. A more analytical approach requires assessing the scope of SME definitions within respective economic contexts. This involves

[180] See Section 2.3.

examining both the upper eligibility thresholds (annual revenue, employee headcount) and their relative significance when measured against national economic indicators such as GDP per capita and median enterprise size. This is particularly important in the context of preferential measures, as the definition of SMEs delimits the beneficiaries of such measures, which will be discussed in Section 2.6.[181]

2.2 The Definitions of SMEs in the EU

The EU presents an instructive example of SME definitions, illustrating the interplay between supranational harmonisation and national variation within the Internal Market.[182] While the European Commission (the Commission) has established a Recommendation providing standardised criteria for SMEs, intended to promote greater consistency in policies targeting SMEs across the Member States, the latter retain discretion to adopt different thresholds. Germany exemplifies this discretion, having implemented its own definition of SMEs that diverges from the EU definition.[183] This section examines both the EU-recommended definition and the German approach, elucidating how definitional divergences may reflect different policy objectives and economic contexts even within an integrated market.

[181] For a definition of preferential measures for SMEs in public procurement, see Chapter 1, Section 1.2.2. Also see Burgi (n 48).

[182] The internal market is defined as 'an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties'. See TFEU, art 26(2).

[183] See Section 2.2.2.

2.2.1 SME definition at the EU level

At the EU level, SMEs are defined by a unified framework intended to harmonise the understanding of enterprise size classification across all Member States. The Commission Recommendation 2003/361/EC (hereinafter referred to as the 2003 Recommendation) defines an SME as an enterprise that has fewer than 250 employees and an annual turnover not exceeding EUR 50 million.[184] This turnover threshold may be applied alternatively with an annual balance sheet total threshold of EUR 43 million.[185] The Commission's User Guide clarifies that turnover represents the total income that an enterprise receives during a year from the sale of products or provision of services within the company's ordinary activities, after deducting rebates.[186] The annual balance sheet total is the value of an enterprise's main assets.[187] This framework further divides SMEs into three categories: a microenterprise has fewer than 10 employees and an annual turnover or annual balance sheet total not exceeding EUR 2 million; a small enterprise has fewer than 50 employees and an annual turnover or annual balance sheet total not exceeding EUR 10 million; a medium-sized enterprise has fewer than 250 employees and an annual turnover not exceeding EUR 50 million or an annual balance sheet not exceeding EUR 43 million.[188]

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[184] Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises [2003] OJ L124/36, annex art 2. The concept of 'enterprise' encompasses an entity engaged in economic activity, regardless of its legal form.

[185] Recommendation 2003/361/EC, annex, art.2.

[186] Commission: Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs, *User Guide to the SME Definition* (Publications Office, 2020) <https://data.europa.eu/doi/10.2873/255862> accessed 11 August 2025, 13.

[187] ibid; Recommendation 2003/361/EC, annex, art.2.

[188] See European Commission, 'User Guide to the SME Definition' (n 186) 1.

This definition focuses primarily on quantitative criteria, with staff headcount considered as the main criterion.[189] Financial indicators are represented by either annual turnover or annual balance sheet total. The dual financial thresholds accommodate sectoral variations, particularly for manufacturing enterprises that typically generate higher turnover relative to their actual economic scale, for which the balance sheet total serves as a more appropriate size indicator.[190] To address cases where an enterprise marginally exceeded these thresholds, Article 4(2) Recommendation 2003/361/EC provides that SME status is retained unless the thresholds are exceeded for two consecutive accounting periods.[191] This arrangement provides SMEs with more time to prepare for the loss of their SME status and to adapt their operations accordingly. Such a transitional period is particularly relevant in the context of SME policies that confer benefits based on SME status. However, in the context of public procurement, the SME-friendly measures adopted in Directive 2014/24/EU are facilitative in nature, offering no explicit preference to SMEs.[192] As such, losing SME status has little practical impact when participating in public procurement, since there were no direct preferences attached to that status in the first place. This contrasts with the US system, where small business status is a prerequisite for accessing preferential programmes such as set-asides, as discussed in Section 2.3 and Chapter 7.

The staff and financial thresholds apply to individual enterprises, with adjustments required where an enterprise forms part of a larger corporate group. This approach incorporates qualitative consideration by assessing not merely enterprise size but also

[189] Recommendation 2003/361/EC, recital 4.
[190] ibid.
[191] Recommendation 2003/361/EC, annex, art 4(2).
[192] See Chapter 4; also see Trybus and Andrecka (n 55).

the degree of economic independence.[193] An enterprise controlled by a larger entity may possess capabilities exceeding those of a genuinely independent small business, even if formally meeting the size criteria.[194] Under the previous Commission Recommendation 96/280/EC, any enterprise with 25 per cent or more of its capital or voting rights held by other enterprises was not considered autonomous and was therefore excluded from SME status, subject to limited exceptions for specified investor types.[195] The 2003 Recommendation refined this approach through a more nuanced system of 'partner' and 'linked' enterprise categories, requiring proportional or full aggregation of data to reflect the real scale of the business group.[196]

To facilitate calculation, the 2003 Recommendation categorises enterprises into three types: autonomous, partner, and linked enterprises.[197] An enterprise is not considered autonomous if it owns 25 per cent or more of another enterprise, or if 25 per cent or more of its capital or voting rights are held by another enterprise or a group of linked enterprises, unless the holding is by certain exempt investors who are not linked to the enterprise, such as venture capital companies or universities.[198] Enterprises are deemed linked where one has a dominant influence over the management of another. This may occur, for example, where one enterprise holds the majority of the shareholders' or members' voting rights in another, or has the right to appoint or remove a majority of the members of its administrative body.[199] Partner enterprises are those which are not linked but have the following relationship: one enterprise (the

[193] Recommendation 2003/361/EC, recital 8.
[194] ibid, recital 9.
[195] Recommendation 96/280/EC of 3 April 1996 concerning the definition of small and medium-sized enterprises [1996] OJ L107/4, art 1(3).
[196] Recommendation 2003/361/EC, annex, art 3.
[197] ibid.
[198] Recommendation 2003/361/EC, annex, art 3(2).
[199] ibid art 3(3).

upstream enterprise), either individually or together with one or more linked enterprises, owns 25 per cent or more of the capital or voting rights of another enterprise (the downstream enterprise).[200] Linked enterprises have a closer relationship than partner enterprises.

For partner and linked enterprises, staff headcount and annual turnover are calculated on the basis of both the enterprise's own accounts and the relevant consolidated accounts. In the case of linked enterprises, the number of employees is the sum of both staff headcounts in full.[201] For partner enterprises, the data of any directly upstream or downstream partner enterprise is also included on a proportionate basis.[202] The proportion is calculated using whichever is greater: the share in capital or the share in voting rights. Where cross-holdings exist, the higher percentage applies to reflect the stronger link between enterprises.[203] The 2003 Recommendation further clarifies that if 25 per cent or more of an enterprise's capital is held by a public body, it will not be deemed as an SME even if it meets the quantitative thresholds, unless the holding is by an exempt investor such as a public investment corporation.[204]

The calculation rules for linked and partner enterprises are intended to deter large businesses from presenting themselves as SMEs, ensuring that the definition applies to undertakings which genuinely face the challenges of smaller scale. Nonetheless, a subsidiary of a large enterprise may still qualify as an SME if, after aggregation, it remains within the staff headcount and financial ceilings. In this respect, the 2003 Recommendation adopts a less restrictive approach than Recommendation

[200] Recommendation 2003/361/EC, annex, art 3(2).
[201] ibid art 6(2); also see European Commission, 'User Guide to the SME Definition' (n 186) 28.
[202] Recommendation 2003/361/EC, annex, art 6(3).
[203] ibid annex, art 6(2).
[204] Recommendation 2003/361/EC, recital 13.

96/280/EC, which imposed an automatic exclusion where 25 per cent or more of capital or voting rights were held by another enterprise, subject to limited exceptions.[205]

Regarding the application scope of this definition, Article 8 Recommendation 2003/361/EC provides that any EU legislation or programme to be adopted should refer to it.[206] The Public Sector Directive 2014/24/EU does so in Article 83, which specifies that, for the purposes of paragraphs 3 and 4, SME shall be understood as defined in the 2003 Recommendation.[207] Article 83(3) requires Member States to submit a monitoring report every three years on the level of SME participation in public procurement, while Article 83(4) requires them to ensure that relevant information on EU public procurement law is available free of charge to assist contracting authorities and economic operators, particularly SMEs, in complying with the rules.[208]

In summary, the objective of a uniform definition of SMEs in the EU is to remove the barriers within the Internal Market arising from different understandings and treatment of such enterprises across Member States.[209] Although the 2003 Recommendation is not legally binding on Member States, its application can improve the consistency and effectiveness of SME policies and limit the risk of distortions of competition.[210] Although there is currently no explicit preference for SMEs in EU public procurement rules, the use of a common definition reduces the risk of future inconsistencies should preferential measures be introduced. Divergent national criteria of SMEs could

[205] Recommendation 96/280/EC, annex, art 1(3).
[206] Recommendation 2003/361/EC, annex, art 8.
[207] Directive 2014/24/EU, art 83.
[208] ibid art 83(4).
[209] Recommendation 2003/361/EC, recital 1.
[210] ibid.

otherwise lead to discrimination contrary to the fundamental principle of non-discrimination in EU law.[211] For example, if Germany were to define an enterprise with up to 500 employees as an SME, while France retained the 250-employee ceiling, a French SME could find itself competing in Germany's SME preferential programmes against a significantly larger German SME. A unified definition ensures that any potential SME preferences would, in principle, be applied equally. [212] In practice, however, whether such preferences could be implemented in a genuinely equal manner is open to doubt.[213]

2.2.2 SME definition at the national level – Germany

Among the Member States, the SME definition in the 2003 Recommendation is not legally binding unless expressly incorporated into national law. Recital 7 Recommendation 2003/361/EC provides that Member States may apply lower staff or financial ceilings if they wish to target a specific category of SMEs.[214] Most Member States have adopted this definition in their national legislation.[215] For example, in France, the government formally defines SMEs in the French law on the modernisation of the economy (*loi de modernisation de l'économie*, LME) in 2008, which is consistent with the definition set out in the 2003 Recommendation.[216]

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[211] TFEU, art 18(1) and art 34.

[212] For a similar view on this, see Yukins and Piga (n 123) 225.

[213] See Chapter 8, Section 8.3.2.

[214] Recommendation 2003/361/EC, annex, art 7

[215] European Commission, 'User Guide to the SME Definition' (n 186) 28.

[216] Before LME was enacted, a threshold of 500 employees was mainly used to define SMEs in France. See *loi n° 2008-776 du 4 août 2008 de modernisation de l'économie*, LME; also see Eurofound, *Born Global: The Potential of Job Creation in New International Businesses* (Publications Office of the

Although there is no legally binding definition of SMEs in Germany, a widely used policy-based definition is provided by the Federal Ministry for Economic Affairs and Energy and by the *Institut für Mittelstandsforschung (IfM) Bonn*.[217] Under this approach, SMEs are defined as businesses with fewer than 500 employees or an annual turnover of up to EUR 50 million.[218] While the turnover ceiling aligns with the EU 2003 Recommendation, the employee threshold is double the EU limit, reflecting the relatively larger average size of German enterprises.[219]

In Germany, there is another category of enterprises often compared with SMEs, the '*Mittelstand'*, which is frequently described as the backbone of the German economy.[220] Although the terms SME and *Mittelstand* are sometimes used interchangeably, even on official government websites, their defining characteristics differ.[221] Many enterprises that exceed the EU SME thresholds, or even the 500-

European Union 2012) <https://www.eurofound.europa.eu/system/files/2021-05/EF12477EN.pdf> accessed 26 July 2025.

[217] See Federal Ministry for Economic Affairs and Energy, 'SMEs are driving economic success facts and figures about German SMEs' (SME Policy, 30 January 2018) <https://www.bundeswirtschaftsministerium.de/Redaktion/EN/Publikationen/Mittelstand/driving-economic-success-sme.html> accessed 26 July 2025.

[218] IfM BONN, 'SME definition of the IfM Bonn' <https://www.ifm-bonn.org/en/index/definitions/sme-definition-of-the-ifm-bonn> accessed 25 April 2022. The Ifm Bonn is a research institute established in 1957 and its main research area is SMEs, Mittelstand and economy. Also see Hansjörg Herr, Zeynep M. Nettekoven, 'The Role of Small and Medium-sized Enterprises in Development: What Can be Learned from the German Experience?' (2018) Global Labour University Working Paper, No. 532.

[219] IfM Bonn, 'SMEs in the EU: Comparison' <https://www.ifm-bonn.org/en/statistics/mittelstand-themes/sme-in-the-eu-comparison> accessed 13 July 2025.

[220] D B Audretsch and E E Lehmann, *The Seven Secrets of Germany: Economic Resilience in an Era of Global Turbulence* (Oxford University Press 2016) 15.

[221] On the website of the Federal Government, it is said that SME is know as Mittelstand in German and referred to the EU definition, See Federal Ministry for Economic Affairs and Energy, 'The German Mittelstand as a model for success', (Ministry website) <https://www.bundeswirtschaftsministerium.de/Redaktion/EN/Dossier/sme-policy.html> accessed 08 June 2025.

employee threshold, still consider themselves as *Mittelstand*.[222] This is because *Mittelstand* is defined primarily by qualitative rather than quantitative criteria.

There is no statutory definition of *Mittelstand*, according to the IfM Bonn, it refers to companies in which up to two natural persons (or their family members) hold at least 50 per cent of the company shares and are also part of the company's management.[223] The concept, therefore, encompasses both independent SMEs and large family-owned businesses.[224] The core feature is the unity of ownership and management, excluding listed companies from this category.[225] Owner-managers are able to determine the strategic direction of the business, often treating it as a lifetime commitment rather than a short-term investment.[226] *Mittelstand* companies generally have high equity ratios, are not listed on capital markets, and are guided as much by personal values as by purely economic considerations.[227] An SME may be affiliated with another enterprise, but a *Mittelstand* is, by definition, independent.[228] A company with more than 500 employees may qualify as *Mittelstand*, but will not meet the SME definition.

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[222] IfM Bonn, 'SME definition of the IfM Bonn' (n 218).

[223] Ibid; also see McKinsey, How the German Mittelstand is Mastering the COVID-19 crisis, (20th May 2020) <https://www.mckinsey.com/business-functions/mckinsey-digital/our-insights/how-the-german-mittelstand-is-mastering-the-covid-19-crisis> accessed 10 February 2022.

[224] IfM Bonn, 'The economic contribution of small and medium-sized enterprises remains high despite the current crises' <https://www.ifm-bonn.org/en/news/meldung/the-economic-contribution-of-small-and-medium-sized-enterprises-remains-high-despite-the-current-crises> (Press Release, 12 August 2024) accessed 10 June 2025.

[225] Friederike Welter and others, 'German Mittelstand – Between Facts and Perceptions' (IfM Bonn, IfM-Materialien No 234, 2015) 2.

[226] Mark Lehrer and Stefan Schmid, 'Germany's industrial family firms: Prospering islands of social capital in a financialised world?' (2015) 19(4) Competition & Change 301.

[227] Welter and others (n 225).

[228] André Pahnke, Friederike Welter and David B Audretsch, 'In the Eye of the Beholder? Differentiating between SMEs and Mittelstand' [2022] Small Business Economics <https://link.springer.com/10.1007/s11187-022-00612-x> accessed 24 April 2022.

In summary, *Mittelstand* and SMEs have a significant intersection but also have differences. The absence of a quantitative threshold means *Mittelstand* companies can retain their status even as they grow, allowing owners to focus on long-term, sustainable development without the constraints of size limits.[229] However, this also creates uncertainty as to the intended beneficiaries of any size-linked support measures. In public procurement, Germany has a long tradition of *Mittelstand-friendly* measures, notably through dividing large contracts into lots, which will be discussed in Chapter 4. This approach does not confer explicit preference on a specific group, meaning that both *Mittelstand* and SMEs can benefit, and size standards are of limited relevance. By contrast, in the context of preferential measures that target a defined group, size standards become critical in determining eligibility, as will be seen in the next section on small businesses in the US.

2.3 The Definition of Small Businesses in the US

The US uses a markedly different approach to defining what it terms 'small business', with the term SME being less prevalent in the US context. Medium-sized enterprises are not recognised as a distinct category within the regulatory framework. Rather than adopting a blanket definition, the US utilises industry-specific size standards established by the Small Business Administration (SBA).[230] The governing legislation

[229] ibid. also see David B Audretsch, Erik E Lehmann and Julian Schenkenhofer, 'Internationalization Strategies of Hidden Champions: Lessons from Germany' (2018) 26 Multinational Business Review 2.

[230] Small businesses in the U.S. vary in size and are represented in all industries of the national economy, including manufacturing, farming, services, and other industries. See United States International Trade Commission, 'Small and Medium-Sized Enterprises: Overview of Participation in U.S. Exports' (Publication 4125, January 2010) <https://www.usitc.gov/publications/332/pub4125.pdf> accessed 08 June 2025.

comprises the Small Business Act (15 USC § 632) and SBA regulations (13 CFR § 121), which delegate authority to the SBA Administrator to establish detailed criteria.[231]

In the US, the small-business size standards are not merely a statistical tool; they are directly embedded in the federal procurement framework. Small-business status determines eligibility for a range of procurement-based preferences, most notably small business set-asides, which are contracts reserved exclusively for small businesses to bid for and prohibit large businesses from submitting offers.[232] For each federal contract, the contracting officer must assign a single NAICS code and apply the corresponding small business size standard, which determines the scope of businesses that are eligible to compete when the contract is reserved for small businesses.[233] Thus, the size standards of small businesses delimit the beneficiaries of preferential programmes in federal procurement.

The Small Business Act mandates that the Administrator ensure size standards vary across industries to reflect the diverse characteristics of different sectors.[234] The industry-specific size standards established by the SBA are based on the 4-digit North American Industry Classification System codes (NAICS codes).[235] The SBA's Table of Size Standards provides comprehensive coverage, listing every NAICS industry alongside its corresponding thresholds.[236] The rationale underlying this approach is to tailor small business size standards to their specific contexts.[237] A unified size

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[231] See 15 USC § 632; 13 CFR § 121.
[232] See Chapter 7.
[233] 13 CFR § 121.402(b).
[234] 15 USC § 632(a)(3).
[235] 13 CFR § 121.201.
[236] ibid.
[237] United States Census Bureau, *What Is a Small Business?* (U.S. Census Bureau, 19 January 2021) <https://www.census.gov/library/stories/2021/01/what-is-a-small-business.html> accessed 05 June 2025.

standard that proves suitable for one industry may be inappropriate for another. In determining size standards, the SBA defines thresholds that typically encompass 97 per cent of enterprises and 30 per cent of annual receipts within each industry.[238]

The size standards established by the SBA are expressed in either total receipts (revenue) or the number of employees.[239] Most industries require only one type of size standard.[240] The SBA reviews these size standards every five years to account for inflation impacts.[241] Under 13 CFR § 121.104, 'receipts' encompass all revenue received or accrued from any source, including sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances.[242] Average annual receipts are calculated by dividing total income over the five most recently completed fiscal years.[243] The calculation of employee number includes all individuals employed on full-time, part-time, or other bases, including those obtained from temporary employee agencies, professional employee organisations or leasing concerns.[244] The calculation is based on employee numbers for each pay period during the preceding 24 calendar months.[245] Unlike EU calculation methods,

[238] Congressional Research Service (CRS), *Small Business Size Standard: A Historical Analysis of Contemporary Issues* (R40860) <https://crsreports.congress.gov/> accessed 05 June 2025, 2.
[239] Annual receipts refer to all revenue in whatever form received or accrued from whatever source. See 13 CFR § 121.104 (a).
[240] 13 CFR § 121.201. For example, the maximum of a firm's average annual receipts is USD 1 million to be a small business specializing in Soybean Farming. Its number of employees is not required to be under a certain level.
[241] See Small Business Administration (SBA), 'Small Business Size Standards: Adjustment of Monetary-Based Size Standards, Disadvantage Thresholds, and 8(a) Eligibility Thresholds for Inflation' (19 July 2023) 88 *Federal Register* 46048.
[242] 13 CFR § 121.104(a).
[243] 13 CFR § 121.104(c)(1).
[244] 13 CFR § 121.106(a).
[245] 13 CFR § 121.106(b)(1).

the US treats part-time and temporary employees identically to full-time employees.[246] Where affiliates exist, both the business and its affiliates' average number of employees are included in the calculation.[247]

Beyond size criteria, the definition of small businesses requires meeting independence requirements similar to those under the EU SME definition. To qualify, a business must be independently owned and operated for profit within the US, meaning it must be free from large company control and lack dominant market power.[248] The SBA applies a set of affiliation rules to determine the independence of a small business.[249] In principle, where one enterprise controls or has the power to control another, the two are treated as affiliates.[250] In such cases, the employee numbers and annual receipts of all affiliates are aggregated for the purpose of assessing size.[251] This approach prevents subsidiaries of large businesses from qualifying for small business preferences.

In comparison, the US approach is more stringent than the EU methodology for addressing subsidiaries. While the EU framework takes account of the degree of linkage between enterprises, the US SBA requires aggregation wherever control or power to control exists, irrespective of the extent to which it is exercised. In the US, explicit preferential programmes for small businesses confer tangible advantages, such as reserved contracts in federal procurement.[252] A rigorous definition is therefore

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[246] 13 CFR § 121.106(b)(2). The EU approach counts annual work unit (AWU); for example, two part-time workers are regarded as one employee in the EU. See Recommendation 2003/361/EC, annex, art 5.

[247] 13 CFR § 121.103.

[248] 15 USC § 632 (a)(1); 13 CFR § 121.301.

[249] 13 CFR § 121.103.

[250] 13 CFR § 121.103 (a)(1).

[251] 13 CFR § 121.103 (a)(6).

[252] See Chapter 7 on reserved contracts in US federal procurement.

essential to prevent large businesses from securing the benefits intended for genuinely small businesses. Additionally, small businesses must operate mainly within the US or contribute significantly to the American economy through taxation or utilisation of American products, materials, or labour.[253]

Although the US definition of small businesses offers flexibility and is relatively convenient to apply, it is not without shortcomings. The reliance on quantitative thresholds makes the system susceptible to manipulation. In some cases, businesses may deliberately remain below the relevant thresholds to retain small business status; in others, they may alter their business activities to fall within a NAICS code that has a more advantageous standard, such as an employee-based ceiling rather than a financial one. It has been noted that such incentives are amplified in the US context, as the small-business status determines eligibility for substantial preferential measures, notably reserved contracts in federal procurement, thereby increasing the motivation for businesses to avoid 'growing' out of small-business status.[254]

The incorporation of qualitative aspects may compensate for the shortcomings of quantitative criteria. The Small Business Act stipulates that a small business must not be dominant in its field of operation, but provides no statutory definition of dominance, instead delegating to the SBA the authority to determine if a business is dominant.

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[253] See 13 CFR § 121.105 (a)(1). Foreign businesses cannot qualify as small businesses in the US, which means that preferential programmes for small businesses in federal procurement are only applicable to US small businesses, which might raise concerns from trade partners, as will be discussed in Chapter 8. See Christopher R. Yukins, 'The U.S. Federal Procurement System: An Introduction' (2017) UPPHANDLINGSRÄTTSLIG TIDSKRIFT 69, 78.

[254] William Lucyshyn and John Rigilano, Evaluating the Impact of Small Business Set-Asides On Acquisitions Efficiency, (Acquisition Research Program June 2017) https://dair.nps.edu/handle/123456789/1457 accessed 06 August 2025; also see Yukins and Piga (n 123) 229.

Without a transparent framework for assessing dominance, this qualitative safeguard remains largely unused.[255]

Moreover, the intricacy of industry-specific size standards also creates operational challenges, as 13 CFR § 121.402(b) permits contracting officers to assign only one NAICS code and only one corresponding size standard to each federal contract.[256] For example, 'Poured Concrete Foundation and Structure Contractors' and 'Highway, Street, and Bridge Construction' are subject to two different size standards, the latter with a higher annual receipts ceiling.[257] This requires careful decision-making of contracting officers, as the choice of NAICS code directly affects the pool of eligible bidders in a reserved contract for small businesses. Accordingly, contracting officers must verify that a prospective contractor qualifies as a small business before awarding such contracts.[258]

Interestingly, the industry segmentation by NAICS codes also functionally encourages or facilitates the disaggregation of procurement, as solicitations (calls for tenders) are sector-specific. For example, under 'Sector 23 Construction', different codes correspond to flooring, framing, roofing, etc., which allows specialised small businesses to participate more readily than they might in a single contract containing different types of construction activities. This may explain why contract division into lots is not the primary approach for supporting small businesses in US federal procurement, as the contracts are already segmented by sector (subject matter).[259]

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[255] Major Clark and Chad Moutray, 'The Future of Small Businesses in the U.S. Federal Government Marketplace' (2004) 4 Journal of Public Procurement 450.
[256] 13 CFR § 121.402 (b).
[257] 13 CFR §121.201, Sector 23 Construction.
[258] 13 CFR § 121.411; 48 CFR § 19.301-1(b).
[259] See Chapter 4 for a detailed analysis on the division into lots regime.

Instead, reserved contracts serve as the principal support mechanism.[260] Additionally, the FAR establishes limitations on contract bundling, which is a practice of combining two or more separate procurement contracts with different NAICS codes into larger, more complex contracts.[261]

Lastly, while the definition of a small business is not limited to incorporated entities, it requires the enterprise to operate in a legal form, such as a sole proprietorship, partnership, limited liability company, etc.[262] To participate in federal procurement and benefit from small business set-aside programmes, a business must be formally registered in the System for Award Management (SAM) and self-certify its small business status annually in accordance with the applicable SBA size standards.[263] Federal agencies are required to apply SBA size standards in reserved contracts for small businesses, and contracting officers must ensure that the NAICS code assigned to a contract corresponds to the size standard under the business claims eligibility. [264] Under the FAR, there are several reserved contracts programmes (set-asides) for specific subgroups of small businesses, including women-owned small businesses (WOSB), service-disabled veteran-owned small businesses (SDVOSB), 8(a) businesses, and those situated in Historically Underutilised Business Zones (HUBZone).[265] To participate in these socioeconomic set-asides, businesses must first self-certify their status by registering in SAM and selecting the appropriate

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[260] See Chapter 7.

[261] For the definition of bundling, see 48 CFR § 2.101; for the limitation on bundling, see 48 CFR § 7.107-3.

[262] 13 CFR § 121.105(b).

[263] 13 CFR § 121.404(g); 48 CFR § 4.1102.

[264] 13 CFR § 121.402(b)–(c); 48 CFR § 19.303(a)(2).

[265] 48 CFR § 19.8 (8(a) Program), § 19.13 (HUBZone Program), § 19.14 (SDVOSB Program), and § 19.15 (WOSB Program). To facilitate discussion, these subgroups of small businesses are termed as ‘socioeconomic small businesses’ in this thesis.

representation under FAR 52.219-1.[266] For certain set-aside programmes mentioned above, businesses must obtain formal SBA certification, rather than relying solely on self-certification. The reserved contracts programmes for small businesses will be discussed in detail in Chapter 7.

2.4 The Definition of MSEs in Brazil

In Brazil, the term micro and small enterprises (MSEs) is used rather than SMEs, as medium-sized enterprises are not recognised as a specific category under Brazilian law.[267] *Lei Complementar 123*/2006 (LC 123/2006), known as the General Law of MSEs, defines MSEs based on annual gross revenue.[268] Under the current thresholds, which have been periodically updated since the law's enactment, a microenterprise is defined as having annual gross revenue up to BRL 360,000.[269] A small enterprise has annual gross revenue between BRL 360,000 and BRL 4.8 million.[270] Notably, unlike EU and US definitions, annual gross revenue serves as the sole criterion for classifying enterprises as MSEs, with no employee thresholds applied.

The reliance on gross revenue as the exclusive criterion presents both advantages and disadvantages. Revenue proves more difficult for businesses to manipulate

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[266] 'Representation' means whether it is a small business or a socioeconomic small business. See 48 CFR § 52.219-1

[267] Whenever the term 'MSEs' is used in this thesis, it refers to micro and small enterprises, but it does not explicitly refer to Brazilian MSEs as South Africa also provides preferential treatment for MSEs, rather than SMEs.

[268] Grégory Dos Passos Carvalho and Denilson Bandeira Coêlho, 'Diffusion of the Micro and Small Business Law in Municipalities of São Paulo' (2023) 57 *Revista de Administração Pública* <http://www.scielo.br/scielo.php?script=sci_arttext&pid=S0034-76122023000300503&tlng=en> accessed 11 June 2025.

[269] *Lei Complementar No 123, de 14 de dezembro de 2006*, art 3 (LC 123/2006) (Brazil).

[270] ibid.

compared to employee numbers, which can be distributed across multiple legal entities to circumvent thresholds.[271] However, revenue volatility may result in enterprises exceeding thresholds due to inflation alone, causing loss of MSE status despite unchanged headcount and market position. In this regard, the EU definition provides a two-year buffer to prevent reclassification due to temporary fluctuations, ensuring enterprises lose SME status only when headcount and financial ceilings are exceeded for two consecutive accounting periods.[272] Similarly, the US definition uses five-year average revenue calculations rather than single-year assessments for eligibility determinations.[273] Additionally, the independence criterion is embedded within the definition of MSEs in LC123/2006, designed to benefit autonomous MSEs rather than entities integrated into larger corporate structures.[274] This is operationalised through eligibility criteria in Article 3 §4 LC123/2006, which disqualify enterprises owned by, jointly managed with, or otherwise formally linked to other legal entities.[275]

Moreover, Article 3 §4 LC 123/2006 excludes entities that are subsidiaries or representations in Brazil of foreign companies, ensuring only domestic companies receive MSE treatment under LC 123/2006, consistent with Article 170(IX) Federal Constitution mandating preferential treatment for MSEs organised under Brazilian laws with headquarters and management in Brazil.[276] LC 123/2006 dedicates a

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[271] Tom Gibson and H.J. van der Vaart, *A Less Imperfect Way of Defining Small and Medium Enterprises in Developing Countries* (Brookings Institution 2008) <https://www.brookings.edu/wp-content/uploads/2016/06/09_development_gibson.pdf> accessed 28 July 2025, 4.

[272] Recommendation 2003/361/EC, annex, art.4.

[273] 13 CFR § 121.104(c)(1).

[274] LC 123/2006, art 3 § 4.

[275] LC 123/2006, art 3 § 4

[276] *Constituição da República Federativa do Brasil de 1988* (Federal Constitution of Brazil), art 170(IX); LC 123/2006, art 3 §4 (II).

chapter to preferential treatment of MSEs in public procurement, implementing the constitutional mandate, which requires government support for MSEs as a means of promoting social and economic development.[277] LC123/2006 operationalises this through measures including reserved contracts, bid preferences, and subcontracting quotas designed to foster inclusion and competition among MSEs.[278] Lastly, the definition of MSEs in LC123/2006 requires formal registration, reflecting the government's commitment to increasing the proportion of formal business in the national economy, particularly within the MSE sector.[279] In 2010, approximately 10 million companies operated in Brazil, with only half being legally formalised.[280] Given that MSEs often lack resources for administrative procedures, the proportion of legally formalised MSEs likely falls below 50 per cent of all MSEs. This issue resembles the situation in South Africa, as discussed in the next section. By contrast, the substantially lower informal employment rates in the EU (approximately 15 per cent) and the US (approximately 18 per cent) indicate correspondingly higher levels of business formalisation in those jurisdictions.[281] In the EU and the US, SME-friendly measures can reach a broader proportion of the small business sector because most enterprises operate within the formal economy. Conversely, in Brazil and South Africa, such measures reach a more limited segment of small enterprises due to a relatively higher

[277] Federal Constitution of Brazil, arts 170(IX), 179.

[278] Chapter 6 will discuss the bid preference regime under LC123/2006 in detail. See Chapter 6, Section 6.2.

[279] LC 123/2006 art 3; see Janine Berg, 'Laws or Luck? Understanding Rising Formality in Brazil in the 2000s' in S Lee and D McCann (eds), *Regulating for Decent Work* (Palgrave Macmillan 2011)

[280] See Daniel Pezzutti Ribeiro Teixeira, 'The Brazilian Experience of Using Public Procurement Policies to Promote the Development of Micro and Small Enterprises from the Legal Point of View' (Paper presented at the 4th International Public Procurement Conference, Seoul, South Korea, 26–28 August 2010) 21 <https://www.ippa.org/IPPC4/Proceedings/13ProcurementPreferences/Paper13-3.pdf> accessed 24 April 2025, 9.

[281] Fernando G Benavides, Michael Silva-Peñaherrera and Alejandra Vives, 'Informal Employment, Precariousness, and Decent Work: From Research to Preventive Action' (2022) 48 Scandinavian Journal of Work, Environment & Health 169.

level of informality, potentially reducing their overall economic impact and effectiveness in achieving the objectives of SME-friendly measures.[282]

2.5 The Definition of MSMEs in South Africa

In South Africa, the legal definition of micro, small, and medium-sized enterprises (MSMEs) is established through ministerial regulations issued pursuant to the National Small Business Act 102 of 1996 (NSBA), as amended by the National Small Enterprise Amendment Act 21 of 2024.[283] Unlike the previous amendment in 2004, which prescribed the thresholds in the act itself, the amendment in 2024 deliberately delegates the threshold-setting authority to the Minister of Small Business Development, enabling regular updates in response to changes in the economy.[284] Under this delegated authority, although no binding regulation on MSME standards has yet been promulgated, the Minister published an MSME policy in 2025, which provides the most recent size thresholds applicable to such enterprises.[285] The policy adopts a sector-specific approach to annual turnover ceilings, whilst applying a uniform employee headcount across all sectors.[286] Under this framework, a microenterprise is defined as employing no more than 10 persons; a small enterprise as employing up to 50 persons; and a medium-sized enterprise as employing up to

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[282] The objectives of SME-friendly measures may differ across jurisdictions, which will be discussed in the corresponding chapters.

[283] National Small Business Act 102 of 1996, as amended by National Small Enterprise Amendment Act 21 of 2024 (Republic South Africa, RSA).

[284] ibid, ss 7-8.

[285] Department of Small Business Development, *SMMEs and Co-operatives Funding Policy* (Government Gazette No 52109, 13 February 2025) <https://www.gov.za/sites/default/files/gcis_document/202502/52109gon5869.pdf> accessed 29 July 2025.

[286] ibid.

250 persons.[287] The corresponding annual turnover standards range from ZAR 5 million to ZAR 220 million, depending on the sector in which the enterprise operates.[288]

Additionally, South Africa introduced the definition of Exempted Micro Enterprises (EMEs) and Qualifying Small Enterprises (QSEs) in the context of the Broad-Based Black Economic Empowerment (BBBEE) initiative.[289] Under the BBBEE Codes of Good Practice, an EME is defined as a business with turnover below ZAR 10 million, and a QSE is one with turnover between ZAR 10 million and ZAR 50 million.[290] These definitions differ from the NSBA's general SME definition, but they are used specifically for preference scoring in public procurement. The existence of multiple definitions creates complexity, as a business may qualify as 'small' under one standard while failing to meet the criteria of another. Generally, an enterprise with turnover exceeding ZAR 50 million is neither an MSME under the NSBA nor a QSE under the BBBEE framework and is regarded as a large enterprise for most policies.

South Africa's economy exhibits a duality: a formal sector dominated by large enterprises alongside a vast number of small, predominantly informal businesses, especially in townships and rural areas.[291] The majority of MSMEs in South Africa operate on an informal basis, with only 37 per cent being formally registered.[292]

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[287] Department of Small Business Development, *SMMEs and Co-operatives Funding Policy* (2025) (n 285).

[288] ibid.

[289] Broad-Based Black Economic Empowerment Amendment Act 53 of 2003, as amended by Broad-Based Black Economic Empowerment Act 46 of 2013 (BBBEE Act).

[290] Broad-Based Black Economic Empowerment Act: Code of Good Practice, Paras 4-5 (Government Gazette 36928, 11 October 2013) (BBBEE Code of Good Practice).

[291] Al Berry et al, The Economics of SMMEs in South Africa (Trade and Industrial Policy Strategies, December 2002) <https://www.tips.org.za/files/506.pdf > accessed 12 August 2025, 6; also see SME South Africa, 'A Guide to South African Township Economy' <https://smesouthafrica.co.za/sme-guides/a-guide-to-south-africas-township-economy/> accessed 12 August 2025.

[292] Department of Small Business Development, *SMMEs and Co-operatives Funding Policy for South Africa* (Government Gazette, No. 48483 655, 28 April 2023)

However, legal registration in South Africa constitutes a prerequisite both for MSME qualification and eligibility to participate in public procurement.[293] Some argue that the public procurement system should facilitate or provide preferences for small businesses from the informal sector, rather than exclusively limiting to the formal sector.[294] Nevertheless, this regulatory approach is intentional, reflecting the government's policy of encouraging formalisation through simplified registration procedures and the creation of a more supportive business environment.[295]

The South African Constitution provides the legal foundation for contracting authorities to provide preferences for individuals previously disadvantaged by unfair discrimination.[296] The Preferential Procurement Policy Framework Act (PPPFA), enacted in 2000, served as the primary legislation governing preferential procurement for over two decades.[297] Under the PPPFA regime, MSME status does not automatically entitle a business to benefit from the preferential procurement framework; enterprises must satisfy additional eligibility criteria to qualify as either an EME, with an annual turnover under ZAR 10 million, or a QSE, with an annual turnover between ZAR 10 million and ZAR 50 million.[298] However, the new Public Procurement Act 28 of 2024 (PPA 2024) replaces the previous preference point system with a combination of preferential measures, particularly reserved contracts.[299] Significantly, the PPA

<https://www.dsbd.gov.za/sites/default/files/Final%20Gazetted%20SMMEs%20and%20Co-operatives%20Funding%20Policy.pdf> accessed 29 July 2025.

[293] Public Procurement Act 28 of 2024, 31 (2)(a)(iii) (Government Gazette(GG), Vol. 709, No. 50967, 23 July 2024) (South Africa).

[294] Annerita Maritz, 'Gender-Responsive Public Procurement under the Broad-Based Black Economic Empowerment Act: Benefits and Challenges' (2022) 9 African Public Procurement Law Journal 76.

[295] Al Berry et al (n 291) 2.

[296] Constitution of the Republic of South Africa, 1996, s 217(1).

[297] Preferential Procurement Policy Framework Act 5 of 2000 (PPPFA).

[298] BBBEE Code of Good Practice, pt 2.

[299] Public Procurement Act 28 of 2024(Government Gazette 50967, 23 July 2024), Chapter 4. The use of reserved contracts to support small businesses will be discussed in detail in Chapter 7 of this thesis.

2024 explicitly references the definition of MSMEs established in the NSBA, enabling MSMEs to benefit from preferential treatment, such as reserved contracts, where contracting authorities choose to implement such measures.[300]

Although the PPA 2024 was approved by the President on 23 July 2024, it is still not in force.[301] The PPPFA and associated PPPFA Regulations 2022 continue to govern procurement processes, which provide no clear guidance regarding the treatment of MSMEs. Neither the PPPFA nor the PPPFA Regulations 2022 reference MSMEs, EMEs, or QSEs as defined in the BBBEE Act. Under the PPPFA, contracting authorities retain discretion to define specific goals, which correspond to beneficiary groups.[302] Section 2(1)(d) PPPFA stipulates that specific goals may encompass contracting with individuals 'historically disadvantaged by unfair discrimination on the basis of race, gender or disability', and implementing the programmes outlined in the Reconstruction and Development Programme (RDP) 1994, which includes supporting MSME access to public procurement.[303] While it remains possible for MSMEs to benefit from preferential procurement, the current legal framework lacks certainty regarding their eligibility and treatment.[304]

In summary, MSMEs in South Africa are defined using similar criteria to other jurisdictions examined in this chapter, using employee numbers and annual turnover thresholds. However, MSMEs do not automatically qualify for preferential treatment in

[300] National Small Business Act 102 of 1996, s 1 (as amended). A small enterprise refers to a separate and distinct business entity, together with its branches or subsidiaries, classified as a micro, small, or medium enterprise which satisfy the prescribed criteria.

[301] Public Procurement Act 28 of 2024, s 69(1).

[302] PPPFA, s 2(1)(d).

[303] Republic of South Africa, *White Paper on Reconstruction and Development* (Government Gazette No 16085, 23 November 1994), para 3.10.2.

[304] This will be further discussed in Chapter 6.

public procurement. This reflects the distinct objective of South Africa's preferential procurement system: redressing individuals who were discriminated against in the past and reducing inequality in the economy, rather than supporting the MSME sector.[305] Consequently, the currently effective public procurement law contains no dedicated SME-friendly measures; it establishes a complex preferential procurement framework from which MSMEs may benefit.

This contrasts with other jurisdictions analysed in this thesis, where public procurement legislation refers to consistent SME definitions and provides greater legal certainty for SMEs participating in public procurement. Additional criteria are typically required only when preferential treatment targets specific categories of small businesses, as observed in US federal procurement. Such legal certainty ensures that SMEs understand available supportive measures and eligibility criteria, thereby encouraging greater participation. South Africa's preferential procurement system, while intricate and socially oriented, appears *prima facie* strongly committed to supporting historically disadvantaged groups. However, the lack of clarity in defining the beneficiary groups may compromise the effectiveness of these measures, raising questions about whether the intended social objectives can be achieved. This question will be further discussed in Chapter 6.

[305] See Chapter 6, Section 6.4.

2.6 A Comparison of SME Size Standards

The rationale for defining SMEs is to identify entities that face disadvantages due to smaller scale and target supportive policies towards them,[306] and one of the policies is to facilitate their access to public procurement opportunities.[307] Across the four jurisdictions examined, there are both similarities and divergences in SME definitions and their alignment with public procurement frameworks.

All four jurisdictions share common definitional elements: at least one quantitative criterion and often an independence requirement to exclude subsidiaries of large businesses. Additionally, formal registration is universal required for participating in public procurement procedures, meaning that informal SMEs are excluded from direct participation. This requirement has different implications in emerging economies, such as Brazil and South Africa, where informal businesses constitute a larger proportion of the SME sector compared to the EU and the US. Consequently, SME-friendly measures in public procurement reach a broader scope of enterprises in more developed economies, where formal business registration is more prevalent.

Although there is no universally accepted definition of SMEs, Gibson and van der Vaart have proposed a formula for defining SMEs: formal enterprises with annual turnover of between 10 and 1,000 times the mean per capita gross national income (GNI at purchasing power parity) of the country in which it operates.[308] Inspired by this formula, a comparison can be made among the four jurisdictions regarding the scope

[306] European Commission, 'User Guide to the SME Definition' (n 186) 32.
[307] OECD, *SMEs in Public Procurement* (n 18) 29.
[308] Gibson and van der Vaart (n 271) 18. They define that '[A]n SME is a formal enterprise with annual turnover, in U.S. dollar terms, of between 10 and 1000 times the mean per capita gross national income, at purchasing power parity, of the country in which it operates'.

of SMEs, by calculating the ratio between annual revenue ceiling and GNI per capita.[309] Table 2.1 reveals significant variation in SME classification thresholds. When measured as multiples of GNI per capita, the EU (using Germany as proxy) defines the most expansive category at approximately 941 times GNI per capita, followed by the US (546 times), South Africa (445 times), and Brazil (89 times).[310]

Jurisdiction	**Annual revenue ceiling of SMEs (local currency)**	**Adjusted ceiling (int$)[311]**	**GNI per capita (PPP, int$)**	**Ratio (ceiling/GNI p.c.)**
EU(Germany)	EUR 50,000,000	70,422,535	74,880	940.47
US	USD 47,000,000	47,000,000	85,980	546.64
Brazil	BRL 4,900,000	1,935,484	21,650	89.40
South Africa	ZAR 50,000,000 (QSE)	6,746,286	15,150	445.30

Table 2.1 A comparison of SME size standard across jurisdictions

However, caution is required when interpreting the US's position in this ranking. While the SBA adopts an annual receipts ceiling for many sectors, with USD 47 million being the maximum, it applies only an employee headcount ceiling in other sectors, particularly in manufacturing sectors, such as tobacco manufacturing, small electrical appliance manufacturing. Their employee headcount ceilings could be as high as 1,500 employees, much higher than the EU SME standard. Conversely, the SBA sets

[309] The data on GNI per capita (PPP) was extracted from the world bank database, see World Bank Group, 'GNI per capita, PPP (current international $)' <https://data.worldbank.org/indicator/NY.GNP.PCAP.PP.CD> accessed 14 August 2025. In 2024, the recent value of GNI per capita (PPP) was USD 21,650 in Brazil, USD 62,279 in the EU, USD 85,980 in the US, and USD 15,150 in South Africa.

[310] See Table 2.1.

[311] Since all the turnover thresholds are expressed in their own currency, it is necessary to convert them into international dollar, based on PPP conversion factor published by the World Bank Group. See World Bank Group, 'PPP conversion factor, GDP (LCU per international $) '<https://data.worldbank.org/indicator/PA.NUS.PPP> accessed 14 August 2025.

much lower annual receipts ceilings in some sectors, for instance, the maximum is USD 2.25 million in certain agricultural sector.[312] This internal variation within the US size standards makes direct cross-jurisdictional comparisons more complex.

Regarding the linkage between SME definitions and public procurement rules, some differences exist among these jurisdictions. The EU SME definition is more closely linked to general supportive programmes than public procurement.[313] In the EU, SME-friendly measures in public procurement remain largely facilitative, such as dividing large contracts into lots, rather than preferential.[314] In contrast, the US definition of small businesses directly determines eligibility for federal procurement set asides and other preferential programmes. The US, Brazil, and South Africa all incorporate preferential measures for SMEs within their public procurement frameworks, though with varying approaches.[315] Nonetheless, it is evident that the US maintains the most expansive pool of potential beneficiaries of such measures, both in absolute financial terms and when adjusted for national income levels.

In summary, although SME definitions are often regarded as a technical matter of statistical classification, they in fact shape economic opportunities. This chapter has provided the necessary background by clarifying what is meant by 'SMEs' in each of the four jurisdictions examined, facilitating subsequent analysis of specific SME-friendly measures in following chapters. The four jurisdictions examined provide a rich

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[312] 13 CFR § 121.201, Subsector 111.

[313] For example, only enterprises satisfying the SME definition in Recommendation 2003/361 are eligible for applying the SME Fund 2025 provided by the European Union Intellectual Property Office (EUIPO), see EUIPO, 'SME Fund 2025' <https://www.euipo.europa.eu/en/sme-corner/sme-fund/2025> accessed 14 August 2025.

[314] See George O'Brien, 'Public procurement and the small or medium enterprise (SME)' (1993) 2 Public Procurement Law Review, 82; also see Burgi (n 48).

[315] See Chapter 6.

comparison and illustrate that there is no single ‘correct’ way to define SMEs. Rather, a definition is a policy choice intertwined with a country’s economic structure and goals. A clear understanding of these definitional frameworks allows for a more nuanced assessment of SME-friendly measures, especially where the definition of SMEs shapes the scope and operation of those measures. Before turning to an evaluation of whether these measures achieve their intended objectives, it is necessary to examine the barriers and challenges that SMEs typically face in engaging with public procurement processes, which is discussed in the next chapter.

Chapter 3 Barriers and Challenges to SME Participation in Public Procurement

3.1 Introduction

As introduced in Chapter 1, this thesis examines SME-friendly measures in public procurement law and assesses how such measures effectively support SME participation. Building on the definitional groundwork in Chapter 2, this chapter addresses the first research question by identifying and conceptualising the barriers that limit SME participation in public procurement. Clarifying what constitutes a barrier is essential to determining which challenges justify regulatory intervention and which instead reflect competitive disadvantages or perceptions. This distinction has important implications. Firstly, identifying genuine structural barriers provides legislators and policymakers with a clearer understanding of the obstacles hindering SMEs engagement in public procurement. Second, for governments considering the adoption of SME-friendly measures, recognising these barriers is a necessary step in designing targeted interventions. Finally, in jurisdictions where such measures already exist, their effectiveness can be evaluated by examining the extent to which they alleviate the barriers identified in this chapter.

3.2 The Definition of a 'Barrier'

In the current discourse on SME involvement in public procurement, barriers faced by such enterprises have attracted the most attention from academics and practitioners, and the term 'barrier' is frequently used without a clear or consistent definition.[316]

Scholars commonly concur on categorising these barriers into two distinct types: those necessitating intervention from the public sector (external factors) and those requiring proactive measures from SMEs (internal factors). [317] Loader provided a comprehensive literature review on this topic, collected 23 barriers from the literature, and divided them into two categories: 'public sector (public sector environment and procurement process)' and 'small business sector'.[318] In the first category, associated barriers include pro-large-business attitudes, contract size, difficulty getting onto the approved supplier list, etc.[319] The second category includes a lack of appropriate resources, poor completion of bids, a lack of required standards, etc.[320] This approach includes problems originating from both external factors (public procurement rules and practices) and intrinsic issues within SMEs themselves.[321] Similarly, an investigative report conducted by the United Nations Development Programme (UNDP) categorised barriers into two groups: demand-side barriers and supply-side

[316] See Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (n 49).
[317] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74); also see UNDP, New Playbook on Inclusive Public Procurement' (*Business Call to Action*, 21 September 2022) <https://www.businesscalltoaction.org/news/now-online-new-playbook-on-inclusive-public-procurement> accessed 31 October 2023.
[318] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).
[319] ibid.
[320] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).
[321] ibid.

barriers.[322] Demand-side barriers encompass risk aversion in public procurement, incoherent policies, restrictive procurement design and administrative burden.[323] On the supply side, identified barriers involve limited competitiveness and an unfriendly business environment.[324]

Both studies above consider the inherent attributes of SMEs as potential barriers. In contrast, Flynn has proposed the term ‘systemic barriers’ to refer to barriers inherent in the public procurement system that impose a disproportionate burden on SMEs in their participation.[325] Similarly, Thomas has recognised the difference between the natural disadvantages of SMEs and the barriers confronting them. [326] Natural disadvantages refer to conditions that may place firms at a disadvantage, such as firm size, experience, or geographic location, and they do not warrant regulatory intervention. [327] Barriers are defined as structural impediments arising from procurement rules or practices that may make it disproportionately more difficult for SMEs to bid for or win public contracts, compared with large businesses.[328] These structural barriers contribute to the perceived underperformance of SMEs in public procurement, which may justify government intervention.[329] In this chapter, natural disadvantages are considered as factors behind barriers, rather than barriers themselves, which will be discussed in Section 3.4.1.

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[322] UNDP (n 317).
[323] ibid.
[324] UNDP (n 317).
[325] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence’ (n 74). 5.
[326] Thomas (n 73).
[327] ibid.
[328] Thomas (n 73) 81.
[329] Nicholas and Fruhmann (n 126) 331.

While recognising a wide range of barriers is beneficial in providing a comprehensive overview, it may not necessarily facilitate the effective resolution of these issues. As Storey pointed out, SME policies with numerous objectives warrant caution, as achieving a singular objective may be deemed sufficient for policy success.[330] Therefore, researchers and policymakers need to be cautious, defining the primary objective and pinpointing the most deterrent factors (barriers) for SMEs in public procurement. Moreover, it is crucial to recognise that relying solely on direct survey results from SMEs to identify problems may be insufficient, as certain perceived issues may reflect subjective perceptions rather than concrete hindrances to their participation in public procurement. Therefore, a nuanced approach is necessary to distinguish between perceived challenges and actual barriers that may impede SME engagement in public procurement.

In this thesis, a 'barrier' is construed as an entry obstacle for SMEs, including three key dimensions. Firstly, it represents an external factor beyond the control of SMEs, emerging from either public procurement rules or the practices of contracting authorities. Secondly, it hinders small and medium-sized enterprises from participating in public procurement tenders, thereby restricting their access to the public procurement market. Thirdly, this barrier does not restrict large businesses from accessing the procurement market as much as it does for SMEs. Compared to the definition proposed by Flynn[331] or Thomas,[332] this definition of a barrier limits the focus

[330] Storey (n 89).
[331] Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (n 49) 5.
[332] Thomas (n 73) 81.

on gaining access to the procurement market and does not delve into whether this factor influences the probability of SMEs securing contracts.

Essentially, barriers are factors that increase costs for SMEs up to an prohibitive level, leading them to opt out of the public procurement market. When analysing whether an issue constitutes a barrier, it is necessary to exercise caution regarding the heterogeneity among the subcategories of SMEs. SMEs encompass a broad scope of economic operators with different capacities; the cost of a procurement procedure could be prohibitive for a microenterprise but may be acceptable for medium-sized enterprises.

Section 3.3 will use this definition to assess whether the frequently cited 'barriers' satisfy the proposed definition. Having identified the barriers that align with the definition proposed in this section, Section 3.4 undertakes a theoretical analysis to discuss the contributing factors, including the inherent limitations of SMEs and the risk-averse attitude of contracting authorities. The rationale behind employing a theoretical analysis lies in recognising that barriers often exist against the backdrop of a jurisdiction or a specific region. Nevertheless, there are instances where common barriers transcend jurisdictions and regions.[333] Thus, the theoretical analysis establishes a framework for comprehending the prevalence of these barriers and understanding the factors that either contribute to or mitigate them.

[333] OECD, *SMEs in Public Procurement* (n 18) 37.

3.3 Identifying Barriers Faced by SMEs in Public Procurement

The European Commission commissioned six comprehensive studies on SME participation in public procurement in 2004, 2007, 2010, 2014, 2019, and 2021, and most of them examined survey results obtained from SMEs, highlighting the barriers that they encounter in public procurement.[334] In these reports, the terms 'problems', 'barriers', 'challenges', and 'difficulties' are used interchangeably and encompass both external and internal factors, such as insufficient information, lack of clarity, large contract value, high financial requirements, SMEs' lack of knowledge and expertise, etc.[335]

In the US, small businesses face comparable barriers and challenges in public procurement. A 2020 Censeo Consulting Group survey of 455 small businesses identified five systematic barriers: (1) incumbent supplier advantage, (2) complex and inefficient processes, (3) poor communication with buyers, (4) onerous legal and regulatory requirements, and (5) political uncertainty.[336] More recently, at a hearing before the House Committee on Small Business, small business owners testified to

[334] EIM Business & Policy Research, commissioned by European Commission, 'SMEs' access to public procurement contracts, Executive summary' (2004) <https://ec.europa.eu/docsroom/documents/2155/attachments/1/translations/en/renditions/native> accessed 23 Oct 2023; GHK and Technopolis, 'Evaluation of SMEs' access to public procurement markets in the EU' (Specific contract No ENTR/E4/04/93/1/07/11, 2007); GHK, 'Evaluation of SMEs' access to public procurement markets in the EU' (DG Enterprise and Industry, Final Report, September 2010) <https://ec.europa.eu/docsroom/documents/14808/attachments/1/translations/en/renditions/pdf> accessed 31 December 2022; PwC, ICF GHK and ECORYS (n 66); de Bas P and others (n 68); t33 Srl, *SME Needs Analysis in Public Procurement: Final Report* (Study commissioned by the European Commission, DG Internal Market, Industry, Entrepreneurship and SMEs, February 2021) ('EU SME Needs Analysis').

[335] PwC, ICF GHK and ECORYS (n 66).

[336] Censeo Consulting Group. 'Cracking the Government Procurement Code' (Censeo Consulting Group, 2021) <https://www.censeoconsulting.com/insights-news/> accessed 23 September 2023.

several entrenched barriers in federal procurement.[337] In particular, they pointed to the overwhelmingly complex regulatory framework under the Federal Acquisition Regulation (FAR), delayed payments, and the excessive costs and lengthy procedures required to qualify for multiple-award contracts as barriers that hinder small businesses from contracting with the federal government.[338]

To facilitate the analysis in the following chapters, this section examines the frequently reported barriers and challenges faced by SMEs, drawing on insights from four key reports sourced from the EU, the US, and the OECD, as presented in Table 3.1.[339] These reports, based on surveys and consultations with SMEs and contracting authorities, identify common concerns that inform the conceptual framework for analysing barriers in this thesis. The discussion presented here is intended to be representative of frequently cited barriers rather than exhaustive.

	OECD SMEs in Public Procurement (2017)	**EU SME Needs Analysis (2021)**	**US Bipartisan Policy Center (2021)**	**Censeo Consulting Group (2020)**
1	Access to relevant information / Quality and understanding of the information provided / Lack of visibility of available contracts of smaller value / Lack of dialogue and feedback	ESPD and TED are too technical	Insufficient information on federal contract opportunities	Poor communication with buyers

[337] United States House of Representatives, 'Levelling the Playing Field: Challenges Facing Small Business Contracting' (Hearing before the Subcommittee on Contracting and Infrastructure of the Committee on Small Business, 118th Congress, 2nd Session, 15 February 2024) <https://www.congress.gov/118/chrg/CHRG-118hhrg54744/CHRG-118hhrg54744.pdf> accessed 31 July 2025.

[338] ibid.

[339] The survey result is from 2017 OECD survey on strategic use of public procurement to support SMEs. For more information, see OECD, *SMEs in Public Procurement* (n 18) 37; t33 Srl (n 334); Bipartisan Policy Center 'Supporting Small Business and Strengthening the Economy Through Procurement Reform' (July 2021) <https://bipartisanpolicy.org/report/supporting-small-business-and-strengthening-the-economy-through-procurement-reform/> accessed 26 April 2023; Censeo Consulting Group (n 336).

	with public contracting authorities			
2	Difficulties relating to the size of the contracts	Business opportunities are too large / Opportunities on TED are too big	Category management	-
3	Difficulties relating to proportionality of qualification levels and financial requirements	Unreachable selection criteria	-	Onerous legal and regulatory requirements
4	-	Complex procedures	Process too complicated	Complex and inefficient processes
5	Late payments or lengthy terms of payment	Delays in payment	-	-
6	Emphasis on price only rather than value for money	Price to be the main criterion	-	-
7	Too short a time to draw up tenders	Time is not enough for a small firm to prepare bids	-	-
8	-	Time-consuming	Too time-consuming	-
9	Administrative burden too high	High administrative burden	-	-
10	-	-	-	Incumbent supplier advantage
11	-	-	Success unlikely because small bushiness not adequately prioritized	Political uncertainty

Table 3.1 Barriers and challenges reported by SMEs in public procurement

3.3.1 Information barrier

As shown in Table 3.1, information-related issues are the most frequently cited challenges by SMEs, a finding also supported by the studies of Fee et al and

Saastamoinen et al.[340] These issues encompass the availability of tender information, especially lower-value contracts, the prior information about upcoming tenders, and the clarity and quality of procurement documents provided by contracting authorities.

3.3.1.1 Contract notices

Within any public procurement system, contracting authorities are generally obligated to publish calls for tenders when the contract value surpasses a specified threshold.[341] In the EU, contracts exceeding the EU threshold necessitate publication in the EU-wide online version of the Supplement to the Official Journal of the European Union (OJEU), the Tenders Electronic Daily (TED) platform.[342] In theory, the implementation of the TED database is intended to alleviate the challenges of locating tender information for prospective bidders, serving as an online portal with business opportunities. However, the 2021 EU SME Needs Analysis reveals notably low awareness of the TED platform, with only 28.3 per cent of respondents familiar with it.[343] Awareness varies by the size of enterprises: 24 per cent of micro-enterprises, 31 per cent of small enterprises, and 39.3 per cent of medium-sized enterprises.[344] Even among respondents with successful tendering experience, reliance on the websites of

[340] Ruth Fee, Andrew Erridge and Sean Hennigan, 'SMEs and Government Purchasing in Northern Ireland: Problems and Opportunities' (2002) 14 European Business Review 326, 330; also see Jani Saastamoinen, Helen Reijonen and Timo Tammi, 'The Role of Training in Dismantling Barriers to SME Participation in Public Procurement' (2017) 17 Journal of Public Procurement 1, 6.

[341] In the US, the equivalent term used is 'request for proposals' and 'solicitation'. See 48 CFR § 15.203.

[342] Contracts with higher monetary value or cross-border interests shall be published on the Official Journal of the European Union. Commission Implementing Regulation (EU) 2019/1780 of 23 September 2019 establishing standard forms for the publication of notices in the field of public procurement and repealing Implementing Regulation (EU) 2015/1986 [2019] OJ L272/7.

[343] t33 Srl (n 334).

[344] ibid.

contracting authorities or conventional search engines, such as Google, surpasses the use of TED.[345] Respondents cited challenges with TED, attributing difficulties to an intricate interface with an excess of filters and technical terms that are challenging to understand.[346]

For contracts valued below the EU thresholds, contracting authorities in the Member States can publish tender information voluntarily on TED.[347] Other than TED, tender information shall be published on national procurement portals or local authorities' websites if the tender is over a certain value.[348] The thresholds for publishing tender information vary among Member States, with some setting relatively low thresholds while others establish higher thresholds for authorities to publish tenders on electronic platforms.[349] Taking Germany as an example, the Regulation for Procurement Below the EU Threshold (UVgO) stipulates a threshold of EUR 25,000 for publishing contract notices.[350] According to Paragraph 4 of Section 38 UVgO, if the contract value falls

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[345] ibid.

[346] t33 Srl (n 334). Another problem frequently mentioned by respondents is the language of tenders and they suggest tenders shall be published in an international language, such as English, on TED. As it is a unique problem in the EU for cross-border procurement, this research mainly focuses on SMEs in national procurement, thus, it is not being discussed here.

[347] For contracts below the EU threshold with a cross-border interest, there are controversial opinions on if the contracting authority shall publish the tender in the same way as the contracts above the threshold. For a comprehensive understanding of this question, see Carina Risvig Hansen, Contracts not Covered or not Fully Covered by the Public Sector Directive (DJØF Publishing 2012). The European Court of Justice ruled in *Telaustria* that a certain degree of publicity is required to guarantee the principle of non-discrimination. See Case C-324/98 *Telaustria Verlags GmbH and Telefonadress GmbH v Telekom Austria AG* [2000] ECR I-10745.

[348] European Commission, 'Public Procurement: A data space to improve public spending, boost data-driven policy-making and improve access to tenders for SMEs' [2023] OJ C98I/1.

[349] ibid.

[350] *Unterschwellenvergabeordnung (UVgO),Bekanntmachung of the Federal Ministry for Economic Affairs and Energy, BAnz AT 07.02.2017 B1* (applied to federal authorities from 2 September 2017; application in Länder subject to adoption). An English version provided by the Ministry was consulted: Federal Ministry of Economic Affairs and Energy, 'Regulation on sub-threshold procurement – UVgO' (non-official publication, 7 February 2017) <https://www.xfel.eu/sites/sites_custom/site_xfel/content/e35152/e46557/e47200/e47206/xfel_file472

below EUR 25,000, the contracting authority is not obligated to publish the contract notice on the Federal website.[351] In the OECD survey on strategic use of public procurement to support SMEs, nearly 20 per cent of the respondents highlighted a lack of visibility of available contracts of lower value.[352] SMEs, given their capacity scale, typically exhibit more interest in lower-value contracts, whereas these contracts are subject to less stringent publication requirements than higher-value contracts.

In the US, federal agencies are mandated to publish solicitations (call for tender) on the Federal government's System for Award Management (SAM) when the contract value exceeds USD 25,000; they may also post them on their websites.[353] Contracts falling between USD 15,000 and USD 25,000 necessitate the display of solicitation in a public place or any suitable electronic medium, though SAM publication is not obligatory.[354] For contracts of micro value (under USD 10,000), agencies typically employ alternative procurement methods, such as government purchase cards, task orders under existing contracts, or ordering from a General Services Administration (GSA) schedule.[355] According to the Federal Acquisition Regulation (FAR), contracts valued between USD 10,000 and USD 250,000 are required to be reserved for small

09/UVgOEnglisch_eng.pdf> accessed 18 July 2024. Paragraph 1 of Section 28 regulates that contract notices should be published on the contracting authority's website or on the federal internet portal.

[351] ibid. Paragraph 4 of Section 38 *UVgO* states that if the contract value is lower than EUR 25,000, the contracting authority is not obliged to publish the contract notice.

[352] OECD, SMEs in Public Procurement (n 18).

[353] The dissemination of contracts information is stipulated in Part 5 of Federal Acquisition Regulation, codified in 48 CFR § 5.102.

[354] 48 CFR § 5.101.

[355] The schedule is referred to the Federal Supply Schedule (multiple award schedule) maintained by the General Services Administration. The schedule is a list of goods and/or services provided by businesses who are related to GSA. GSA award indefinite contracts to firms through competitive process. For more information, see CRS, 'Overview of the Federal Procurement Process and Resources' (14 April 2014) <https://crsreports.congress.gov/product/pdf/RS/RS22536> accessed 26 April 2023.

businesses unless the contracting officer reasonably expects that there will not be two or more small businesses bidding for this contract.[356]

The Small Business Administration (SBA) website provides a specific section for 'finding contracts', listing all potential platforms for bidders to discover contract opportunities.[357] However, these platforms adhere to regulatory requirements, leading to a lack of information on contracts valued at less than USD 15,000. The SBA's 'Dynamic Small Business Search' offers a singular database for federal agencies to identify potential small business bidders, and small businesses can explore opportunities for collaboration with others.[358] Apart from this dedicated platform, alternative sources encompass the SAM website, GSA website, and micro-purchasing website.[359] Additionally, most federal agencies maintain an Office of Small and Disadvantaged Business Utilisation or an Office of Small Business Programs, assisting small businesses in identifying potential contract opportunities.[360] The various platforms and dispersed information might pose challenges to new entrants, irrespective of the company's size.

The GHK study *Evaluation of SME Access to Public Procurement Markets in the EU* in 2007 highlights that large businesses do not have better access to information since enterprises from all size classes were nearly equally satisfied with their access to

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[356] 48 CFR § 19.502-2. See Chapter 7.

[357] US SBA, 'How to Win Contracts' <https://www.sba.gov/federal-contracting/contracting-guide/how-win-contracts> accessed 11 October 2023.

[358] The Dynamic Small Business Search (DSBS) is maintained by the SBA. See SBA DSBS <https://dsbs.sba.gov/search/dsp_dsbs.cfm> accessed 11 October 2023. On this database, the SBA has verified certain certifications for small businesses, such as women-owned small businesses, veteran-owned small businesses. This will be discussed further in Chapter 7.

[359] US Digital Service, 'Finding Opportunities and Providing Services to the Federal Government' (TechFAR Hub) <https://techfarhub.usds.gov/resources/learning-center/field-guides/finding-opportunities/> accessed 11 October 2023.

[360] ibid.

information, with approximately 50 per cent of respondents expressing satisfaction.[361] However, this result shifted slightly in 2010, as shown in Table 3.2, where approximately 66 per cent of large enterprise respondents reported satisfaction with their information access, contrasting with a lower 45 per cent satisfaction rate among micro-enterprises. [362] An additional question about sources of information, as presented in Table 3, could shed light on this shift, suggesting that large companies possess more diverse information sources than smaller companies.[363]

Company size class	Fully agree	Rather agree	Total
Large	38	28	66
Medium	33	30	63
Small	31	27	58
Micro	24	21	45

Table 3.2 Views on appropriateness of information about above-threshold tender opportunities, by company size class (in percentage)[364]

Information sources	Micro	Small	Medium	Large	Total
Official procurement portal	66	61	56	61	61
Commercial proc. portals	45	47	40	41	43
Contracting authority	29	43	43	44	41
OJEU/TED	27	31	43	44	39
Government publications	26	41	30	46	38

Table 3.3 The top 5 mostly used information sources by company size class (proportion of companies using the source ‘always’ or ’often’, in percentage).[365]

[361] GHK (2010) (n 334).

[362] ibid.

[363] GHK (2010) (n 334).

[364] ibid 359.

[365] GHK (2010) (n 334) 52, figure 4.11. In this report, the official procurement portals refer to national or regional web portals for public tenders. Commercial proc. portals refer to commercial public procurement portals. Government publications are usually paper-based procurement journals.

In this GHK report, responses regarding information sources are collected from both SMEs and large businesses regarding their information sources. Surprisingly, there is no significant distinction between large enterprises and SMEs regarding their views on information appropriateness, except for micro-sized enterprises. The only significant difference between small enterprises and large ones is the use of OJEU/TED. However, this difference could be because large businesses are more interested in large contracts than SMEs, and TED has more information on large contracts compared with contracts below the EU threshold. However, when large contracts are divided into lots, SMEs shall make more use of OJEU/TED as information for lots is required to be published on OJEU/TED.[366]

Additionally, this GHK report interpreted that large businesses have more access to direct contact with contracting authorities, which could be through subscribing to emails or participating in supplier events.[367] However, as shown in Table 3.3, direct contact with contracting authorities serves as an information source for SMEs, except for micro-sized enterprises, which use this channel less frequently.[368] Micro-sized enterprises, instead, use the official procurement portal as the primary source of information, compared with other platforms such as OJEU/TED.[369]

In summary, a variety of platforms for contract notices exist, and SMEs generally face relatively limited barriers in accessing these sources of information. One notable exception pertains to information on lower-value contract opportunities, as contracting authorities are usually not obligated to adhere to public procurement procedural rules;

[366] The division into lots regime will be discussed in Chapter 4.
[367] GHK (2010) (n 334) 48.
[368] ibid 49.
[369] GHK (2010) (n 334) 49.

the lack of information on lower-value contracts can pose a potential barrier for SMEs, particularly micro-sized enterprises, which are more interested in lower-value contracts. This observation also implies that the design of SME-friendly measures shall also take the disparities between the three subgroups of SMEs into account, which will be discussed further in the following chapters.

3.3.2.2 Prior information notices

Beyond contract notices, contracting authorities may publish Prior Information Notices (PINs) to disseminate information regarding upcoming tenders or specific tender opportunities.[370] The publication of PINs is not mandatory for contracting authorities under the current EU public procurement law.[371] According to the 2021 *EU SME Needs Analysis*, SMEs express the view that providing prior information through PINs can enhance their preparation for bidding.[372] This may involve the dissemination of a procurement calendar, pre-procurement information meetings for tenders or engaging in open dialogues with potential bidders.[373] Contrary to expectations, the 2019 *EU SME Participation in Public Procurement* report explored the correlation between the publication of PINs and the share of contracts awarded to SMEs. Interestingly, no significant increase in SMEs' share of awarded contracts was observed when PINs were published.[374] The marginal distinction between scenarios involving 'No PIN' and 'PIN' is more reasonably associated with contract value, given that the average

[370] de Bas P and others (n 68).
[371] See Directive 2014/24/EU, arts 27, 48.
[372] t33 Srl (n 334).
[373] ibid.
[374] de Bas P and others (n 68).

contract value with published PINs is higher than that without.[375] The connection between SMEs' participation and contract value will be further discussed in Section 3.2.2.

Presolicitation notices in the US are not identified as a major concern by small businesses in the reports reviewed in this chapter.[376] This absence may be attributed, in part, to the stricter regulations imposed on federal agencies. Specifically, for construction contracts, presolicitation notices become mandatory when the contract value surpasses the simplified acquisition threshold. Additionally, contracting officers may publish presolicitation notices when the contract value is anticipated to be lower than the simplified acquisition threshold, or in the case of supply and services contracts.[377]

Upon assessing the lack of prior information against the definition of 'barrier' proposed at the beginning of the chapter, there is no compelling evidence demonstrating its impact on SMEs bidding for contracts. Consequently, the absence of prior information on tenders does not qualify as a barrier for SMEs. Establishing rules to encourage or mandate the publication of PINs or presolicitation notices may be beneficial for all bidders, as such regulations serve to enhance communication between contracting authorities and bidders.

[375] ibid.
[376] See Table 3.1.
[377] See 48 CFR § 36.213-2, 5.204, 15.201.

3.3.2.3 Clarity and quality of information

In the *OECD Survey on Strategic Use of Public Procurement to Support SMEs*, a consensus among respondents highlighted the significance of the quality and comprehensibility of the information provided by buyers as key factors influencing SME participation in public procurement.[378] A similar observation is found in the UNDP's *Inclusive Public Procurement Playbook*, where 33 per cent of respondents attributed non-participation to difficulties in navigating tender opportunities and understanding procurement terminology.[379] While the lack of accessible information has been widely discussed, another, less visible yet equally significant challenge stems not from the absence of information, but from its complexity and lack of clarity. While such language may be necessary to convey precise requirements, it often creates a barrier for SMEs, especially those without specialised legal or procurement expertise.[380] Moreover, the issue is compounded by a tendency among contracting authorities to err on the side of over-disclosure, resulting in extensive documentation that, although transparent, can overwhelm or confuse less-resourced economic operators.[381]

This raises an important distinction between transparency and clarity. Public procurement rules rightly emphasise transparency, grounded in the principle of equal treatment, requiring that all published information be clear and unequivocal to all

[378] OECD, *SMEs in Public Procurement* (n 18) 37.
[379] UNDP (n 317).
[380] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).
[381] Omri Ben-shahar and Carl E Schneider, 'The Failure of Mandated Disclosure' (2011) 159 University of Pennsylvania Law Review 647.

potential tenderers.[382] However, in practice, it is easier to assess whether information has been disclosed than whether it has been disclosed in a way that is clear and unequivocal to all tenderers so that they understand and interpret the specifications in the same manner.[383] A case adjudicated by the Higher Regional Court of Düsseldorf clarified that transparency is not breached merely because procurement documents require detailed interpretation, provided that reasonably experienced and well-resourced tenderers can understand them.[384] However, this reasoning arguably overlooks the reality that SMEs often lack the legal and technical capacity to interpret such complex criteria, raising concerns about the inclusiveness of such standards.

While the use of complex or technical language in procurement documents is frequently cited as a barrier to SME participation, it is important to acknowledge that a certain degree of complexity is often necessary, particularly in relation to high-value or specialised contracts. As Thomas has observed, difficulties faced by SMEs may not always constitute an unfair disadvantage,[385] but rather a natural consequence of their more limited internal capacity and technical expertise. From this perspective, the issue lies less in the language of procurement documents themselves and more in the structural limitations inherent to SMEs.[386] However, this view must be approached with caution. Transparency under Article 18 Directive 2014/24/EU is not satisfied by

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[382] Kirsi-Maria Halonen, 'Many Faces of Transparency in Public Procurement' in Kirsi-Maria Halonen, Roberto Caranta and Albert Sanchez-Graells (eds), *Transparency in EU Procurements: Disclosure Within Public Procurement and During Contract Execution* (Edward Elgar Publishing 2019) 25.

[383] Carina Risvig Hamer and Marta Andhov, 'Article 18 Public Procurement Principles' in Roberto Caranta and Albert Sanchez-Graells (eds), European Public Procurement: Commentary on Directive 2014/24/EU (Edward Elgar Publishing 2021) 186, 187; also see Case-27/15 *Pizzo* ECLI:EU:C:2016:404, para 36.

[384] Risvig Hamer and Andhov (n 383), at 195 citing *OLG Düsseldorf, Beschluss,* 13 December 2017, VII-Verg 19/17.

[385] Thomas (n 73).

[386] See Section 3.4.1.

disclosure alone; it requires that information be presented in a manner that is clear, precise, and unequivocal to a reasonably informed economic operator.[387] The difficulty is to determine what constitutes a reasonable level of clarity across a diverse Internal Market. In practice, objective reference points may be needed to assess whether procurement documents are too complex for SMEs, such as evidence indicating that SMEs consistently struggle to interpret procurement documents that pose no difficulty for large businesses. If this is the case, this issue goes beyond a natural disadvantage and instead reflects an entry barrier. Equally, where such patterns are not evident, the solution may lie not in simplifying the documentation, but in improving SMEs' internal capabilities through training or other support.

In summary, SMEs encounter a range of information-related challenges, including insufficient tender information, especially for lower-value tenders, the lack of prior information, and concerns about the quality of information. Empirical evidence from the EU suggests that SMEs do not, in general, face disproportionate difficulties in accessing publicly available tender information compared to large businesses. However, a more specific concern arises in relation to lower-value contracts, where publication requirements are often less stringent. In such cases, the limited availability of information may pose a barrier, particularly for microenterprises that tend to focus on lower-value opportunities. However, given that SMEs dominate this segment of the market, it would be misleading to treat the lack of information concerning lower-value contracts in this context as a universal entry barrier for SMEs. Likewise, while the use of complex terminology may hinder some smaller firms, this is not an entirely external

[387] See Case C-19/00 *SIAC Construction Ltd v County Council of the County of Mayo* [2001] European Court Reports I-07725, para 42; also see Case C-42/13 *Cartiera dell'Adda SpA v CEM Ambiente SpA* (Judgment of 6 November 2014, Fifth Chamber) ECLI:EU:C:2014:2345 para 44.

constraint. SMEs must also take active steps to build internal capacity and improve their ability to engage with procurement procedures.

3.3.2 Large contract size

Large contract size has frequently been cited by SMEs across jurisdictions as a barrier to participation in public procurement.[388] In the *2017 OECD Survey on Strategic Use of Public Procurement to Support SMEs*, nearly 70 per cent of respondents concurred that challenges associated with the scale of contracts restrict their participation in public procurement.[389] Similarly, the EU *SME Needs Analysis* highlights that when the contract value exceeds specific thresholds, such as the annual revenue of a small business, it may exceed the enterprise's operational capacity, particularly when stringent qualification requirements cannot be met, which will be discussed in the subsequent section.[390]

A crucial question to consider is: What constitutes a 'large' contract for SMEs? Drawing insights from the 2014 EU *SMEs in Public Procurement* report, covering data from 2009 to 2011, micro-enterprises secured approximately 20 to 22 per cent of contracts valued below EUR 100,000, small enterprises secured slightly fewer contracts in this category, and medium-sized enterprises secured 15 per cent of contracts in this category.[391] However, the landscape shifts among successful bidders for contracts valued between EUR 100,000 and EUR 300,000, where the shares of micro-

[388] See Table 3.1.
[389] OECD, *SMEs in Public Procurement* (n 18) 37.
[390] See Chapter 5.
[391] PwC, ICF GHK and ECORYS (n 66) 50; de Bas P and others (n 68) 54.

enterprises decrease, and those of small and medium-sized enterprises increase.[392] Further, in contracts valued between EUR 300,000 and EUR 1 million, the share of micro-enterprise contractors decreased significantly, and the share of small contractors slightly decreased, with an increase in the share of medium-sized contractors.[393] From this data, it is evident that micro-sized enterprises performed the best when the estimated contract value was below EUR 300,000; small-sized enterprises performed the best in contracts valued between EUR 30,000 and EUR 1 million; and medium-sized enterprises performed the best in contracts valued between EUR 100,000 and EUR 5 million. When the value of contracts exceeds EUR 5 million, the proportion of all categories of SMEs among successful bidders decreases drastically.[394] The changes in the proportion of SMEs illustrate that three categories of SMEs might have different perceptions of 'large' when they report the barrier 'large contract size'. For micro-sized enterprises, contracts above EUR 300,000 could be perceived as large, for small-sized enterprises above EUR 1 million, and for medium-sized enterprises above EUR 5 million.

According to the 2019 report commissioned by the European Commission, data covering the period from 2011 to 2017 reveals a similar trend: micro-sized enterprises secured around 22.5 per cent of contracts when the estimated value of contracts was below EUR 300,000, and they secured fewer contracts when the estimated value exceeded EUR 300,000.[395] For small-sized enterprises, this threshold is EUR 1 million, and for medium-sized enterprises, it is EUR 5 million.[396]

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[392] ibid.
[393] PwC, ICF GHK and ECORYS (n 66) 50.
[394] ibid.
[395] de Bas P and others (n 68) 54.
[396] ibid.

From 2015 to 2017, the average value of a tender won by an SME was EUR 779,386, compared to EUR 1,523,245 for a tender won by a non-SME.[397] Consequently, it is reasonable to assume that contracts exceeding EUR 1 million are considered large for most SMEs except medium-sized enterprises. This assumption aligns with the observation that SMEs tend to undertake more contracts below the EU thresholds.[398] The EU threshold is approximately EUR 5.5 million for works contracts, and the thresholds for supplies and services contracts range from EUR 143,000 to EUR 750,000.[399] Thus, dividing works contracts above the EU threshold would benefit all categories of SMEs, whereas dividing supplies and services contracts that are above the EU threshold but lower than EUR 1 million will mainly benefit micro-sized enterprises.[400]

From the empirical evidence in the EU, the proportion of contracts awarded to large businesses increased as the estimated value of contracts increased, especially when the contracts are above EUR 5 million, which shows that large businesses do not perceive the large size of contracts as a barrier.[401] Moreover, the *GHK 2010 study*, incorporating interviews with both large businesses and SMEs, provides insights into the distinct perceptions of problems between these two categories, as detailed in Table 3.2.[402]

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[397] Jorg Becker, 'Contribution to Growth. European Public Procurement. Delivering Economic Benefits for Citizens and Businesses', 2019, <https://www.europarl.europa.eu/RegData/etudes/STUD/2018/631048/IPOL_STU(2018)631048_EN.pdf> accessed 20th October 2023, 7.

[398] Above EU-threshold, 38 per cent, below the EU-threshold 73 per cent, calculated by the overall contract value. See de Bas P and others (n 68) 54.

[399] See Directive 2014/24/EU, art 4

[400] See Chapter 4.

[401] de Bas P and others (n 68) 54; PwC, ICF GHK and ECORYS (n 66) 50.

[402] GHK (2010) (n 334) 48.

Potential problems	Micro	Small	Medium	Large	Total
Over-emphasis on price	58	55	51	55	**54**
Long payment terms	52	42	38	36	**40**
Late payments	47	36	39	35	**38**
No debriefing	43	36	33	36	**36**
Administrative burden	45	34	35	30	**34**
Lack of clarity	38	28	29	28	**30**
Limited options for interaction	30	23	19	22	**23**
Disproportionate financial criteria	34	21	18	17	**20**
Insufficient time to bid	27	23	14	20	**20**
Lack of information on opportunities	23	22	18	17	**19**
Tenders not evaluated fairly	16	14	26	30	**19**
Disproportionate technical criteria	18	18	14	13	**15**
Large contract value	22	15	5	1	**7**
Joint fulfilment of criteria not allowed	8	5	6	4	**5**

Table 3.4 Problems faced by bidders by company size (in percentage). Source: Figure 4.11 Problems faces by bidders, by company size class (proportion of companies using the source 'always' or 'often', in percentage), GHK, Evaluation of SMEs' access to public procurement markets in the EU, final report 2010.

From these results, the 'large contract value' appears not to be on top of the problems reported by bidders, with only 7 per cent of the respondents on average.[403] A reason proposed by Saussier is that SMEs did not even consider tendering large contracts because they filtered out these contracts automatically when looking for tender opportunities.[404] However, this study conducted interviews with 'SMEs and large companies who have participated (at least once) in public procurement above the EU

[403] See Table 3.4.

[404] Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) at 320, citing Stéphane Saussier, '*L'accès des PME aux marchés publics: une analyse économique'* (Bibliothèque PSSFP 2019) <http://bibliotheque.pssfp.net/index.php/institutions/institutions-nationales/senat/articles/economie/1735-lacces-des-pme-aux-marches-publics-une-analyse-economique/file>, accessed 28 March 2023, 6.

thresholds'.[405] Consequently, the telephone interview and survey results from this study inherently reveal issues arising after the contract award, specifically during the contract performance stage. Furthermore, it is noteworthy that the respondents encompass not only SMEs but also large companies, as detailed in Table 3.2, revealing divergent opinions on the impact of large contract values.[406]

In the US, the issue of contract size does not appear to be as prominent as it is in the EU. According to *Goldman Sachs 10,000 Small Business Voices*, the challenges reported by small businesses are not primarily related to the size of contracts.[407] Instead, difficulties are noted throughout the procurement process, from obtaining certification for preferences to navigating complex bidding procedures.[408] One plausible explanation for the lack of concern about contract size is the relative scale of US small businesses, which are often considerably larger than EU SMEs.[409] As discussed in Chapter 2, small businesses in the US can have up to 1,500 employees, particularly in the manufacturing sector, whereas the EU definition of an SME imposes a ceiling of 250 employees.[410] Compared with the US, the EU has a significantly higher proportion of microenterprises, which may explain differing experiences and capacities when engaging in public procurement.[411]

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[405] GHK (2010) (n 334) 48.

[406] See Table 3.4.

[407] Michelle Kumar and Jason Wiens, *The Small Business Policy Playbook: Winning Strategies to Drive Economic Growth* (Goldman Sachs 10,000 Small Businesses Voices, Bipartisan Policy Center, January 2025) <https://www.goldmansachs.com/images/community-impact/voices/policy-agenda/policy-playbook/report.pdf> accessed 01 August 2025, 26.

[408] ibid 26.

[409] See Chapter 2.

[410] ibid.

[411] European Commission, *An EU-US Statistical Overview: Business Demography and Scaling up Comparisons* (Joint Research Centre Technical Reports, 2018) <https://ec.europa.eu/research/participants/documents/downloadPublic?documentIds=080166e5c0dca59d&appId=PPGMS> accessed 20 October 2023.

Nevertheless, another concern raised by US small businesses and their advocates pertains to category management, an initiative introduced in 2014 and formalised through OMB Memorandum M-19-13 in 2019.[412] It aimed to streamline procurement by consolidating commonly purchased goods and services into ten standardised categories and encouraging the use of government-wide contract vehicles by federal agencies.[413] This leads to a reduction in the number of contracts awarded by agencies, which results in more high-value contracts that might be out of the capacity of small businesses.[414] The US Government Accountability Office's assessment of category management highlighted that over half of the contracts eliminated by this approach were previously awarded to small businesses.[415] Under category management, federal agencies are encouraged to purchase common goods and services through a limited number of GWACs, MACs, or BIC vehicles. Each of these has a pre-competed, closed list of contractors, businesses have to be on those lists to bid for contracts in those vehicles. However, these supplier lists are not always open for new suppliers. Thus, even though some of those lists include a large proportion of small businesses, they create an additional entry barrier for small businesses that are interested in participating in federal procurement, compared with bidding for unconsolidated procurement contracts.

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[412] Office of Management and Budget (OMB), Memorandum M-19-13: *Category Management – Making Smarter Use of Common Contract Solutions and Practices* (20 March 2019) <https://www.whitehouse.gov/wp-content/uploads/2019/03/M-19-13.pdf> accessed 01 August 2024.

[413] ibid; CRS, 'Small Business Contracting Under Category Management' (4 April 2023) <https://sgp.fas.org/crs/misc/IF12374.pdf> accessed 13 October 2023.

[414] US Government Accountability Office (GAO) Report to Congressional Requesters, *Federal Buying Power – OMB Can Further Advance Category Management Initiative by Focusing on Requirements, Data, and Training*, GAO-21-40, 2020.

[415] ibid 46.

Governments, in their pursuit of economies of scale, often implement procurement policies such as 'contract bundling', 'contract consolidation', and 'contract aggregation'.[416] Contract bundling, identified as a barrier to small businesses by the US Congress in 1940, discouraged and hindered them from participating in bidding by consolidating multiple procurement requirements into a single contract.[417] Although bundling without justification is generally prohibited, its occurrence prompted concern from the SBA due to its perceived adverse impact on small businesses.[418] Consequently, it becomes a deliberate balancing act, posing a conflict between protecting the interests of small businesses and striving for efficiency in procurement through the implementation of multiple award schedule contracts and category management, which will be discussed in Chapter 7.[419]

Similarly, in the EU, the *GHK and PwC Study* found a weak negative correlation between centralised purchasing and SMEs' estimated share in above-threshold procurement, alongside a positive correlation between centralised purchasing and the value of the contract.[420] The link between large-value contracts and reduced SME participation is well-established, but the correlation between centralised purchasing and SME participation is not significant. This suggests that the challenge lies not in

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[416] James W Hamister and Sima M Fortsch, 'Cumulative Impact of Category Management on Small Retailers' (2016) 44 International Journal of Retail & Distribution Management 680.

[417] Bundling of contract requirements means 'consolidating two or more procurement requirements' for goods or services which were provided under separate contracts into one single contract. See 15 U.S.C. § 632(o); also see Max V Kidalov and Keith F Snider, 'US and European Public Procurement Policies for Small and Medium-Sized Enterprises (SME): A Comparative Perspective' (2011) 13 Business and Politics 1, at 14 citing Leverett Saltonstall, 'Small Business and National Security' (Lecture at the Industrial College of the Armed Forces, Publication No. L57-102, 1957).

[418] Kidalov and Snider, 'US and European Public Procurement Policies for Small and Medium-Sized Enterprises (SME): A Comparative Perspective' (n 417) 16.

[419] See Chapter 7; also see Bipartisan Policy Center (n 339).

[420] Defined in Directive 2014/24/EU, art 2, a central purchasing body refers to 'a contracting authority providing centralised purchasing activities and, possibly, ancillary purchasing activities'.

centralised purchasing per se, but in the way it is implemented. For example, if large contracts are divided into smaller lots, SMEs can still access and compete for those opportunities even within centralised purchasing frameworks.[421] Conversely, where aggregation results in contracts of a scale beyond the capacity of SMEs, their participation will inevitably be limited.

In summary, large contract sizes disproportionately impede SMEs from accessing public procurement contracts, compared to large businesses. Albano and Zampino's study shows that contract value is positively correlated with company size, as indicated by data from the Italian procurement database.[422] It suggests that the higher the value of the contract, the more likely the supplier is to be a large company.[423] SMEs are more likely to submit bids when the estimated contract value is relatively lower, and there is a significant negative correlation between the contract value and SMEs' success rate.[424] Additionally, based on the reports discussed in this chapter, this issue is more significant in the EU than in the US. Chapter 4 will examine the division into lots regime in the EU, which is perceived as an important measure to reduce the size of contracts and facilitate SME access to public procurement.[425]

[421] For the contract division into lots regime, see Chapter 4.
[422] Gian Luigi Albano and Roberto Zampino, 'Some Evidence of "Smart" Public Procurement: Solutions for SMEs in Italy' (2013) 3 *Piccola Impresa* / Small Business.
[423] ibid.
[424] Hoekman and Taş (119) 383. Glas and Eßig (n 66) 65.
[425] See Chapter 4.

3.3.3 Excessive qualification criteria

Empirical evidence consistently demonstrates that excessive qualification requirements constitute one of the primary barriers hindering SME participation in public procurement.[426] Qualitative requirements are established by contracting authorities to ensure that the potential contractor is 'reliable, appropriately trained, capable, experienced and trustworthy'.[427] Frequently used qualification criteria include financial and technical capacity thresholds, as well as a certain level of past performance.[428] From the competition perspective, the qualification process restricts the pool of potential competitors in most instances,[429] and smaller businesses are more likely to be excluded due to their limited resources. When contracting authorities impose excessive qualification criteria, they risk excluding SMEs that possess adequate capacity to perform the work but lack the extensive track record or financial resources demanded by overly stringent thresholds.

In the EU, the qualification process can be divided into three phases: the initial phase involves the exclusion of tenderers; the subsequent phase entails the evaluation of tenderers' technical and financial capacities, and the final phase constitutes the shortlisting process, which limits the number of applicants eligible for participation in

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[426] See OECD, *SMEs in Public Procurement* (n 18) 37; Wayne A. Wittig, 'SME and Export-Led Growth: Are There Roles for Public Procurement Programmes? A Practical Guide for Assessing and Developing Public Procurement Programmes to Assist SMEs' (International Trade Centre), <https://www.wto.org/english/tratop_e/gproc_e/wkshop_tanz_jan03/itcdemo3_e.pdf> accessed 17 July 2025, 20.

[427] Martin Trybus, 'European Union Law and Public Procurement' (Institute of European Law Working Papers, 2017) <http://epapers.bham.ac.uk/3052/> accessed 12 October 2023.

[428] Laura Carpineti, Gustavo Piga, and Matteo Zanza, 'The Variety of Procurement Practice: Evidence from Public Procurement' in Nicola Dimitri, Gustavo Piga, and Giancarlo Spagnolo (eds), *Handbook of Procurement* (Cambridge University Press 2006) 18.

[429] Steen Treumer, 'Exclusion, Qualification and Selection of Candidates and Tenderers in EU Procurement' in Martin Burgi, Martin Trybus, Steen Treumer (eds), *Qualification, Selection and Exclusion in EU Procurement* (DJØF Publishing 2016) 15.

tendering.[430] Based on this division, the open procedure pursuant to Article 27 Directive 2014/24/EU does not include the third phase.[431] By establishing selection criteria, contracting authorities narrow down potential bidders to those possessing a specific level of technical and financial capacity.[432] Therefore, the qualification assessment focuses on tenderers themselves, rather than the merits of the tenders.

Specifically, selection criteria comprise three key aspects: suitability to pursue the professional activity, economic and financial standing, and technical and professional ability.[433] Contracting authorities may require evidence from economic operators to prove they meet the selection criteria.[434] Among these, the need for past performance records by the contracting authority to demonstrate technical and professional ability poses a barrier for new entrants lacking prior experience.[435]

In the EU, six competitive tendering procedures are recognised under Directive 2014/24/EU: the open procedure, the restricted procedure, the competitive negotiated procedure, the competitive dialogue, the innovation partnership, and the design contest.[436] While all aim to foster competition among economic operators, they differ in structure and complexity, differences that are particularly relevant to SMEs. The open procedure is perceived as the most accessible and competitive procedure, as it is a single-stage process in which any interested economic operator can submit a

[430] Michael Steinicke, 'Qualification and Shortlisting' in Martin Trybus, Roberto Caranta and Gunilla Edelstam (eds), *EU Public Contract Law: Public Procurement and Beyond* (Bruylant 2014) 123.
[431] Directive 2014/24/EU, art 27.
[432] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 183.
[433] Directive 2014/24/EU, arts 27(1), 56.
[434] Directive 2014/24/EU, art 58(4).
[435] ibid. This will be discussed in depth in Chapter 7.
[436] Directive 2014/24/EU, ch 1.

tender in response to a call for competition.[437] By contrast, all the other procedures involve a two-stage approach, where authorities first conduct a qualitative selection and a shortlisting process to limit the number of suitable candidates to be invited to tender.[438]

Although the single-stage structure of open procedures formally precludes the exclusion of participants prior to tender submission, thus appearing to facilitate SME access, this procedural openness conceals a more complex internal process. Pursuant to Article 56(2) Directive 2014/24/EU, unless a Member State restricts or excludes this option, contracting authorities may choose to review tenders submitted by all bidders before assessing whether they meet the selection criteria and whether any exclusion grounds apply.[439] As this is a permissive rather than an obligatory provision,[440] contracting authorities may also decide to conduct qualitative selection before evaluating tenders, particularly as tenderers are required to submit all requested information for qualitative selection along with their tenders.[441] As the Court of Justice of the European Union has confirmed, Article 27(1) Directive 2014/24/EU does not prohibit the simultaneous evaluation of qualifications and tenders.[442] In practice, this flexibility enables contracting authorities to carry out a two-step assessment within the nominally single-stage procedure.

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[437] Directive 2014/24/EU, art 27; also see 'Article 27 Open Procedure' in Roberto Caranta and Albert Sanchez-Graells (eds), *European Public Procurement: Commentary on Directive 2014/24/EU* (Edward Elgar Publishing 2021) 186, 304.

[438] The shortlisting process will be discussed further in Chapter 5, Section 5.4.

[439] Directive 2014/24/EU, art 56(2).

[440] See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 718, para 7-144.

[441] Directive 2014/24/EU, art 27(1). Article 27(1)(3) states that 'the tender shall be accompanied by the information for qualitative selection that is requested by the contracting authority', which means bidders have to submit information for qualitative selection along with its tender.

[442] Case C-546/16 *Montte SL v Musikene* ECLI:EU:C:2018:752, para 27.

Moreover, Article 27(1)(3) requires that all requested information for qualitative selection be submitted alongside the tender, placing a significant administrative burden on bidders from the outset.[443] This creates a paradox: although the open procedure is structurally inclusive, it may in practice prove burdensome for SMEs, particularly those with limited legal and technical capacity to prepare fully compliant submissions within a given time limit.[444] Given that the qualification process reduces the volume of tenders to be evaluated, contracting authorities may have limited incentive to review tenders without first evaluating qualifications.[445] Accordingly, open procedures are not necessarily the most SME-friendly procedure; they may, in practice, present greater challenges as they require submission of a full tender and all accompanying qualification documentation at the initial stage.

At the qualitative selection stage, SMEs mainly have difficulties meeting the financial criteria, contending that the financial and technical capacity requirements disproportionately burden small bidders with limited capacity.[446] From the perspective of contracting authorities, imposing financial and technical requirements can ensure that potential contractors possess the capability to fulfil the contract, albeit with no full guarantee of satisfactory contract performance.[447] Restricting bidders to companies with a certain level of financial capacity appears to be a method of mitigating the risk

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[443] Directive 2014/24/EU, art 27(1)(3).

[444] There is a concern that the time limit for open procedures could be too short for SMEs. See Pedro Telles and Luke Butler, 'Public Procurement Award Procedures in 2014 Directive', in Francois Lichère, Roberto Caranta and Steen Treumer (eds), *Modernising Public Procurement: The New Directive* (DJØF Publishing 2014) 138.

[445] Albert Sanchez-Graells, 'Exclusion, Qualitative Selection and Short-Listing in the New Public Sector Procurement Directive 2014/24' in Lichère, Caranta and Treumer (eds) (n 444) 97.

[446] GHK (2010) (n 334) 48.

[447] Contracting authorities may require performance bond to ensure their interests protected when contract is not delivered. See Chapter 5, Section 5.2.3.

of potential failure, a reasonable approach, but a delicate balance is needed.[448] Typically, the financial requirement relies on annual turnover as an indicator to assess whether the economic operator possesses sufficient financial resources. For instance, if a contract is valued at EUR 5 million, the contracting authority may require that bidders have an annual turnover of at least EUR 10 million, or even more. This approach poses a barrier for micro and small businesses to get access to large contracts, potentially with an estimated value exceeding EUR 10 million, as small enterprises have a maximum annual turnover of EUR 10 million.[449] Consequently, turnover requirements or similar financial criteria can act as entry barriers for SMEs to participate in the bidding process, especially for those micro and small enterprises interested in higher-value contracts. The crucial task at hand is striking the right balance between encouraging SME participation and establishing qualitative requirements to safeguard contracting authorities from the risks of contractor default. Chapter 5 will discuss these issues in depth.[450]

In the US, the qualification process is slightly different. Prospective contractors need to be identified as 'responsible' by the federal agency.[451] In the case of a small business, if a contracting officer determines that it 'lacks certain elements of responsibility', the contracting officer shall refer to the SBA, which will decide whether a Certificate of Competency (COC) shall be issued.[452] The contracting officer can appeal the decision of a COC, but the SBA Associate Administrator makes the final

[448] See Chapter 5, Section 5.2.1.
[449] As reflected in Table 3.4, micro-sized enterprises report the issue of disproportionate technical and financial criteria more frequently than small and large enterprises. See GHK (2010) (n 334) 48, figure 4.11.
[450] See Chapter 5.
[451] 48 CFR § 9.105-2.
[452] ibid.

determination in such matters.[453] General standards for responsibility, stipulated in FAR 9.104-1, include having 'adequate financial resources to perform the contract or the ability to obtain them,' a 'satisfactory performance record,' a 'satisfactory record of integrity and business ethics,' and the 'necessary production, construction, and technical equipment and facilities or the ability to obtain them'.[454] In comparison with the EU, the US qualification procedure incorporates past performance more straightforwardly, potentially posing a barrier for new entrants to the Federal market. This concern was also raised and discussed in a hearing hosted by the House Committee on Small Business of the US Congress, where a small business owner testified that past experience is like a 'vehicle' for bidders to compete for federal contracts.[455] Without this 'vehicle', it is difficult for small businesses to participate in this marketplace. Despite the stringent standards, FAR 9.104-1 specifies that the contracting officer should not deem a bidder 'nonresponsible' solely based on a lack of relevant experience.[456] Even if a contracting officer determines that a small business lacks certain aspects of responsibility, the officer shall refer this concern to the SBA.[457] The SBA has its own regulations and guidelines about COC competency, which is beneficial for those small businesses without past experience or adequate financial resources.[458] With regard to the the financial capacity standard, as long as

[453] 48 CFR § 19.6.

[454] 48 CFR § 9.104-1.

[455] US House Committee on Small Business, 'Leveling the Playing Field: State of Small Business Contracting' (Hearing, 11 May 2023) <http://www.congress.gov/> accessed 28 May 2023, testimony of Ms. Jacqueline K. Lopez.

[456] In France, it is also stipulated that a contracting authority cannot exclude a bidder based solely on no past experience. See Francois Lichère, 'Qualification, Selection and Exclusion of Economic Operator under French Public Procurement Law' in Burgi, Trybus, and Treumer (eds) (n 429) 41.

[457] 48 CFR § 9.105-2.

[458] The SBA published a workbook on the content and procedures of applying for a COC. See US SBA Office of Government Contracting and Business Development, 'Certificate of Competency (Program Overview)' (September 2014) <https://www.sba.gov/sites/default/files/2018-02/COC_workbook.pdf> accessed 28 May 2023.

the bidder can obtain financial resources to undertake the contract, it will be deemed a responsible contractor. Various funding programs offered by the SBA can help small businesses prove their potential to obtain financial resources.[459]

In summary, excessive qualification criteria can act as barriers to entry for SMEs, especially for micro and small businesses. In the US, although the terminology differs, a comparable assessment is carried out through the determination of responsibility under FAR Part 9. This includes factors such as financial capacity, technical skills, and past performance record. While these standards can be demanding, small businesses in the US have access to various forms of support from the SBA. The different approaches taken by the EU and the US to managing the qualification process and making them more friendly to SMEs will be discussed in Chapter 5.[460]

3.3.4 Lowest price as the award criterion

The lowest price award criterion is often perceived as a barrier for SMEs aiming to secure public contracts.[461] The emphasis on price disproportionately benefits larger companies that can achieve economies of scale more readily than SMEs and consequently offer lower prices. While the lowest price criterion is widely utilised in

[459] For example, the loan program can help a small business directly, and the surety premium scheme provides guarantees to protect contracting authorities against possible default of a small business. For more information, see US SBA 'Surety Bonds' <https://www.sba.gov/funding-programs/surety-bonds#sba-guarantees-surety-bonds> accessed 28 May 2023.

[460] See Chapter 5.

[461] See Kim Loader, 'SME Suppliers and the Challenge of Public Procurement: Evidence Revealed by a UK Government Online Feedback Facility' (2015) 21 Journal of Purchasing and Supply Management 103; David Pickernell and others, 'Competing Agendas in Public Procurement: An Empirical Analysis of Opportunities and Limits in the UK for SMEs' (2011) 29 Environment and Planning C: Government and Policy 641.

practice due to its simplicity of implementation and monitoring, it has inherent limitations, neglecting qualitative aspects such as quality, innovation, and life-cycle costs.[462]

Recognising these limitations, Directive 2014/24/EU introduced the most economically advantageous tender (MEAT) as the default award criterion.[463] Member States have the flexibility to incorporate various factors, such as quality, price, social considerations, and environmental concerns into the award criteria.[464] Nevertheless, despite the implementation of the MEAT criterion, the lowest price criterion continues to dominate in approximately 58 per cent of awards on average across EU Member States, and in over 80 per cent of awards in eleven Member States.[465] Some argue that the MEAT criterion could positively impact SME participation in public procurement, as it allows contracting authorities to consider innovative solutions, an area where SMEs often excel.[466] If this assumption is accepted, the use of the MEAT criterion is likely to enhance the probability of SME being awarded contracts, compared with the lowest price criterion.

Empirical studies show mixed findings regarding this assumption. Ancarani et al. discovered that the MEAT criterion is either not significantly correlated with SMEs' success rate or, conversely, the lowest price criterion, rather than the MEAT criterion,

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[462] OECD SIGMA, *Brief 8 Public Procurement, Setting the Award Criteria* (OECD Publishing 2011) 3 <https://www.oecd.org/content/dam/oecd/en/publications/reports/2011/01/setting-the-award-criteria_g17a25e0/5js4wzvcz69q-en.pdf> accessed 12 June 2024.

[463] Directive 2014/24/EU, art 67.

[464] ibid.

[465] European Commission, 'Single Market and Competitiveness Scoreboard, Access to public procurement' <https://single-market-scoreboard.ec.europa.eu/business-framework-conditions/public-procurement_en> accessed 12 June 2024.

[466] OECD SIGMA (n 462) 3; Carmela Di Mauro, Alessandro Ancarani and Tara Hartley, 'Unravelling SMEs' Participation and Success in Public Procurement' (2020) 20 Journal of Public Procurement 377.

is positively correlated with the success of SMEs.[467] This finding is also supported by Albano et al., indicating that SMEs' rate of success remains approximately the same when applying the lowest price criterion or the MEAT criterion.[468] The overall value of contracts awarded to SMEs tends to be greater when the lowest price criterion is used, as opposed to the MEAT criterion.[469] This discrepancy is likely due to the fact that a majority of public procurement contracts are awarded using the lowest price criterion, and the MEAT criterion is only used in a limited share of contracts.[470]

Furthermore, the success rate of SMEs increases significantly when the lowest price criterion is used compared with the MEAT criterion.[471] Stake has found that, when the MEAT criterion is used, the probability of SMEs being awarded contracts decreases compared with large businesses, i.e. the probability of large businesses being awarded contracts increases.[472] This outcome might be attributed to a potential positive correlation between the MEAT criterion and contract value, leading contracting authorities to prefer the MEAT criterion for larger and more complex contracts while opting for the lowest price criterion for lower-value contracts.[473] A more detailed empirical study by Mauro et al. examined the correlation between the use of the MEAT criterion and SME participation and success.[474] Findings show that while the MEAT criterion is correlated with an increased SME participation in bidding for

[467] This finding is evidenced by Ancarani and others (n 128) and Luigi Albano and Zampino (n 422).
[468] GHK (2010) (n 334) 48.
[469] ibid.
[470] European Commission, 'Single Market and Competitiveness Scoreboard, Access to public procurement' (n 465).
[471] ibid.
[472] Johan Stake, 'Evaluating Quality or Lowest Price: Consequences for Small and Medium-Sized Enterprises in Public Procurement' (2017) 42 Journal of Technology Transfer 1143.
[473] ibid.
[474] Di Mauro, Ancarani and Hartley (n 466).

public contracts, the success rate is negatively correlated with this criterion, consistent with previous findings by Stake.[475]

In the US, the use of the lowest price as an award criterion does not draw many complaints from small businesses. One plausible explanation is that small businesses often bid for contracts exclusively reserved for small businesses or within their sub-categories, which will be discussed in Chapter 7. Consequently, the competition remains within a group of enterprises with similar capacities. In contrast, within the EU, competition in public procurement markets consistently involves both SMEs and large enterprises.

In summary, there is a lack of sufficient evidence demonstrating that the lowest-price criterion is hindering SME participation and success in public procurement. Instead, it is more of a perceptual concern for SMEs rather than a tangible barrier. More importantly, the lowest-price criterion is not an entry barrier, regardless of whether it is associated with a higher winning rate of SMEs or not, as it does not hinder SMEs from accessing public procurement markets.

3.3.5 Delayed payment

Stakeholders across countries have recognised that long payment cycles and delayed payments diminish SMEs' incentives to bid for government contracts.[476] Pursuant to Article 2 Directive 2011/7/EU, late payment is defined as 'payment not made within

[475] ibid.
[476] UNDP (n 317); OECD, *SMEs in Public Procurement* (n 18) 37.

the contractual or statutory period of payment'.[477] In the EU, late payment has been regarded as a significant factor discouraging SMEs from participating in public procurement since the 1990s.[478] According to Ancarani et al, it takes nearly double the time of the contractual terms for suppliers to receive payment from contracting authorities in Italy.[479] Across all EU Member States, governments tend to take longer to pay contractors than private-sector businesses, thereby exacerbating cash flow challenges for SMEs involved in public procurement.[480]

In the US, the Prompt Payment Act (PPA), enacted by Congress in 1982, requires all federal agencies to pay contractors by the date specified in the contract or within 30 days of receiving a proper invoice, whichever is later.[481] In cases of delayed payments, federal agencies are obligated to pay interest penalties.[482] While the statutory framework aims to ensure financial fairness, subsequent amendments to the FAR have further advanced this objective by addressing the specific needs of small businesses.[483] Notably, FAR 32.009 requires federal agencies to provide accelerated payments to small business contractors 'to the fullest extent permitted by law', with a recommended goal of 15 days after receiving proper invoices and documentation, unless a specific due date is defined in the contract.[484] Although FAR 32.009 expresses a government-wide policy to provide accelerated payments to small

[477] Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions, OJ L 48.
[478] Andrew Erridge, 'Involvement of SMEs in Public Procurement' (1998) 2 Public Procurement Law Review 37.
[479] Ancarani and others (n 128) 1106.
[480] European Commission, *EU Payment Observatory Annual Report 2023* (Publications Office 2024) 6.
[481] 31 USC § 3903(a)(1); 48 CFR § 52.232-25.
[482] 31 USC § 3903(a)(1).
[483] 48 CFR § pt 32.
[484] 48 CFR § 32.009.

businesses, it remains predominantly aspirational and late payments persist in federal procurement.[485]

While late payments do not directly hinder SMEs from entering the procurement market or reduce their probability of being awarded contracts, they do exert a negative influence on SMEs' willingness to engage in public procurement. Given that SMEs often rely on private lending and encounter higher financing and operational costs than their larger counterparts, payment delays prove detrimental in both contractor and subcontractor scenarios.[486] The latter is particularly exacerbated, as payments typically emanate from prime contractors unless explicitly stated otherwise in the contract, thereby intensifying the impact on subcontractors.[487] Late payments can set off a chain reaction among suppliers, particularly affecting smaller businesses.[488] Operational disruptions and potential cash flow crises could, in extreme cases, lead to the exit or bankruptcy of small enterprises.[489]

Payment delays are prevalent not only in public procurement but also within the private market, especially in industries characterised by long supply chains.[490] The *European Payment Report 2023* by Intrum reveals that approximately 53 per cent of surveyed

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[485] According to testimony given during a congressional hearing in 2024, small business contractors continue to be routinely burdened by payment delays. See US House of Representatives (n 337).

[486] World Bank Group, *Benchmarking 2020 Infrastructure Development* (Report 153567, 7 October 2020) <https://documents1.worldbank.org/curated/en/369621602050134332/pdf/Benchmarking-Infrastructure-Development-2020-Assessing-Regulatory-Quality-to-Prepare-Procure-and-Manage-PPPs-and-Traditional-Public-Investment-in-Infrastructure-Projects.pdf> accessed 28 May 2023.

[487] Max V Kidalov, 'U.S. and E.U. SME Subcontracting Policy and Practice Trends: Towards a Transatlantic Accountability Consensus' (2013) 13 Journal of Public Procurement 39.

[488] Sam Wood, 'The Domino Effect - the Impact of Late Payments' (*Plum Consulting*, 7 December 2017) <https://plumconsulting.co.uk/domino-effect-impact-late-payments/> accessed 16 February 2023.

[489] ibid.

[490] Mohamed Hicham Salah Eddine, Tarik Saikouk and Abdelaziz Berrado, 'Payment Delay in Supply Chain Management: A Systematic Literature Review' (2021) 14 International Journal of Procurement Management 441.

enterprises find negotiating payment terms increasingly challenging.[491] Across SMEs in the EU, it took approximately 64 days to collect payments in 2021, with an anticipated increase of 1.5 days due to observed inflation in 2022.[492] The Single Market Scoreboard indicates an average payment cycle of over 60 days for business-to-business transactions.[493] Although SMEs express concerns about payment delays in public procurement, they perceive payments from governments as more secure compared to transactions in the private market.[494] In the private sector, if a business fails to pay, the available remedies can take so long that an SME may face bankruptcy before the matter is resolved.[495] This partly explains the reason that SMEs participate in government procurement despite various barriers and challenges discussed in this chapter.

In summary, payment delays do not function as an entry barrier for SMEs to participate in public procurement, nor do they have an impact on their winning. Resolving the delayed payment issue stands to benefit all businesses, especially SMEs, as they have limited financial resources compared with large businesses. Moreover, payment delays indirectly increase bidding costs, as bidders need to allocate additional cash flow to manage them. The issue of bidding costs is discussed in the next section.

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[491] intrum, 'European Payment Report 2023 White Paper Country snapshots' (26th Annual Edition, 2023) <https://b2b.intrum.com/l/700283/2023-05-31/tvhqx/700283/1685515014buHdcQfU/EPR_2023_Country_Snapshots_White_Paper.pdf> accessed 29 October 2023.

[492] European Commission, *Annual Report on European SMEs 2022/2023* (JRC134323, 12 July 2023) <https://publications.jrc.ec.europa.eu/repository/handle/JRC134323> accessed 29 October 2023.

[493] European Commission, 'Access to Finance' (Single Market and Competitiveness Scoreboard) <https://single-market-scoreboard.ec.europa.eu/business-framework-conditions/access-finance_en> accessed 01 June 2025.

[494] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74); also see Susan A MacManus, 'Why Businesses Are Reluctant to Sell to Governments' (1991) 51 Public Administration Review 328.

[495] t33 Srl (n 334) 93.

3.3.6 Costs of bidding

Several of the barriers most frequently reported by SMEs pertain to the procurement process itself. As shown in Table 3.1, these include complex and time-consuming procedures, short deadlines for preparing tenders, and excessive administrative burden.[496] These issues are not isolated; rather, they reflect the high transaction costs associated with participating in public procurement. In economic terms, transaction costs include expenses incurred in identifying trading partners, negotiating prices, and resolving disputes.[497] In public procurement, SMEs experience these transaction costs when searching for opportunities, navigating complex regulations, preparing tender documents, and ensuring compliance throughout the bidding process.[498] These costs are particularly burdensome for SMEs, as they often lack specialised legal and procurement expertise. To reduce the administrative costs associated with the qualification process, the EU introduced the European Single Procurement Document (ESPD), which is a self-declaration system under which bidders are not required to provide supporting certificates and documentation when requested, usually after the tender evaluation.[499] The implications of this mechanism for SMEs will be examined in Chapter 5.[500]

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[496] See Table 3.1.

[497] See RH Coase, 'The Nature of the Firm' (1937) 4 Economica 386.

[498] Trybus and Andrecka (n 55); Loader, 'SME Suppliers and the Challenge of Public Procurement: Evidence Revealed by a UK Government Online Feedback Facility' (n 461); K Karjalainen and K Kemppainen, 'The Involvement of Small and Medium-Sized Enterprises in Public Procurement: Impact of Resource Perceptions, Electronic Systems and Enterprise Size' (2008) 14 Journal of Purchasing and Supply Management 230.

[499] Directive 2014/24/EU, art 59.

[500] See Chapter 5, Section 5.1.

In the US, a survey conducted by Censeo Consulting Group revealed that 85 per cent of small business respondents viewed the procurement process as overly complex, from the initial call for tenders to contract award.[501] The volume of paperwork required during the bidding process can make participation unprofitable for a small business.[502] Similarly, in the EU, SMEs have recurrently identified the high cost of the procurement process as a barrier to access.[503] In 2013, the estimated cost of preparing a standard tender in the EU exceeded GBP 3200.[504] The same study found that the average cost of a competitive procurement process was GBP 23,900 in the EU, and as much as GBP 45,200 in the UK, with only GBP 8,000 borne by contracting authorities and the remainder falling on bidders.[505] Since these costs are usually mostly fixed per tender, they represent a greater proportion of lower-value contracts than of larger ones.[506] Empirical work has further shown that although the overall transaction cost of procurement averaged about 1 per cent of contract value, it increased to 6.6 per cent to 8.1 per cent for small purchases.[507] These figures suggest that SMEs, which typically target lower-value contracts, face disproportionately high costs relative to the value of the contract.[508] Moreover, the lack of any assurance of success necessitates

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[501] Censeo Consulting Group. 'Cracking the Government Procurement Code' (n 336).

[502] ibid.

[503] See European Commission, *Evaluation of SMEs' access to public procurement markets in the EU* (2010) 52; European Commission, *Analysis of the SMEs' participation in public procurement and the measures to support it* (2019) 197; European Commission, *An Analysis of SMEs' Needs in Public Procurement* (2021) 47.

[504] Flynn and Davis (n 58) at 342 citing Centre for Economic and Business Research, 'UK procurement most expensive in the EU' <https://cebr.com/reports/uk-procurement-most-expensive-in-eu/> accessed 02 August 2024.

[505] ibid.

[506] Karjalainen and Kemppainen (n 498); OECD, *SMEs and Public Procurement* (n 18) 84.

[507] Olga Balaeva and others, 'Public Procurement Transaction Costs: A Country-Level Assessment' (2022) 42 Public Money & Management 181, 186.

[508] European Commission, 'European Code of Best Practices Facilitating Access by SMEs to Public Procurement Contracts' (Staff Working Document) SEC (2008) 2193 final, 5.

that such investments be factored into bids, potentially diminishing their competitiveness and discouraging their participation.

Significantly, the source of these burdens is not merely from administrative practice but is embedded in the legal and regulatory procurement frameworks themselves.[509] Although some governments have adopted SME-friendly measures, these provisions are situated within broader regulatory regimes that remain complex and costly to navigate. The scale of regulatory burden has been illustrated by recent evidence from the US. At a 2024 hearing before the House Committee on Small Business, a small business owner testified to the considerable expenses incurred in interpreting the estimated 94,000 pages of federal procurement rules.[510] Most small businesses cannot afford full-time legal counsel, yet are compelled to engage lawyers simply to understand the rules.[511] A similar pattern is evident in the EU. In a public consultation conducted in 2013, the European Commission identified public procurement as one of the ten most burdensome policy areas for SMEs.[512] Although simplification was one of the stated objectives of the 2014 reform of public sector directives, Directive 2014/24/EU (79 pages excluding annexes) is almost twice the length of Directive 2004/18/EC (43 pages excluding annexes). [513] These developments demonstrate that, despite policy commitments to SME participation, the cumulative effect of expanding

[509] Open Contracting Partnership, IDRC, OD4D, 'Inclusive and effective public procurement: Findings and lessons from research in 12 countries' (2022) <https://www.open-contracting.org/resources/action-research-inclusive-and-effective-public-procurement/> accessed 15 August 2024, 3.

[510] US House of Representatives (n 337) 11.

[511] ibid.

[512] European Commission, 'Top 10 most burdensome EU laws for small and medium-sized enterprises: How the Commission is helping SMEs' (MEMO 13/168, 7 March 2013).

[513] See Directive 2014/24/EU, recital 127; also see European Commission, 'EU Public Procurement reform: Less bureaucracy, higher efficiency' (Ref.Ares (2016)1875822 - 20/04/2016) 6.

and increasingly detailed procurement legislation may risk entrenching, rather than alleviating, the barriers such measures seek to remove.

In summary, the costs associated with bidding can function as an entry barrier for SMEs, whether arising from procedural inefficiencies or regulatory design. Surveys and economic analyses consistently demonstrate that these costs are disproportionately burdensome for SMEs. Subsequent chapters will examine mechanisms for alleviating this burden. In particular, Chapter 5 explores how qualification procedures can be managed to facilitate SME access to public procurement opportunities.

3.3.7 Advantages of the incumbent supplier

In the Censeo Consulting Group survey of 455 small businesses in the US, 83 per cent of respondents agreed that incumbent contractors are in a privileged position when competing for new procurement contracts.[514] Moreover, 84 per cent believed that contracting authorities tend to favour businesses with more past experience.[515] These responses reflect a prevalent perception that incumbents benefit from structural advantages, even in open and competitive procedures.[516]

[514] Censeo Consulting Group. 'Cracking the Government Procurement Code' (n 336).
[515] ibid.
[516] Elisabetta Iossa, 'Competition for the Market: Tackling the Incumbency Advantage' (OECD Global Forum on Competition, 2019) <https://one.oecd.org/document/DAF/COMP/GF(2019)10/en/pdf> accessed 15 November 2023.

In the US, incumbency is not inherently regarded as an unfair advantage.[517] Contracting authorities may lawfully take past performance into account, provided this factor is expressly stated in the solicitation's evaluation criteria.[518] This stance is consistently upheld in the bid protests reviewed by the Government Accountability Office (GAO). For instance, in *Dalfi, Inc.*, the GAO denied a protest by an unsuccessful bidder, holding that the solicitation had explicitly specified past performance and personnel resources as the primary evaluation criteria, with price given comparatively less weight.[519] Accordingly, the agency's decision to award the contract to the incumbent was considered reasonable and lawful, despite a higher bid.[520] In *Native Energy & Technology, Inc.*, the GAO upheld a protest where the contracting authority had relied on internal knowledge of the incumbent's past performance to award additional points, despite the absence of such information in the bid itself.[521] The GAO concluded that this practice violated the requirements of procedural fairness and transparency, consequently mandating a re-evaluation of the submitted tenders.[522] While the incumbent contractors may leverage their past experience, such advantages can only be considered if the evaluation criteria explicitly include the relevant aspects; otherwise, contracting officers cannot take them into account without breaching transparency requirements. To address the risk that past performance criteria may discourage small businesses, Chapter 5 will examine the regulatory framework in the

[517] Steven W Feldman, '§ 10:6 Role of incumbency' in Government Contract Awards: Negotiation and Sealed Bidding (Westlaw, October 2023 update) accessed 15 November 2023.
[518] See Chapter 5. Section 5.2.2.
[519] US Government Accountability Office (GAO), Matter of B-224248 (7 January 1987) 87-1 CPD 24.
[520] ibid.
[521] US GAO, Matter of Native Energy & Technology, Inc. B-416783, B-416783.2, B-416783.3, B-416783.4 (11 December 2018) 2019 CPD 6.
[522] ibid.

Federal Acquisition Regulation and the support mechanisms provided by the Small Business Administration.[523]

Similar issues have arisen before the Court of Justice of the European Union (CJEU). In Case T-345/03 *Evropaiki Dynamiki*, the General Court annulled an award decision where a subcontractor of a successful tenderer, also the incumbent, was alleged to have had access to undisclosed pricing-relevant information.[524] The CJEU determined that the failure to provide equal access to this information constituted a breach of the principle of equal treatment.[525] However, in Case T-10/17, the CJEU upheld the contracting authority's decision to award a contract to an incumbent, emphasising that advantages arising from previous experience do not contravene the principle of equal treatment, provided that all tenderers are provided equal access to information and that transparency is guaranteed.[526]

Regarding whether incumbency advantages constitute a barrier to SME participation, the cases reviewed suggest that while incumbency can offer a competitive advantage, its impact is nuanced and depends on how procurement rules and evaluation criteria are applied. Applying the first criterion in the definition of a barrier proposed in section 3.2, incumbency does not originate in procurement rules or practices. However, the design of evaluation criteria may indirectly reinforce an incumbent's advantage. Regarding the second criterion, there is some evidence of a discouraging effect on SME participation, particularly when past performance is included in evaluation criteria. As for the third criterion, which concerns whether the barrier disproportionately affects

[523] See Chapter 5, Section 5.2.3.
[524] Case T-345/03 *Evropaiki Dynamiki v Commission of the European Communities* [2006] ECR II-3415.
[525] ibid para 68.
[526] Case T-10/17 *Proof IT SIA v European Institute for Gender Equality* (EIGE) ECLI:EU:T:2018:682.

SMEs compared to large businesses, the answer is less definitive. Large businesses lacking relevant experience within the public sector may face comparable disadvantages, and the incumbents themselves may be SMEs. A study by GovShop indicates that the incumbency advantage is widely perceived as an entry barrier affecting all bidders in the US federal procurement market, rather than small businesses specifically.[527] It is noteworthy that small businesses more frequently raise this concern in the US than by SMEs in the EU, a divergence that may be attributed to the different approaches to past performance within the qualification process. Chapter 5 will examine how such requirements can, depending on their design and application, either discourage or facilitate SME participation.

3.3.8 Political uncertainty

Concerns regarding political uncertainty have primarily been identified in empirical studies conducted in the US.[528] According to the *Goldman Sachs 10,000 Small Business Voices* survey, a number of small business owners cited political uncertainty as a reason for hesitating to participate in federal procurement.[529] Respondents expressed concerns that small businesses are not sufficiently prioritised in the federal

[527] Among different understanding of 'entry barriers', Stigler proposed that 'entry barriers' are the costs borne by new entrants but not borne by the incumbent firms. See George Stigler, *The Organization of Industry* (Richard D Irwin 1968) 67. In the public procurement context, incumbent suppliers have the advantages of being familiar with the contracting authority and procurement process, the costs of finding information will have to be borne by new entrants.

[528] For example, see Raj Sharma, Rob Handfield, and Daniel J. Finkenstadt, 'Why Suppliers Struggle To Do Business With the Government', (California Management Review Insights, 22 January 2025) <https://cmr.berkeley.edu/2025/01/why-suppliers-struggle-to-do-business-with-the-government/> accessed 15 August 2025.

[529] Kumar and Wiens (n 407).

procurement system.[530] Likewise, findings from the Censeo Consulting Group survey show that political uncertainty is a recognised concern among small businesses, although it is ranked lower in relevance than more immediate challenges such as the complexity of procurement procedures or incumbent supplier advantages.[531] The concern regarding political uncertainty within the US context may be attributed to distinctive features of the federal procurement system, including its emphasis on efficiency and the coexistence of multiple preferential programmes targeting specific sectors, such as the use of Multiple Award Contracts, various small business set-aside programmes, and contracts awarded to prison industries, etc.[532] Chapter 7 will examine the reserved contracts regime in detail, with particular attention to the potential tensions that may arise between the promotion of small businesses and other competing objectives embedded within the federal procurement framework.[533] Given this policy context, it is comprehensible that small business owners may perceive alterations in administration or fiscal priorities as potential threats to the consistency of procurement preferences that support their participation. Nevertheless, political uncertainty does not in itself constitute a structural barrier to market access. Rather, it is more appropriately regarded as a factor influencing SMEs' willingness to participate in public procurement.

[530] ibid.
[531] Censeo Consulting Group. 'Cracking the Government Procurement Code' (n 336)
[532] See Chapter 7.
[533] See Chapter 7, Section 7.1.

3.3.9 Summary

This section has critically examined eight challenges commonly faced by SMEs in public procurement: lack of clear information, large contract size, demanding qualification criteria, the lowest price as the award criterion, delayed payments, high bidding costs, the advantages of incumbent suppliers, and political uncertainty. Although all of them are frequently cited in surveys and policy consultations, only some genuinely act as entry barriers that justify government intervention.

Upon closer analysis, three of these challenges emerge as structural barriers to entry within the procurement system: contracts of excessive size that exclude SMEs from participation; qualification criteria that impose disproportionate burdens on SMEs relative to contract requirements; and transaction costs associated with bidding, which weigh more heavily on SMEs due to their limited administrative capacity. These barriers are not simply matters of perception or market competition; they arise from procurement rules and practices that restrict SME access to public procurement markets.

It is important to emphasise, however, that the extent to which these barriers are experienced varies considerably across SMEsAs discussed in Chapter 2, the SME category encompasses a wide spectrum of enterprises, ranging from microenterprises to medium-sized enterprises, entities that differ significantly in their internal resources, capacity, and experience within public procurement. A barrier that proves insurmountable for a microenterprise may pose little difficulty for a medium-sized enterprise. Indeed, survey evidence suggests that medium-sized enterprises often display capacities similar to those of large businesses. Therefore, the analysis of barriers in this chapter, and the SME-friendly measures examined in subsequent

chapters, should be read with due regard for this heterogeneity within the SME category.

To understand the persistence and universality of these barriers, it is essential to examine the underlying factors. The subsequent section undertakes this theoretical inquiry. Drawing on law and economics reasoning, it explores how both the internal limitations of SMEs and the behavioural patterns of contracting authorities contribute to the entrenchment of barriers to SME participation in public procurement.

3.4 A Theoretical Analysis of the Barriers Faced by SMEs

The previous section discussed a range of barriers and challenges identified in surveys on SME participation in public procurement across the EU and the US. Notably, the OECD has found that these concerns are broadly shared across jurisdictions, suggesting the presence of common factors.[534] This section turns to the underlying causes of those barriers. It considers how both market characteristics and institutional dynamics contribute to the persistent difficulties experienced by SMEs in public procurement.

3.4.1 Inherent limitations of SMEs

As discussed in Chapter 2, the SME category is highly heterogeneous.[535] However, many SMEs share certain limitations that impact their ability to engage in public

[534] OECD, *SMEs in Public Procurement* (n 18) 37; also see DCED (n 42) 18.
[535] See Chapter 2.

procurement, especially micro and small enterprises.[536] These inherent constraints include limited financial and human resources, as well as gaps in knowledge or expertise in public procurement.[537] Access to finance remains a critical concern. SMEs occupy a weaker position in credit markets relative to larger enterprises, and financial constraints are widely recognised in the economic literature as a key barrier to SME growth and development.[538] The financial constraint, as a consequential effect, impedes SMEs in satisfying the financial capacity criterion required by contracting authorities, thereby limiting their eligibility or competitiveness.[539] To address the issue of an excessively high financial capacity requirement, the EU has adopted a 'twice-the-contract-value' approach, which prohibits contracting authorities from requiring bidders to possess an annual turnover exceeding twice the contract value, except in duly justified cases.[540] This issue will be addressed in Chapter 5.[541]

Furthermore, Nooteboom has illustrated that smaller businesses incur higher transaction costs than larger businesses, especially in the context of regulatory compliance.[542] For instance, in the US, the cost of regulation per employee is estimated to be at least 36 per cent higher for small businesses than for large

[536] ibid.

[537] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74); UNDP (n 317).

[538] Yukins and Piga (n 123) 15; also see Thorsten Beck and Asli Demirguc-Kunt, 'Small and Medium-Size Enterprises: Access to Finance as a Growth Constraint' (2006) 30 Journal of Banking & Finance 2931.

[539] Hoekman and Taş (n 119).

[540] See Directive 2014/24/EU, art 58(3).

[541] See Chapter 5.

[542] Bart Nooteboom, 'Firm Size Effects on Transaction Costs' (1993) 5 Small Business Economics 283.

businesses.[543] In public procurement, these disproportionate compliance burdens help explain the lack of incentives for SMEs to participate.

In addition to financial constraints, human resources constitute a significant limiting factor for SMEs in engaging with public procurement.[544] SMEs often lack the internal capacity to dedicate staff to public procurement activities. Unlike large businesses, they may not have in-house legal or technical experts capable of navigating procurement regulations or prepare competitive bids.[545] The absence of such expertise undermines the quality and professionalism of tender submissions, reducing their probability of success and disincentivising future participation.[546]

Under the assumption of rational choice in economic theory, market participants, including SMEs, make a calculated assessment of the costs and benefits before committing themselves to a particular course of action.[547] Specifically, SMEs will invest in bidding for public procurement only if the expected benefits outweigh the anticipated costs. In many cases, SMEs incur high costs of bidding at an early stage, while the potential benefits are uncertain and contingent on a competitive process often skewed toward more experienced or better-resourced businesses. This asymmetry of costs and benefits discourages SME participation. The rational choice model, therefore, offers a conceptual framework for understanding SME participation and emphasises

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[543] National Association of Manufacturers, 'The Cost of Federal Regulation' (26 April 2019) <https://nam.org/issues/regulatory-and-legal-reform/cost-of-regulations/> accessed 13 November 2023.

[544] Kassa Woldesenbet and Ian Worthington, 'Public Procurement and Small Businesses: Estranged or Engaged?' (2019) 57 Journal of Small Business Management 1661.

[545] Marta Andhov, 'Sustainability, Public Procurement and SMEs – Challenges and Opportunities' (University of Copenhagen Faculty of Law Research Paper No. 2019-81, 5 February 2017) <https://papers.ssrn.com/abstract=2911828> accessed 22 November 2022.

[546] Flynn and Davis (n 58).

[547] Gary S. Becker, *The Economic Approach to Human Behavior* (University of Chicago Press 1976).

the importance of reducing costs or increasing perceived benefits as a strategy for government intervention.

3.4.2 Risk-aversion of contracting authorities

The barriers and challenges confronting SMEs reflect the risk-aversion of contracting authorities. Scholars in public choice theory posit that the prevalence of large companies in public procurement is rooted in the risk-averse nature of public officials.[548]

As previously discussed in 3.3.3, contracting authorities frequently rely on qualification criteria, such as financial capacity and past performance requirements, that are more easily satisfied by large businesses.[549] This tendency reflects an underlying assumption that SMEs are less reliable, less capable of absorbing contractual risk, and more likely to default.[550] Constrained by limited information and under institutional pressure to avoid contract performance, contracting officers often favour predictable outcomes and established large businesses over SMEs.[551] This risk perception, shaped by the bounded rationality,[552] can hinder foresight of long-term consequences, including market concentration, stronger negotiating positions for large businesses,

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[548] Christopher R Yukins, 'A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model' (2010) 40 Public Contract Law Journal 63.

[549] See Section 3.3.3.

[550] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).

[551] Flynn, 'Research on SME involvement in public procurement: A review, critique and conceptual framework' (n 49) 423. Also see Martin Trybus and Baudouin Heuninckx, 'Small and Medium-Sized Enterprises and EU Defence Procurement Law: The Soft Impact of Recommendation 2018/624/EU' (2023) 3 Public Procurement Law Review 115.

[552] For bounded rationality, see Herbert A Simon, *Administrative Behavior: A Study of Decision-Making Processes in Administrative Organizations* (4th edn, Free Press 1997).

and the strategic use of low-price 'loss-leaders' to secure market dominance.[553] While the belief persists that contracting with large companies reduces risk, this assumption has been challenged.[554] In practice, the bidding process's heavy emphasis on references (past performance) and stringent financial and technical criteria disproportionately advantages large, experienced bidders.[555] This issue will be discussed in Chapter 5, especially how to manage the qualification process to support SMEs in their participation in public procurement.[556]

In some cases, risk aversion translates to a deliberate narrowing of the bidder pool.[557] In the 2021 EU SME Needs Analysis, insights from an interactive session with contracting authorities unveiled a noteworthy rationale behind the imposition of stringent financial and technical criteria: to curtail the number of potential bidders in the tendering process.[558] This introduces an intriguing contradiction, as legislators and policymakers advocate for increased competition, anticipating improved value for money. Paradoxically, contracting authorities appear to be adopting a contrary approach by restricting competition by imposing rigorous qualification prerequisites. At the same time, contracting authorities recognise that reducing the number of tenderers does not necessarily correlate with an enhancement in the quality of proposals.[559] Instead, it reflects a divergence between the interests of the contracting

[553] Andrew Cox, 'Implementing 1992 Public Procurement Policy: Public and Private Obstacles to the Creation of the Single European Market' (1992) 2 Public Procurement Law Review 139.
[554] Thomas (n 73).
[555] See DCED (n 42) 18.
[556] See Chapter 5.
[557] See Chapter 5, Section 5.4.
[558] t33 Srl (n 334).
[559] ibid.

authorities (as agent) and those of the public (as principal).[560] From the perspective of contracting authorities, constraining competition within a pool of qualified bidders is viewed as a means to conserve time and effort required for comprehensive bid evaluations. However, this approach runs counter to the objective of fostering an open competition that maximises potential and identifies the best offers. This misalignment of interests underscores the importance of designing procurement frameworks that incentivise SME participation while still addressing legitimate risk concerns faced by contracting authorities, which will be discussed in Chapter 5 in relation to qualification criteria.

3.5 Conclusion

This chapter has addressed the first research question by distinguishing structural barriers that limit SME participation in public procurement from other commonly cited challenges. Drawing on existing literature, including survey evidence from SMEs, the analysis identifies three principal structural barriers confronted by SMEs in public procurement: large contract size, excessive qualification criteria, and the costs associated with bidding.[561] A theoretical examination further explains how these barriers arise from both supply-side and demand-side factors, including SMEs' resource constraints and contracting authorities' risk aversion. Internally, SMEs grapple with limited financial and technical resources in comparison to large companies, while externally they encounter procurement practices that may favour

[560] In this context, where the end-user of the contract is the public, the contracting authority functions as an agent acting on behalf of the public. For a discussion on the incentives of contracting authorities to implement SME-friendly measures, see Chapter 8, Section 8.4.3.

[561] See Sections 3.3.2, 3.3.3. and 3.3.6.

large contractors. Together, these internal and external constraints either increase the costs of participation or reduce the expected benefits of bidding, thereby discouraging SME engagement in public procurement.

The subsequent chapters will analyse measures that are adopted to address these barriers. More specifically, the EU has adopted dividing contracts into lots as the main approach to address the large contract size barrier, which is discussed in Chapter 4. To facilitate SME participation and reduce the administrative costs associated with bidding, both the EU and the US have implemented measures to streamline the qualification process, thereby making it easier for SMEs to submit applications. Lastly, providing SMEs with a bid evaluation preference or reserving a contract exclusively for small businesses does not address any particular barrier, but they alleviate or eliminate the competition pressure from large businesses to encourage SMEs to participate.

Chapter 4: Dividing Contracts into Lots to Facilitate SME Access to Public Procurement

4.1 Introduction

As discussed in Chapter 3, the large size of public contracts presents a significant challenge for SMEs in many countries, as they often lack the capacity to undertake high-value contracts when compared with large businesses.[562] Moreover, large contracts are linked with more demanding qualification requirements, which also deter SMEs from participating.[563] This is a separate issue from lot division and will be discussed in Chapter 5. Dividing contracts into smaller, more manageable lots, commonly referred to as lot division, helps to reduce contract size, enabling SMEs to participate as contractors rather than subcontractors.[564] This approach has thus been identified as an important means of improving SMEs' access to public procurement.[565] However, doubts have been raised about whether lot division has effectively achieved this objective, and concerns have emerged over how to balance it with other public

[562] For an analysis of how the substantial size of public contracts acts as a barrier to SMEs in accessing public procurement, see Chapter 3, Section 3.3.1; also see OECD, *SMEs in Public Procurement* (n 18) 37. This report conducted a survey across 26 OECD countries and found that 'difficulties relating to the size of contracts' are the most frequently cited constraint on SME access to public procurement.

[563] See Chapter 3, Section 3.3.3.

[564] Temidayo Akenroye and others, 'SME's Disinclination towards Subcontracting in the Public Sector Markets: An Attributional Perspective' (2022) 22 Journal of Public Procurement 109, 110. This thesis uses the terms 'division into lots' or 'lot division' to be consistent with the term in EU legislation.

[565] See OECD, Directorate for Financial and Enterprise Affairs Competition Committee, 'Hearing on Auctions and Tenders: Further issues' (Note by the secretariat, 19 June 2015) <https://one.oecd.org/document/DAF/COMP/WP2(2015)1/en/pdf> accessed 12 July 2024, 18. Also see OECD, *SMEs in Public Procurement* (n 18) 52; Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64); Martin Trybus, 'The Promotion of Small and Medium Sized Enterprises in Public Procurement: A Strategic Objective of the New Public Sector Directive?' in Steen Treumer and Mario Comba (eds), *Modernising Public Procurement: The Approach of EU Member States* (Edward Elgar Publishing 2018) 255.

procurement objectives, such as value for money and efficiency.[566] The central question is whether this measure genuinely enhances SMEs' access to public procurement contracts without undermining those other objectives. This involves several considerations, including whether lot division encourages SMEs to submit more bids and whether it improves their chances of being awarded contracts. The extent to which the balance between enhancing SME access and safeguarding other objectives is achieved depends mainly on the design of lot division, which varies across countries in several aspects.

Since the majority of countries implementing lot division in public procurement law are EU Member States, Directive 2014/14/EU, which establishes lot division ('divide or explain') as a default approach for all Member States, serves as the primary focus for analysis in this chapter.[567] Directive 2014/24/EU leaves Member States discretion to determine whether to render lot division mandatory or retain the more flexible approach it provides.[568] Against this background, this chapter examines how this measure has been transposed into national procurement regimes, focusing on France and Germany. The choice of these jurisdictions is explained by the fact that the division into lots originated in both, and they exemplify different approaches to its design, reflecting differing balances between facilitating SME access and pursuing other objectives in public procurement. In line with the overarching research question of this thesis, this chapter assesses whether lot division has achieved its intended objective of enhancing SME participation in public procurement, while maintaining an appropriate balance with objectives such as value for money and efficiency, and in the

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[566] Miguel Assis Raimundo, '"Aiming at the market you want": a critical analysis of the duties on division into lots under Directive 2014/24/EU' (2018) 4 Public Procurement Law Review 167, 168.
[567] Directive 2014/24/EU, art 46.
[568] ibid.

context of EU public procurement law, the principle of non-discrimination, drawing on both doctrinal analysis and empirical evidence.

4.2 The Purpose of Dividing Contracts into Lots in the EU

Before embarking on the analysis of different aspects of lot division, it is crucial to understand the purpose of this measure, as it influences the choice in the design of lot division. The purpose of implementing lot division varies across countries, and the legislative purpose and the incentives of contracting authorities might not always align with each other.[569] In the survey conducted by the OECD, contracting authorities reported that dividing contracts into lots is to promote SMEs and new entrants to the public procurement market, promote tender participation of some specific groups, foster competition in the market, avoid single supplier dependency, and spread risks.[570] Similarly, 'promoting SMEs' and 'fostering competition' were also cited in a survey as reasons for contracting authorities in EU Member States to implement lot division.[571]

Apart from the above-mentioned reasons, contracting authorities also use lot division to circumvent procedural requirements associated with higher-value contracts, such

[569] This is discussed further in Chapter 8.

[570] These five reasons were put forward by competition agencies in 27 jurisdictions in a survey conducted by the OECD Working Party 2 on Competition and Regulation in 2015. See OECD, *SMEs in Public Procurement* (n 18) 19. The respondents are competition agencies, and some are collaborated with other national governmental agencies overseeing public procurement.

[571] See Carpineti, Piga and Zanza (n 428) 23. In this survey, only two contracting authorities did not divide contracts into lots, Consip divided 40 per cent of its framework contracts into lots. Contracting authorities involved in this survey include ABA (Belgium), BBG (Austria), Consip (Italy), Hansel (Finland), MINEFI (France), GSA (Ireland), OGC (UK), PPD (Cyprus), SKI (Denmark), Statskontoret (Sweden), UMIC (Portugal).

as publishing tenders on a specific platform.[572] While this is not a legislative purpose of the contract division, it is a practical reason behind the lot division observed in practice.[573] Due to this concern, Article 9 Directive 2004/18/EU stipulated that when a proposed contract is awarded in separate lots, the Directive shall apply to each lot if the aggregate value of all lots exceeds the threshold.[574] This rule is reiterated in Article 5 Directive 2014/24/EU, which mandates the application of this Directive to contracts being awarded in the form of separate lots, as long as the total estimated value of lots exceeds or equals the EU threshold.[575] Under this rule, the practice of dividing contracts into lots to evade the obligations under Directive 2014/24/EU will be unsuccessful. Such obligations can include publishing contract notices on OJEU/TED.[576] In fact, this rule is beneficial for SMEs, as publishing contracts awarded in separate lots can lower the risk of SMEs not being able to access information about small lots of a large contract, which was discussed in Chapter 3, Section 3.2.1.[577]

To investigate the legislative purpose of including lot division in public procurement rules in the EU, it is important to trace the historical development of this concept and examine its coherence with the principles of EU public procurement rules. The development of SME-friendly considerations within the regulatory framework of EU public procurement can be classified into three main periods. The first period is signified by two key Communications issued by the European Commission (the

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[572] See Decio Coviello, Andrea Guglielmo, Clarissa Lotti and Giancarlo Spagnolo, 'Procurement with Manipulation' (Centre for Economic Policy Research, Discussion Paper DP17063, February 2022) <http://dx.doi.org/10.2139/ssrn.4118235> accessed 10 July 2024, 2.

[573] ibid 6.

[574] Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts [2004] OJ L134/1, art 9.

[575] Directive 2014/24/EU, art 5.

[576] Directive 2014/24/EU, art 51.

[577] See Chapter 3, Section 3.2.1.

Commission) in 1990 and 1992.[578] The second period started around 2008, with the publication of 'Think Small First – A Small Business Act for Europe' and the 'European Code of Best Practices Facilitating Access by SMEs to Public Procurement Contracts' (hereinafter referred to as the Code of Best Practices).[579] The third period commenced with the adoption of Directive 2014/24/EU and continues to the present day.

4.2.1 The Commission communications in the early 1990s

In the EU, SMEs have consistently been recognised as vital contributors to the economy and society at the highest level of politics.[580] Article 173 (1) Treaty on the Functioning of the European Union (TFEU) mandates that the EU and its Member States take action to 'encourage an environment favourable to the initiative and to the development of undertakings throughout the Union, particularly small and medium-sized undertakings' to maintain the competitiveness of the Union's industry.[581] Two key points emerge from Article 173 (1) TFEU that are pertinent to this analysis. Firstly, both the Union and the Member States must promote the competitiveness of the Union's industry by providing favourable conditions to undertakings operating throughout the Union. Secondly, particular consideration shall be given to SMEs among these undertakings. Article 173 TFEU provides the basis for the EU to regulate facilitating measures for SMEs in public procurement across the Union.

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[578] See COM (90) 166 final; European Commission, 'SME Participation in Procurement in the Community' (Communication) SEC (92) 722 final.
[579] European Commission, '"Think Small First" - A "Small Business Act" for Europe' (Communication) COM (2008) 394 final; SEC (2008) 2193 final.
[580] COM (2008) 394 final, 3.
[581] TFEU, art 173(1).

The EU has sought to dismantle barriers to SME involvement in public procurement, especially since it pursued the establishment of the Single Market in 1992.[582] To build a Community-wide procurement market, improving SMEs' access to public procurement contracts was also regarded as a way to adjust 'regional preference' in some Member States.[583] Recognising the significance of SME engagement, the Commission issued Communications in 1990 and 1992, underscoring the necessity of improving SME access to procurement opportunities in the community-wide market.[584] Although public procurement legislation has been designed to ensure that all businesses have access to public procurement on an equal footing, it is suggested by the 1990 Communication that 'positive measures' to promote SME participation bring more benefits in mobilising new resources, increasing competition and stimulating entrepreneurship.[585] Four criteria were proposed to identify the 'positive measures' that would offer the best prospect without imposing unacceptable costs.[586] Firstly, it underlined that the measure should not create SMEs' dependency on public contracts and should not create incompatibilities with open procurement within the Community.[587] Secondly, it emphasised that the measure should improve the competitiveness of SMEs without discriminating against large businesses.[588] Further, the criteria stressed that the measures should not lead to higher costs of goods and services and a disproportionate increase in administrative costs.[589] Evaluated against these criteria, dividing contracts into lots was recommended to Member States and

[582] European Commission, 'Completing the Internal Market' (Communication) COM (85) 310 final, 34.
[583] COM (89) 402 final, 12; also see COM (89) 400 final, para 87.
[584] COM (90) 166 final; SEC (92) 722 final.
[585] COM (90) 166 final, 2.
[586] ibid, 3.
[587] COM (90) 166 final, 3.
[588] ibid, 3.
[589] COM (90) 166 final, 3

contracting authorities to provide SMEs with access to more manageable contract opportunities.[590]

4.2.2 The 2008 European Code of Best Practices

In 2005, the Commission introduced the Lisbon Growth and Jobs Strategy (the Strategy), aimed at modernising SME policies to promote their growth and employment.[591] One of the five key areas identified to support SMEs is to improve their access to markets, with particular emphasis on facilitating SMEs' access to public procurement.[592] Notably, the Strategy highlighted that SMEs do not fully benefit from the Internal Market due to a lack of information on business opportunities across borders.[593] The Strategy also emphasised the importance of encouraging SMEs to engage in international markets, noting that such participation often strengthens their competitive position and contributes to growth and productivity.[594] From this perspective, it is evident that the Commission's goal in promoting SMEs extends beyond local markets, urging them to become more active within the Internal Market and beyond. By breaking down large contracts into smaller, more accessible lots,

[590] COM (90) 166, 4. The Commission commented in the 1990 Communication that measures discriminating in favour of SMEs, such as reserved contracts or price preferences, distort competition and underlined that these measures are not compatible with the Community law. For a comparison of different measures, see Chapter 8.

[591] European Commission, 'Implementing the Community Lisbon Programme - Modern SME policy for growth and employment' (communication) COM (2005)551 final, 6. Five areas were identified to be the main solutions to support SMEs: (1) promoting entrepreneurship and skills, (2) improving SMEs access to markets, (3) cutting red tape, (4) improving SMEs growth potential, (5) strengthening dialogue and consultation with SME stakeholders. Improving SMEs' access to markets especially calls for the attention of public authorities to facilitate SMEs' access to public procurement.

[592] ibid, 6.

[593] COM (2005) 551 final, 6.

[594] ibid, 6.

SMEs are better positioned to bid for contracts across Member States, particularly in markets historically characterised by larger contracts.[595]

The Commission's commitment to supporting SMEs was further reinforced with the introduction of the 'Think Small First' principle in 2008, advocating policies attuned to SME needs, including their participation in public procurement.[596] Following this, the Code of Best Practices reiterated the importance of dividing contracts into lots to mitigate barriers stemming from contract size.[597] However, the Code of Best Practice pointed out that contracting authorities should not use their discretion in a way that impairs the conditions for fair competition when they are dividing a contract into lots.[598] This concern is particularly relevant when a contracting authority limits the number of lots a single tender can bid for or be awarded, which will be discussed in Section 4.3.3 below. The Code of Best Practice also recognised the benefits of allowing tenderers to bid for an unlimited number of lots, ensuring that large businesses are not discouraged from participating.[599] Section 4.3 will explore the different approaches to lot division in greater detail, examining how various designs may impact SME participation. While the Code of Best Practice offers valuable guidance on the use of lot division, it remains soft law, not being legally binding on Member States.[600] Consequently, Member States were not required to incorporate contract division into their public procurement law, leading to varying levels of adoption across the EU.

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[595] SEC (2008) 2193 final, 7.
[596] COM (2008) 394 final, 2.
[597] SEC (2008) 2193 final, 7.
[598] ibid.
[599] SEC (2008) 2193 final, 7.
[600] Soft law refers to rules that are not legally binding but might have influence on Member States, such as recommendations and communications. For a discussion on soft law, see Senden (n 137) 111.

4.2.3 Directive 2014/24/EU - the shift from soft law to a hard law approach

Directive 2004/18/EC did not include any specific measures to facilitate SMEs' access to public procurement, except Recital 32, which encouraged contracting authorities to consider subcontracting as a means of opening opportunities to SMEs.[601] Moreover, Article 9 (5)(a) Directive 2004/18/EC allowed contracts to be awarded in separate lots but required that the total estimated value of all lots be aggregated for the purpose of determining whether the EU thresholds applied.[602] Where the combined value exceeded the threshold, the Directive applies to each lot, unless the estimated value of an individual lot was below EUR 80,000 for supplies and services or EUR 1 million for works, and provided that such a lot did not exceed 20 per cent of the aggregate value of the whole contract.[603] Directive 2004/18/EC did not explicitly encourage the use of lot division to enhance SME participation, likely due to concerns that the practice could be used to circumvent the thresholds.[604] Directive 2014/24/EU retains this aggregation rule in Article 5, which sets out the methods for calculating the estimated value of procurement and requires that the value of all lots be taken into account when determining whether EU thresholds are met.[605]

Compared with Directive 2004/18/EC, Directive 2014/24/EU for the first time incorporated provisions on lot division at the hard law level and explicitly articulated its

[601] See Directive 2004/18/EC, recital 32.
[602] See Directive 2004/18/EC, art 9(5).
[603] ibid.
[604] Trybus has argued that Article 9 (5) Directive 2004/18/EC appeared to 'tolerate and perhaps timidly encourage' lot division. See Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 325.
[605] Directive 2014/24/EU, art 5.

intended objective: to facilitate SMEs' access to public procurement and increase their participation.[606] By recognising the role of lot division in fostering SME participation, Directive 2014/24/EU frames it as serving a dual purpose: opening market access opportunities for SMEs and enhancing competition in the public procurement market.[607] Recital 78 makes this explicit, stating that '[t]o that end and to enhance competition, contracting authorities should in particular be encouraged to divide large contracts into lots.'[608] Recital 124 adds that these provisions (SME-friendly measures) should contribute towards a higher share of SMEs in the total value of contracts awarded, but cautions that 'it is not appropriate to impose obligatory shares of success'.[609] While the Directive has stated objectives of lot division clearly, the extent to which this measure genuinely advanced SME participation remains to be tested. The remainder of this chapter evaluates whether lot division has effectively increased SME participation in public procurement in the Internal Market. Given that the design and implementation of the measure vary across Member States, the analysis will also examine these differences to assess which approaches best achieve the intended goals of the measure.

[606] Directive 2014/24/EU, recital 78.

[607] ibid.

[608] Directive 2014/24/EU, recital 78.

[609] Directive 2014/24/EU, recital 124. This contrasts with the approach adopted by the US government in federal procurement, which will be discussed in Chapter 7.

4.3 The Division into Lots under Article 46 Directive 2014/24/EU and its Transposition in France and Germany

Article 46 Directive 2014/24/EU sets out rules on lot division in four paragraphs, establishing a default 'divide or explain' approach.[610] Member States are afforded the option to render lot division obligatory under specified conditions, provided that such provisions comply with both national law and EU law.[611] The primary distinction between the mandatory approach and default approaches lies in the degree of obligation imposed on contracting authorities to justify their decisions regarding lot division. Under the default 'divide or explain' regime, contracting authorities retain greater discretion in determining whether or not to divide contracts and are required merely to present reasons for their choice, such as potential additional financial costs or technical complications, rather than to fully justify their decisions.[612] The United Kingdom (UK), Ireland, Austria, and several other Member States have adopted this default approach.[613] In contrast, in countries where the mandatory approach has been implemented, the division of contracts into lots is upheld as a guiding principle, and contracting authorities are required to justify their decisions within a more restrictive legal framework.[614]

The divergence in approaches reflects varying legislative purposes across Member States, with potential consequences for the effectiveness of lot division in enhancing

[610] Directive 2014/14/EU, art 46.
[611] Directive 2014/14/EU, art 46 (4).
[612] Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 330.
[613] ibid 328.
[614] For instance, an increase in the contracting authority's economic costs may not suffice to justify a decision against contract division. This issue will be examined in detail in Section 4.3.1.

SME participation. Additionally, beyond the choice of approach, other elements in the design of lot division may also influence SME bidding behaviour. These include the extent to which bidders are permitted to bid for and be awarded multiple lots, as well as the possibility for bidders to submit alternative tenders based on the number of lots they might be awarded. This section examines these aspects in depth and assesses their potential impact on SME participation. Given that Germany and France have been at the forefront of implementing lot division in public procurement, this chapter will scrutinise their legal frameworks and practices to illustrate the varying designs of lot division.[615]

4.3.1 The scope of explanation for not dividing a contract

Article 46(1) Directive 2014/24/EU establishes the default 'divide or explain' approach, whereby contracting authorities have an obligation to provide reasons for their decision not to divide a contract in the procurement documents.[616] According to Article 2 Directive 2014/24/EU, 'procurement documents' encompass any documents 'produced or referred to by the contracting authority to describe or determine elements of the procurement or the procedure', including contract notices, technical specifications, descriptive documents, and proposed contract conditions.[617] While the obligation to provide reasons for not dividing a contract exists, Article 46 is not stringent regarding where these reasons must be presented within the procurement documents.

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[615] SEC (92) 722 final, 8, para 26.

[616] Directive 2014/24/EU, art 46(1). According to Article 2 Directive 2014/24/EU, 'Procurement documents' refer to documents 'produced or referred to by the contracting authority to describe or determine elements of the procurement or the procedure', including contract notices, the technical specifications, the descriptive document, proposed conditions of contract.

[617] Directive 2014/24/EU, art 2(13).

As a result, bidders may face difficulties in challenging the contracting authority's decision not to divide a contract.[618]

Moreover, the obligation to provide reasons can be easily satisfied as Article 46 does not specify the scope or nature of the explanations that contracting authorities must provide.[619] Nevertheless, any reasoning put forward must comply with the provisions of Directive 2014/24/EU and the principles of EU law.[620] For example, it would not be permissible for a contracting authority to award a contract in its entirety solely because it benefits large domestic businesses, as this would contravene the principle of non-discrimination.[621] Recital 78 offers some potential reasons that contracting authorities might consider, such as concerns about restricting competition, incurring additional financial costs, or facing technical challenges in coordinating different contractors.[622] Overall, Directive 2014/24/EU does not provide detailed guidance on this matter, thereby granting Member States and contracting authorities substantial discretion. Thus, in the 'divide or explain' approach, it is not challenging for contracting authorities to fulfil the obligation to explain the principal reasons for not dividing a contract.[623]

As for whether the decision not to divide a contract is judicially reviewable or not, Article 46 remained silent, and Recital 78 is permissive, simply stating that the decision to divide a contract shall be made autonomously by the contracting authority, without

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[618] Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 342.

[619] ibid at 330 citing Sánchez Graells, Public Procurement and the EU Competition Rules (n 62) 347; Directive 2014/24/EU, art 46(1).

[620] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 470, para 6-119.

[621] Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 331.

[622] Directive 2014/24/EU, recital 78.

[623] Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement' (n 64) 331.

being subject to administrative or judicial supervision.[624] Although recitals are not legally binding, this creates ambiguity regarding bidders' rights to contest a contracting authority's decision not to divide a contract. Nevertheless, the question of judicial review must be addressed within the framework of the Public Sector Remedies Directive 665/89/EEC and the jurisprudence of the Court of Justice of the European Union (CJEU).[625] There is no indication in these sources that decisions on lot division are immune from judicial review.[626] Moreover, the principle of effective judicial protection, as enshrined in Article 47 of the EU Charter of Fundamental Rights and Article 19 (1) of the Treaty of the European Union (TEU), guarantees access to judicial protection in matters governed by EU law.[627] Therefore, contracting authorities' decisions on lot division are subject to judicial review, as are other decisions made by contracting authorities. In the Member States that have adopted the default approach, while decisions concerning lot division can indeed be legally contested, contracting authorities retain broad discretion, provided they comply with national and EU law. This discretion allows them to rationalise their decisions not to divide contracts easily. Conversely, in Member States where contract division is mandated, the discretion of contracting authorities is more restricted, particularly when legislation prescribes a limited set of permissible justifications for not dividing contracts, as exemplified by the French approach, which is discussed below.

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[624] ibid 332.

[625] Trybus 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 332.

[626] ibid.

[627] Roberto Caranta, 'The Changes to the Public Contract Directives and the Story They Tell about How EU Law Works' (2015) 52 Common Market Law Review 391, 428.

4.3.1.1 The 'divide or justify' approach in France

In France, since 2006, the division of contracts into separate lots has been a fundamental principle of public procurement law, as outlined in Article 10 of the old procurement code *Code des Marchés Publics* (Public Procurement Code, hereinafter referred to as CMP 2006).[628] Contracting authorities are required to divide contracts into lots to promote the broadest possible competition unless the nature of the contract does not allow for the identification of distinct components.[629] Consequently, if a contract's subject matter does not have distinct components, contracting authorities may be exempted from the obligation to divide it into lots.[630] The subject matter of a contract is determined by the contracting authority based on the product, service or work they intend to procure.[631] Even if the subject matter of a contract consists of distinct parts, contracting authorities may refrain from dividing it into lots if they can justify their decision under one of the four stipulated exceptions: the division would either restrict competition, increase the technical difficulty of contract performance, result in additional financial costs or if the contracting authority lacks the capacity to manage and coordinate separate lots.[632] These four exceptions provide contracting

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[628] *Code des marchés publics (édition 2006) (version en vigueur du 1 septembre 2006 au 1 avril 2016) abrogé par ordonnance n° 2015-899 du 23 juillet 2015, art 102*. Hereinafter referred to as CMP 2006.

[629] ibid.

[630] See Directive 2014/24/EU, art 29. contracting authorities identify the subject-matter of the procurement by providing a description of their needs and the characteristics required of the supplies, works or services to be procured.

[631] COM (2001) 566 final, 3. Contracting authorities define the subject matter of a contract by defining what product, service or work they intend to procure. See Marc Martens and Stanislas de Margerie, 'The Link to the Subject-Matter of the Contract in Green and Social Procurement' (2013) 8 European Procurement & Public Private Partnership Law Review 8, 11.

[632] CMP 2006, art 10. It was clearly stated that a contracting authority may award an entire contract, with or without identifying separate components, if it considers the division is likely to restrict competition, or that it is likely to make the performance of the services technically difficult or financially costly, or that it is not in a position to carry out the organisational, steering and coordination tasks itself. This provision was in force from 1 September 2006 to 1 April 2016.

authorities with considerable flexibility. As long as one of these justifications is demonstrated, there is no obligation to divide the contract into lots.

Notably, when Directive 2014/24/EU was transposed into Ordinance No. 2015-899 of July 23, 2015 (hereinafter Ordinance 2015), all the exceptions established under CMP 2006 were retained.[633] Additionally, Ordinance 2015 exempted defence and security contracts from the obligation to divide contracts into lots.[634] This aligns with the findings of empirical research conducted by Trybus and Heuninckx, which highlighted that defence contracts are typically awarded in their entirety to large suppliers, with SMEs often participating (only) as subcontractors.[635] Interestingly, in the public procurement code, *Code de la commande publique* (hereinafter CCP 2019), currently in force, the exemption for defence and security contracts is removed.[636]

Article L2113-11 of CCP 2019 reiterates the four exceptions initially laid down in CMP 2006. Moreover, in 2023, Law No. 2023-973 of October 23, 2023, Article 26 introduced a new exception to lot division: the risk of an unsuccessful procedure.[637] Compared to demonstrating increased financial costs or a lack of coordination capacity, proving that the division of a contract might result in an unsuccessful procedure offers greater flexibility, as this risk can be interpreted in various ways. Moreover, Article L2113-11(3)

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[633] O*rdonnance n° 2015-899 du 23 juillet 2015 relative aux marchés publics, art 32*. Compared with CMP 2006, defence or security contracts are excluded from the scope of contract division. This version was in force from 11 December 2016 to 1 April 2019, and replaced by *Code de la Commande Publique (en vigueur depuis le 1 avril 2019)*. See *Code de la Commande Publique (*en vigueur depuis le 1 avril 2019*), art* L.2313-5.

[634] Article 32 of Ordinance No. 2015-899 stipulated that public contracts other than public defence or security contracts shall be awarded in separate lots, unless their subject matter does not allow separate components to be identified.

[635] Trybus and Heuninckx (n 551) 123.

[636] *Code de la Commande Publique 2019,* art L2113-11.

[637] ibid.

does not specify what constitutes an unsuccessful procedure.[638] It requires only the demonstration of a 'risk' of an unsuccessful procedure, a lower threshold than proving additional costs or technical difficulties.[639] This aligns with the suggestions of Recital 78 Directive 2014/24/EU, which notes that 'the need to coordinate the different contractors for the lots could seriously risk undermining the proper execution of the contract'.[640] This could mean, for instance, that certain lots may fail to attract any bids, perhaps because they are too small to be commercially profitable, thereby preventing the contract from being fully awarded if divided in this manner. Regardless of how 'unsuccessful procedure' is interpreted, it represents yet another step away from the principle of mandatory lot division in France. This demonstrates that French legislators are not determined to strictly enforce mandatory lot division but rather are offering contracting authorities greater flexibility to circumvent this obligation. Consequently, although contract division is ostensibly mandatory in France, it closely resembles the default 'divide or explain' approach. Given the explicit legal scope for justifications, the French system might be more appropriately described as a 'divide or justify' approach.

4.3.1.2 The mandatory approach to lot division in Germany

In Germany, public procurement rules are primarily governed by Part 4 of the Act Against Restrictions of Competition (*Gesetz gegen Wettbewerbsbeschränkungen*, hereinafter GWB).[641] When public procurement rules were first incorporated into the

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[638] *Code de la Commande Publique* 2019 (CCP 2019), art L2113-11.

[639] ibid.

[640] Directive 2014/24/EU, recital 78.

[641] Being regarded as part of competition law, public procurement law falls within the sphere of competing competence (*konkurrierende Gesetzgebung*). Accordingly, both the Federation and the *Länder* may legislate, pursuant to Article 72 of the *Grundgesetz* (Basic Law, GG). See *Grundgesetz für*

GWB in 1999, §106(3) GWB stipulated that 'the interests of SMEs are to be considered appropriately, particularly through the division of contracts into specialised and partial lots'.[642] This provision clearly emphasised the significance of lot division for supporting SMEs, but did not impose a mandatory obligation on contracting authorities to divide contracts into lots.[643] Unlike CMP 2006 in France, promoting competition was not set out as an objective of the division into lots; rather, GWB (1999) §106(3) focused purely on SMEs.[644]

In 2009, §97(3) GWB was expanded to a more similar structure to the current law.[645] The wording was changed to impose an obligation on contracting authorities to divide contracts, compared with the 1999 GWB.[646] This provision remained essentially unchanged when Directive 2014/24/EU was transposed into the GWB 2016.[647] §97 (4) GWB 2016 mandates that the interests of SMEs shall primarily be considered in public

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die Bundesrepublik Deutschland (GG), art 72. For a systematic introduction to the legal framework of public procurement in Germany, see OECD, 'Enhancing the Legal Framework and Governance Structure for Public Procurement in Germany' in OECD, *Public Procurement in Germany* (OECD 2019) <https://www.oecd-ilibrary.org/governance/public-procurement-in-germany_154604df-en> accessed 10 October 2023.

[642] See *Gesetz gegen Wettbewerbsbeschränkungen* (GWB), as amended by *Vergaberechtsänderungsgesetz* of 26 August 1998, BGBl I 2512, in force 1 January 1999, § 97(3). Hereinafter referred to as GWB 1999.

[643] GWB 1999, § 106(3).

[644] ibid.

[645] The Federal Council (*Bundesrat*) proposed that public procurement law should be modernised to suit the needs of SMEs, along with the task to transpose Directive 2004/17/EC, Directive 2004/18/EC and Directive 2007/66/EC. The concern was raised that, although Section 97 (3) in GWB 1999 requires the contracting authority to consider the interests of SMEs, mainly through dividing contracts into lots, SMEs are discouraged by contracting authorities' practice of lot bundling, which will be discussed in Section 4.3.4. Given that SMEs make up for most businesses in the national economy, it is reasonable to compensate their disadvantages when awarding large contracts. Thus, it was proposed that Section 97 (3) needed to be strengthened by impose a mandatory division into lots regime. For more information, see *Bundesrat, Gesetzentwurf der Bundesregierung, Drucksache 349/08* (23 May 2008) <https://dserver.bundestag.de/brd/2008/0349-08.pdf> accessed 18 March 2024.

[646] GWB as amended by *Gesetz zur Modernisierung des Vergaberechts* of 20 April 2009, BGBl I 790, § 106(3). Hereinafter referred to as GWB 2009.

[647] GWB (2009) § 106(3).

procurement procedures.[648] Contracts shall be divided into individual lots (partial lots) and awarded separately according to the type or area of specialisation (trade-specific lots).[649] Unlike Article 46 Directive 2014/24/EU, §97(4) GWB 2016 and subsequent §97(4) GWB 2023 do not include an 'or explain' requirement for contracting authorities.[650] This absence, however, does not signal a lenient approach that contracting authorities do not need to justify their decision not to divide a contract. Rather, lot division is established as a fundamental principle in public procurement law in Germany, requiring contracting authorities to divide contracts into lots unless there are objectively compelling reasons to justify an overall award.[651] Although §97(4) GWB does not explicitly outline these compelling reasons, it specifies that several lots can be awarded together if technical or financial reasons require this.[652] Thus, awarding an entire contract without dividing it into lots also requires compelling technical or financial reasons.[653]

Over time, German courts have provided further clarification on what constitutes a compelling reason. In 2004, the Higher Regional Court of Düsseldorf (*Oberlandesgericht Düsseldorf*, hereinafter *OLG Düsseldorf*)[654] ruled that a mere

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[648] GWB, as amended by *Vergaberechtsmodernisierungsgesetz* of 17 February 2016, BGBl I 203, § 97(4). Hereinafter referred to as GWB 2016. The GWB was amended in 2023 but the division into lots regime remained unchanged compared with GWB 2016. See Gesetz gegen Wettbewerbsbeschränkungen (GWB, as amended up to BGBl I 2023, 294), § 97.

[649] GWB 2016 § 97(4).

[650] ibid.

[651] Martin Burgi, Meinrad Dreher, and Marc Opitz, *Beck'scher Vergaberechtskommentar* (4th edn, Beck 2022), para 51.

[652] Awarding several lots collectively is also termed 'combined lots' in Article 46 Directive 2014/24/EU.

[653] Burgi, Dreher and Opitz (n 651), para 51.

[654] The *OLG Düsseldorf* (Higher Regional Court of Düsseldorf) has jurisdiction over proceedings against federal contracting authorities. The judgements can offer some insights to interpret the law. However, it is noteworthy that judgments from *OLG Düsseldorf* are not binding for cases in the future or cases in the lower courts, the judgements can only provide an interpretation of the law, rather than revising or adding elements to the law.

prospect of obtaining better prices by awarding a contract in its entirety does not constitute sufficient justification for not dividing a contract.[655] For economic reasons to be valid, the lot division must result in a disproportionately high increase in overall costs or cause significant delays to the project as a whole.[656] In a more recent case, the *OLG Düsseldorf* reaffirmed that additional economic costs could not justify a decision not to divide a contract unless those costs are disproportionately high.[657] Although there is no legal definition of 'disproportionate', this reasoning helps exclude instances where cost increases are relatively minor. For example, in case *Verg 40/21*, the contracting authority argued that dividing contracts into lots would incur additional costs of EUR 94,000.[658] However, the OLG Düsseldorf ruled that this amount was not a disproportionate increase given the contract's expected value of EUR 35 million.[659]

For technical reasons, contracting authorities may justify their decision not to divide a contract, such as ensuring the compatibility of an IT system.[660] However, this justification is not universally applicable. In case *Verg 38/13*, the *OLG Düsseldorf* held that technical reasons should be directly related to the contract itself.[661] If, for instance, a software system plays only an auxiliary role in the contract, its compatibility is insufficient grounds for awarding the contract as a whole.[662] Technical reasons are more compelling when the individual lots do not align cohesively, even if each lot conforms to the technical specifications. In case *Verg 43/09*, the *OLG Düsseldorf* ruled

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[655] *OLG Düsseldorf, 8 September 2004, VII-Verg 38/04.*
[656] *OLG Düsseldorf, 11 July 2007, VII-Verg 10/07, para 36.*
[657] *OLG Düsseldorf, 30 September 2022, Verg 40/21.*
[658] ibid.
[659] *OLG Düsseldorf, 30 September 2022, Verg 40/21.*
[660] *OLG Düsseldorf*, 30 November 2009, VII-Verg 43/09.
[661] ibid.
[662] *OLG Düsseldorf*, 25 June 2014, VII-Verg 38/13, para 61-63.

that the uniformity of telecommunications systems across multiple schools justified awarding the contract in its entirety.[663] Such consistency is expected to facilitate familiarity with the telecommunications system for both students and teachers, particularly in the event of personnel transitions in schools.[664] The court upheld the contracting authority's decision, asserting that the public interest in system consistency outweighed the interests of SMEs in this case.[665]

In summary, lot division is a general principle of public procurement in Germany, and while the law does not explicitly enumerate justifications for not dividing a contract, contracting authorities' decisions are subject to judicial review. The *OLG Düsseldorf* has clarified that factors such as higher costs or coordination difficulties do not suffice as justifications, though disproportionate cost increases or significant delays may. Technical reasons, such as the coherence of an IT system, are likely to be accepted as valid grounds for not dividing a contract.[666]

In contrast, the French approach clearly defines the scope of justifications for not dividing contracts, whereas German legislators leave it to the courts to decide.[667] While French legislators have increasingly expanded the discretion of contracting authorities in this area, such a trend is not evident in Germany. The choices made by legislators significantly influence how contracting authorities approach lot division. When the scope of justifications for not dividing a contract is broad, contracting authorities may be less inclined to divide contracts, as they lack sufficient incentives

[663] *OLG Düsseldorf*, 30 November 2009, VII-Verg 43/09, para 9.
[664] ibid.
[665] *OLG Düsseldorf*, 30 November 2009, VII-Verg 43/09, para 9.
[666] Burgi, Dreher and Opitz (n 651), para 51.
[667] For the French approach, see Section 4.3.1.1.

to do so. This, as will be discussed in Section 4.4, can hinder the achievement of the intended purpose behind lot division.

4.3.2 The methods for dividing contracts into lots

Contracting authorities have significant discretion in determining the size and subject matter of lots.[668] The subject matter of lots refers to the specific works, supplies, or services to be provided under each lot.[669] While contracting authorities are mandated to specify the size and the subject matter of lots in contract notices, they are not required to justify their choices.[670] The method for dividing a contract involves identifying how to segment the procurement needs into manageable lots. According to Recital 78 Directive 2014/24/EU, contracts can be divided based on quantitative, qualitative or time-phased criteria.[671] Quantitative criteria are typically applied when the contract's subject matter can be divided into measurable units. For instance, a procurement procedure involves 400 sets of desks and chairs for public schools; the contract might be divided into four lots, each containing 100 sets. This approach can also be applied to service contracts, such as dividing a cleaning service for two office buildings into two separate contracts, each covering one building. In the context of works contracts, the construction of a ten-kilometre bridge could be divided into ten lots, with each lot encompassing one kilometre of construction work. Qualitative

[668] Directive 2014/24/EU, art 67.
[669] Subject matter of the public contract refers to the works, supplies or services to be provided under the contract. See Directive 2014/24/EU, art 67 (3).
[670] Directive 2014/24/EU, art 46. See Michael Steinicke, 'Article 46, Division of Contracts into Lots' in Michael Steinicke and Peter L Vesterdorf (eds), *Brussels Commentary on EU Public Procurement Law* (Bloomsbury Publishing 2019) 594.
[671] Directive 2014/24/EU, recital 78.

criteria are typically employed when the subject matter of the contract involves different trades and specialisations.[672] For instance, in a construction project, the contracting authority may divide the contract into lots such as design, groundwork, electrical work, etc. This division enables different specialist contractors, especially SMEs, to compete for specific project parts. Another criterion for dividing contracts is to divide a contract that spans an extended period into multiple lots with shorter time phases.[673] For example, a contracting authority can divide a five-year IT maintenance service contract into three lots, one three-year and two one-year lots. Contracts with shorter duration are more manageable for SMEs compared with long-duration contracts.[674]

In France, Article 10 CMP 2006 provided contracting authorities with discretion to decide the number and size of lots, taking the technical characteristics of the procurement needs and the structure of the economic sector into account.[675] In the new public procurement code, CCP 2019, this guidance has been removed.[676] The current legislation simply mandates that contracting authorities must specify the number, size, and scope of the lots.[677] Akin to the expansion of the scope of justifications for not dividing a contract, contracting authorities have more discretion in determining the size and subject matter of lots compared with the past. In Germany, there are no specific restrictions on the method for dividing contracts. §97(4) GWB stipulates that contracts shall be divided into partial lots by quantity or into trade-

[672] Directive 2014/24/EU, recital 78.
[673] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 463, para 6-109.
[674] See Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64), at 323 citing Saussier (n 404).
[675] CMP 2006, art 10.
[676] CPP 2019.
[677] ibid.

specific lots by type and speciality.[678] These methods align with quantitative and qualitative criteria outlined in Recital 78 Directive 2014/24/EU. Overall, contracting authorities possess the most comprehensive understanding of their procurement needs, making it preferable for them to have discretion in selecting the method for dividing contracts and the number and size of lots.[679]

4.3.3 Lot limitation in tenders and awards

Following the determination of the number and subject matter of lots, contracting authorities shall decide whether to restrict the number of lots for which tenderers may bid or be awarded. Article 46(2) expressly permits tenders to be submitted for one, several or all lots (‘bid limit), provided that this option is clearly indicated in the contract notice or the invitation to confirm interest.[680] When allowing bids containing multiple lots, contracting authorities have the option to limit the maximum number of lots that can be awarded to a single tenderer (‘award limit).[681] Recital 78 suggests that contracting authorities should be allowed to limit the maximum number of lots that one bidder can tender to preserve competition or ensure supply reliability.[682] Arrowsmith contends that decisions to restrict the number of lots a tenderer can bid for or be awarded are explicitly permitted under Directive 2014/24/EU, and these decisions are ‘excluded buying decisions’, which do not require justifications under the TFEU as they

[678] GWB 2023 § 97(4).
[679] Sanchez-Graells, *Public Procurement and the EU Competition Rules* (n 62) 350.
[680] Directive 2014/24/EU, art 46 (2).
[681] ibid.
[682] Directive 2014/24/EU, recital 78.

do not hinder economic operators' access to the Internal Market.[683] This interpretation suggests considerable discretion for contracting authorities in designing lot limitation strategies.

However, both Herrera Anchustegui et al. and Sanchez-Graells contend that bid and award limits must not undermine conditions for fair competition.[684] Sanchez-Graells observes that the consideration of fair competition may be the only significant restriction upon contracting authorities when they impose a relatively low maximum number of lots that tenderers can bid for or be awarded.[685] This concern is also reflected in the Code of Best Practice published by the Commission, which suggests that permitting tenderers to bid for an unlimited number of lots offers an advantage by not discouraging large contractors from participating.[686] However, this suggestion fails to acknowledge the risk that large economic operators may effectively reconstitute divided contracts, utilising economies of scale to offer competitive pricing across multiple lots. While such an approach may deliver value for money, it fundamentally undermines the SME participation objectives that originally motivated the division into lots.

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[683] Excluded buying decisions refer to decisions that do not hinder access to the Internal Market but rather define the scope of that market. See Sue Arrowsmith, *The Law of Public and Utilities Procurement* vol 2 (3rd edn, Sweet & Maxwell, 2018) 738, para 20-59; Arrowsmith, *The Law of Public and Utilities Procurement,* vol 1 (n 57) para 4-25 - 4-30.

[684] Ignacio Herrera Anchustegui, Lisa Margrethe Nes, and Tor Sikkeland, 'Article 46 Division of Contracts into Lots' in Caranta and Sanchez-Graells (eds) (n 383) 502, para 46-15; Sanchez-Graells, *Public Procurement and the EU Competition Rules* (n 62) 350.

[685] ibid, Sanchez-Graells, *Public Procurement and the EU Competition Rules* (n 62) at 350 citing SEC (2008) 2193) final, 6-7.

[686] If contracts are divided into smaller lots and bidders are limited to bidding for and being awarded only one lot, large businesses may lose interest, as they are unable to leverage their economies of scale.

Nevertheless, bid and award limits should be considered within the primary objective of EU public procurement directives, which is to eliminate the trade barriers among Member States and promote the Internal Market.[687] From this perspective, bid or award limits should not hinder economic operators from other Member States from participating in a procurement procedure. The justification for regulating bid or award limits is not whether such limitations affect participation from large businesses, but whether they constitute a barrier to cross-border trade.[688] Consequently, if bidders are only allowed to bid for one lot with a low value, this might *de facto* discourage economic operators from other Member States, due to the limited profitability of an individual small lot. In that scenario, such limits might constitute measures having equivalent effect to quantitative restrictions (MEEQR) under Article 34 TFEU, where only local or domestic economic operators find those individual lots commercially attractive.[689] The rationale of supporting SMEs will prove insufficient to justify such MEEQRs under Article 36 TFEU.[690] However, it may be argued that supporting SMEs could be a 'mandatory requirement' introduced by *Cassis de Dijon,* as Article 173(1) TFEU acknowledges support for SME development as a legitimate objective within the EU.[691] The critical question, therefore, becomes whether the bid limit is a proportionate measure for achieving this objective of supporting SMEs. However, a less restrictive

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[687] Sue Arrowsmith, 'The Purpose of the EU Procurement Directives: Ends, Means and the Implications for National Regulatory Space for Commercial and Horizontal Procurement Policies' (2012) 14 Cambridge Yearbook of European Legal Studies 1.

[688] Arrowsmith expressed a similar view, that the size of the lots should not be so small that competition across borders is curtailed. See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 470-471, para 6-119.

[689] TFEU, art 34; also see Case 8/74 *Procureur du Roi v Benoît and Gustave Dassonville* [1974] ECR 837.

[690] Article 36 TFEU provides an exhaustive list of justifications, including public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures, possessing artistic, historic or archaeological value; or the protection of industrial and commercial property. See TFEU, art 36.

[691] Case 120/78 *Rewe-Zentral AG v Bundesmonopolverwaltung für Branntwein* [1979] ECR 649.

measure would be available, where contracting authorities impose bid limits whilst ensuring that cross-border participation remains commercially viable.

In cases where a tenderer submits bids for more lots than the bid limit, the contracting authority retains discretion over which lots to evaluate.[692] Herrera Anchustegui et al. have identified three possible approaches in such situations. The first option is to reject the entire bid on the grounds of non-compliance.[693] However, this approach is not feasible if all lots are published as separate calls for tenders and the contracting authority evaluates each lot (contract) separately, termed lot-by-lot evaluation. The second option is to request clarification from the tenderer on which specific lots should be considered.[694] The third approach involves evaluating all the submitted lots and determining which ones may be awarded by the contracting authority.[695] The second approach is more appropriate as long as the procedure is transparent. The third option raises concerns regarding the principles of equal treatment and transparency.[696] If there is a bid limit of three lots, a bid containing five lots gains an unfair advantage, potentially increasing the likelihood of being awarded a contract. This practice contravenes the principles of equal treatment, as it incentivises bidders to ignore the bid cap and submit bids for as many lots as possible to enhance their chances of securing an award. To maintain transparency and ensure equal treatment, contracting authorities should specify in the contract notices the specific approach they will adopt when evaluating tenders that encompass more lots than the bid limit.

[692] Herrera Anchustegui, Margrethe Nes, and Sikkeland (n 684) 501.
[693] ibid.
[694] Herrera Anchustegui, Margrethe Nes, and Sikkeland (n 684) 501.
[695] ibid.
[696] Herrera Anchustegui, Margrethe Nes, and Sikkeland (n 684) 502.

When an award limit applies without a bid limit, there is a possible scenario that the 'best tenderer' under the award criterion would be awarded more lots than the award limit. In this scenario, Article 46 (2) requires contracting authorities to determine which lots to award using objective and non-discriminatory criteria.[697] However, neither Article 46 nor any other provision in Directive 2014/24/EU clearly defines what constitutes objective and non-discriminatory criteria.[698] Evaluation methods should be established first before determining which lots are awarded to the best tenderer. Tender evaluation may be conducted on a lot-by-lot basis or a tender-by-tender basis.[699] In a lot-by-lot evaluation, after identifying the most advantageous lots in the best tender, the remaining lots could be awarded to the second-best tenderer. While this approach seems to promote the integrity of the procedure, it may appear counterintuitive from an economic standpoint, as awarding lots to second-best bidders could result in less value for money. In that case, contracting authorities could conduct a proportionality test to determine whether the excess lots should be awarded to the second-best tenderer or retained by the best tenderer.[700] If there is a substantial difference between the two bids, awarding the excess lots to the best tenderer aligns with the contracting authority's interest, which is also implied in Recital 79.[701] If there

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[697] The 'best tenderer' here refers to the tenderer that submits the most economically advantaged tender or the best scored tender against any specific award criteria set by the contracting authority. See Directive 2014/24/EU, art 46 (2).

[698] Article 65 (2) Directive 2014/24/EU requires that contracting authorities indicate the objective and non-discriminatory criteria they intend to apply to reduce the number of qualified candidates to be invited to participate in restricted procedures or other procedures in which contracting authorities may limit the number of tenderers. See Directive 2014/24/EU, art 65 (2).

[699] If the tender evaluation is lot-by-lot based, it means the contracting authority evaluates each lot regardless how many lots are included in one tender. If the tender evaluation is tender-by-tender based, the contracting authority might not have clear information regarding which tenderer has the best offer for a single lot.

[700] See Herrera Anchustegui, Margrethe Nes, and Sikkeland (n 684) 504, para 46-20.

[701] Recital 79 Directive 2014/24/EU first states that contracting authorities shall be allowed to limit the number of lots that may be awarded to one tenderer, it also recognised the potential risk of an ineffective result if contracting authorities are obliged to award contracts lot by lot, whereas awarding several lots

is no substantial difference between the best and the second-best tenderers, contracting authorities can decide to award the excess lots to the second-best tenderers.[702] Nevertheless, Kotsonis cautions that the price difference between the best tenderer's offer and that of the second-best tenderer could potentially amount to state aid, as the competition's outcome does not reflect the most economically advantageous tender.[703] State aid may be involved if the price paid exceeds the market price, thereby granting a financial advantage to the contractor.[704] To mitigate such risks, the contracting authority could request that the second-best tenderer match the price offered by the best tenderer, ensuring no financial advantage is conferred.

If the evaluation is conducted on a tender-by-tender basis, especially when lots are bundled and cannot be easily separated, the contracting authority needs to assess whether awarding more lots than the maximum number provides greater advantages than reallocating some lots to another tenderer.[705] Moreover, if the difference between the best and the second-best tenders extends beyond price, such as differences in quality, contracting authorities can justify awarding more lots to the best tenderer as long as this decision satisfies the requirement of 'objective and non-discriminatory criteria'.[706]

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together or the whole contract is a more advantageous solution. It recommends contracting authorities conduct a comparative assessment to tenders that consists of lots or tenders that combines lots. See Directive 2014/24/EU, recital 79.

[702] Herrera Anchustegui, Margrethe Nes, and Sikkeland (n 684) 503.

[703] Totis Kotsonis, 'The 2014 Utilities Directive of the EU: codification, flexibilization and other misdemeanours' (2014) 4 Public Procurement Law Review 169, 183.

[704] Arrowsmith, *The Law of Public and Utilities Procurement* vol 2 (n 683) 749, para 20-71.

[705] It is possible that a tender comprises multiple lots that are not bundled, and the contracting authority can separate the lots and ascertain the price offered by the tenderer for each individual lot. Then the contracting authority can compare between the best and second-best tenders and make a decision. The next section will discuss lot bundling.

[706] Directive 2014/24/EU, art 46 (2).

In summary, Article 46 provides contracting authorities with discretion to limit the maximum number of lots that a tenderer may either bid for or be awarded. In both France and Germany, contracting authorities are permitted to impose such limits, with rules that are the same as those stipulated in Article 46 Directive 2014/24/EU.[707] Beyond encouraging SME participation, imposing a bid or award limit can mitigate the risk of over-reliance on certain suppliers and diversify risks across multiple contractors.[708] While such limits are generally permissible, they should not hinder cross-border participation in the Internal Market. In the scenario where insufficient bid interest results in unawarded lots, contracting authorities need to consider whether retendering or negotiation is more feasible.[709] To avoid such risks and preserve competition from larger businesses, contracting authorities may permit lot combinations ('lot bundling') in tenders, as discussed in the following section.

4.3.4 Lot bundling

Pursuant to Article 46 (3) Directive 2014/24/EU, Member States may permit contracting authorities to award contracts that combine several or all lots, provided that more than one lot may be awarded to the same tenderer.[710] This is conditional

[707] See CCP 2019, art L.2113-10, which states that the contracting authority may limit the number of lots for which a single economic operator may submit a tender or the number of lots that may be awarded to a single economic operator. In Germany, see Section 30 in the Ordinance on the Award of Public Contracts (Procurement Ordinance (*Vergabeverordnung – VgV*)), entered into force on 18th April 2016.

[708] Sanchez-Graells, *Public Procurement and the EU Competition Rules* (n 62) 411; Müller-Wrede/Delcuvé *'Kommentar'* in Malte Müller-Wrede (ed), *GWB-Vergaberecht einschließlich WRegG: Kommentar* (2nd edn, Reguvis Fachmedien 2023) at 78, para 251 citing *OLG Düsseldorf*, decision of 15 June 2000 – Verg 6/00; Burgi, Dreher and Opitz (n 651) para 61.

[709] See Sanchez-Graells, *Public Procurement and the EU Competition Rules* (n 62) 352.

[710] Directive 2014/24/EU, art 46 (3).

upon the contract notices specifying which lots may be combined.[711] Article 46 (3) differs from Article 46 (2) in that it introduces the possibility for tenderers to bid for combined lots within a single tender, a practice also referred to as lot bundling.[712] It does not simply refer to bidding for multiple lots within a single tender, but rather to treating those lots as if they were bundled into a single contract. Contracting authorities are required to specify which lots may be combined in contract notices.[713] Failure to do so in the contract notice could result in tenderers proposing different combinations of lots, thereby increasing the administrative burden of evaluating tenders.[714]

Lot bundling incentivises large businesses to participate, even when contracts are divided into lots, as it allows them to achieve economies of scale by bidding for bundled lots. However, this practice may deter smaller bidders from submitting bids, as they typically lack the capacity to generate such economies of scale.[715] Consequently, encouraging lot bundling could be at odds with the objective of the division into lots under Directive 2014/24/EU, which is intended to facilitate SMEs' access to public procurement.[716]

In Germany, contracting authorities are required to justify their decision when awarding bundled lots to a single tenderer.[717] §97(4) GWB stipulates that several lots may be

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[711] Directive 2014/24/EU, art 46(3).

[712] ibid.

[713] Directive 2014/24/EU, art 46(3).

[714] A simple example is, if a contract is divided into five lots, A, B, C, D, E, and lot bundling is allowed. If the contracting authority does not specify which lots can be bundled together, bidders might bundle lots AB, ABC, ABD, BC, BD etc. In this scenario, evaluating tenders can be challenging as the contracting authority needs to compare the different permutations. Thus, it is more reasonable for contracting authorities to make it clear which lots can be bundled together.

[715] See Chapter 3, Section 3.3.1

[716] Trybus 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 335.

[717] GWB (2023), § 97(4).

awarded collectively if economic or technical reasons require so.[718] These justifications are interpreted in the same manner as those required when a contracting authority decides not to divide a contract into lots.[719] As discussed in Section 4.3.1.2, reasons such as increased financial costs are not considered sufficient justifications, making the approach to lot bundling equally stringent in Germany.

In France, the previous public procurement code, CMP 2006, did not explicitly address lot bundling but allowed for the possibility of awarding several lots to the same tenderer and signing a single contract encompassing those lots.[720] However, considering the rest of Article 10 CMP 2006, which mandated that contracts be awarded in separate lots and tenders be evaluated lot by lot, this provision implied only the possibility of signing one contract covering multiple lots rather than allowing tenderers to bundle lots.[721] Nonetheless, lot bundling was not entirely excluded under the CMP 2006. It was specified that when a contract involved both construction work and operation or maintenance services, the construction work and operation or maintenance services shall not be bundled in the same lot.[722] Thus, it is possible that operation and maintenance services are bundled together but not with the construction work lot. The rationale behind this prohibition could be to prevent large businesses from combining construction and maintenance lots, thereby encouraging SMEs to bid for operation or maintenance lots. However, the new public procurement code, CCP 2019, removed

[718] ibid.

[719] See Section 4.3.1 for a discussion of economic and technical reasons; also see Müller-Wrede/Delcuvé (n 708) 72, para 234.

[720] CMP 2006, art 10.

[721] Ibid.

[722] CMP 2006, art 10.

this restriction, which is consistent with the trend that the French approach to lot division has become increasingly less mandatory and more discretionary.[723]

The decision on whether lot bundling should be left to the discretion of contracting authorities or require justifications involves a balance of interests. On the one hand, lot bundling can enhance economic efficiency, as large businesses may submit tenders offering greater economic advantage due to economies of scale. On the other hand, encouraging more SMEs to bid for lots is advantageous for competition within the public procurement market, particularly in the long term.[724] In Germany, considering the interests of SMEs is a general principle in public procurement, leading to stricter constraints on lot bundling, as it is perceived to discourage SME participation.[725] In contrast, French procurement law appears to adopt a more permissive approach to lot bundling. Article 10 CMP 2006 emphasised that the primary objective of lot division is to promote the broadest possible competition and, therefore, did not impose specific constraints on contracting authorities to implement lot bundling.[726] The new CCP 2019 also removed the 'lot by lot' evaluation principle, a principle that had persisted through all reforms of public procurement legislation.[727] Contracting authorities are no longer required to evaluate tenders on a lot-by-lot basis, which facilitates the evaluation of tenders that include bundled lots and further reflects a shift away from a rigid approach of the division into lots. It may be attributed to Recital 79 Directive 2024/24/EU, which emphasises the importance of comparing tenders for

[723] For a discussion on the shift from a mandatory approach to lot division to a 'divide or justify' approach in French public procurement law, see Section 4.3.1.
[724] For a discussion about the importance of SME participation in public procurement, see Chapter 1.
[725] Burgi, Dreher and Opitz (n 651) para 33.
[726] CMP 2006, art 10.
[727] ibid.

individual lots with those for multiple or all lots.[728] While not legally binding, Recital 79 suggests that contracting authorities should assess whether lot bundling provides a better solution than awarding contracts lot by lot, based on which tenders best meet the award criteria.[729]

4.3.5 Alternative bids offered by tenderers

Related to lot bundling, an important question is whether tenderers are permitted to submit alternative bids that vary in price based on the number of lots they may be awarded.[730] For instance, consider a cleaning service contract divided into three lots (Lot A, Lot B, Lot C), each corresponding to cleaning services for one office building. If the contracting authority permits lot bundling and states clearly in the contract notice that Lots A and B can be bundled and all three lots can be bundled together, with alternative bids permitted, a tenderer might submit a bid of EUR 3,000 for Lot A, EUR 3,000 for Lot B, and EUR 5,500 for the combination of Lots A and B, and EUR 8,000 for all three lots. Another tenderer, a small business, might bid EUR 2,600 for Lot C alone.

Article 46 Directive 2014/24/EU does not explicitly address alternative bids, leaving it to Member States to decide whether they should be permitted. Both Herrera Anchustegui et al and Steinicke suggest that allowing alternative bids would be

[728] Directive 2014/24/EU, recital 79.

[729] ibid.

[730] There are different terms to describe this practice, alternative bids, discounts, rebates. A simple example in this case: in a procurement procedure to repair a railway, and it is divided into four lots, Lot A, Lot B, Lot C, Lot D. A tenderer offers two different tenders, one tender contains Lot A and Lot B, price is EUR 200, another tender is Lot A, Lot B, Lot C, Lot D, and the corresponding price is EUR 700. The fourth dimension is whether this kind of bidding strategy is allowed or not.

beneficial, as it reflects a discount based on economies of scale.[731] However, similar to lot bundling, allowing such bids could compromise the purpose of dividing contracts into lots, which is to encourage SME participation.[732] Trybus contends that the balance of interests between economies of scale and SME participation should not be determined by whether alternative bids are permitted but rather addressed in the decision on lot bundling itself.[733] It is argued that if lot bundling is permitted, alternative bids should also be permitted; conversely, if bundling is not allowed, the issue of alternative bids becomes irrelevant.[734]

Nonetheless, it is possible for lot bundling to be permitted while alternative bids are not. For instance, in the example above, the contracting authority may allow bids only for Lot A, Lot B, Lot C, or the combination of Lot A and Lot B, thus restricting bidders to one of these four options. This approach provides more certainty for bidders compared to a scenario where alternative bids are allowed.[735] Although prohibiting alternative bids may limit bidding flexibility, it provides a clearer expectation for all bidders. Allowing alternative bids will increase the uncertainty of competition in a procedure, which may discourage SMEs from bidding.[736]

French legislators have shown hesitancy regarding alternative bids. The old CMP 2006 explicitly prohibited bidders from submitting alternative bids based on the number

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[731] Herrera Anchustegui, Margrethe Nes, and Sikkeland (n 684) 503, para 46.17; Steinicke (n 670) 567, para 9.

[732] Trybus 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 338.

[733] ibid.

[734] Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 338.

[735] If alternative bids are allowed and bundling is only allowed for Lot A and Lot B, in this case, bidders might be able to submit a bid which only contains Lot A at price EUR 3000, and they can also submit another bid contains the combination of Lot A and Lot B at price EUR 5,500.

[736] See Chapter 3.

of lots awarded.[737] However, Ordinance 2015-899, which transposed Directive 2014/24/EU, marked a shift by leaving alternative bids to the discretion of the contracting authority.[738] This change may be attributed to Recital 79 Directive 2014/24/EU, which emphasises the importance of comparing bids for individual lots and those for several or all lots, suggesting flexibility in evaluating alternative bids to identify the most advantageous tender.[739] Interestingly, Law 2016-1692 amended Article 32 Ordinance 2015-899 to prohibit alternative bids, reverting to the stance of the CMP 2006.[740] Most recently, however, the CCP 2019 removed this restriction, once again granting contracting authorities the discretion to permit alternative bids.[741] As noted earlier, the lot-by-lot assessment principle was also removed in CCP 2019, further enhancing the discretion of contracting authorities in tender evaluation.[742] Thus, currently in France, there does not appear to be any constraints on contracting authorities permitting the submission of alternative bids from tenderers.

In Germany, alternative bids offering combination discounts (*Kombinationsrabatt* or *Koppelungsnachlass*) allow tenderers to provide reduced pricing when awarded multiple lots.[743] The *OLG Düsseldorf* argued that the principle of considering SME interest prohibits combination discounts unless each individual lot within the

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[737] A tenderer might submit variable tenders. For example, in a tender for cleaning service for 10 buildings and divided into 10 lots, a tenderer submits a tender at the price EUR 12,000 for one lot and another tender for 10 lots at EUR 100,000.

[738] Article 32 of the Ordinance 2015 mandated that tenders be assessed on a lot-by-lot basis but permitted alternative bids if authorised by the contracting authority. See *Ordonnance n° 2015-899*, art 32.

[739] Directive 2014/24/EU, recital 79.

[740] *Ordonnance n° 2015-899* was in force from 1 April 2016 to 11 December 2016. *Ordonnance n° 2015-899 du 23 juillet 2015 relative aux marchés publics*, art 32 (as amended by Loi n° 2016-1691 du 9 décembre 2016, art 39)

[741] CCP 2019, arts L.2113-10, L.2113-11.

[742] See Section 4.3.4.

[743] Müller-Wrede/Delcuvé (n 708) 78, para 252.

combination must also represent the most economical offer when considering the discount.[744] Delcuve challenges this interpretation, contending that considerations for SMEs shall not compromise the principle of cost-effectiveness.[745] From this perspective, an overall award or a combination of lots is justified if they are more economically advantageous than a sum of individual lot offers.[746] For instance, in the previous example involving cleaning service, Tenderer A submits a discounted offer of EUR 8,000 for all three lots (EUR 2,667 for each lot), and an alternative offer of EUR 5,500 for Lot A and B combined, while an SME Tenderer B offers EUR 2,600 for Lot C alone.[747] If the contracting authority evaluates bids on a lot-by-lot basis and the lowest price is the award criterion, Tenderer B will win Lot C. Lots A and B will be awarded to Tenderer A for EUR 5,500. This decision results in a total cost of EUR 8,100, which exceeds Tenderer A's lot-bundling offer of EUR 8,000.

Tenderer	**Lot A**	**Lot B**	**Lot C**
Tenderer A	Bid 1 EUR 8,000		
	Bid 2 (alternative bid) EUR 5,500		N/A
Tenderer B (an SME)	N/A	N/A	Bid 3 EUR 2,600

Table 4.1 An example to illustrate lot bundling and alternative bids

If the contracting authority compares all tenders, as Recital 79 of Directive 2014/24/EU suggests, the decision might favour awarding all three lots to Tenderer A. In fact, this consolidates the lots back into a single contract. While one could argue that this outcome benefits the contracting authority by lowering overall costs, it overlooks the

[744] *OLG Frankfurt am Main*, 09 May 2017, 11 Verg 5/17. This is reiterated in *OLG Düsseldorf*, 28 March 2018, VII-Verg 54/17.
[745] Müller-Wrede/Delcuvé (n 708) 78, para 252. For a discussion on the principles of public procurement in Germany, see Burgi, Dreher and Opitz (n 651) para 33.
[746] Müller-Wrede/Delcuvé (n 708) 78, para 252.
[747] See Table 4.1 for an illustration.

resources spent on designing the lot division and evaluating tenders for both individual lots and bundled lots. If awarding the entire contract is an intended outcome, it might be more practical to allow the contracting authority not to divide the contract from the beginning, rather than undergoing the complex process of dividing it into lots and reconsolidating them after bid evaluation.

Burgi argues that considering the interests of SMEs is a fundamental principle of the German public procurement system, the same as the principle of competition, the principle of equal treatment, and the principle of transparency.[748] Although cost-effectiveness is supposed to be upheld in the procurement process, contracting authorities are not obliged to choose the least-costly offer.[749] In the scenario outlined above, if the contracting authority selects the lot-bundling offer of EUR 8,000, it may achieve cost savings, but it risks sidelining the interests of SMEs, especially if the SME's bid was the most advantageous tender for Lot C. As previously discussed, for an overall award to be justified, there must be disproportionately higher economic costs or technical benefits.[750] This implies that awarding all lots to a single bidder should only be permissible when each individual lot within the bundled offer represents the most economically advantageous tender, thereby demonstrating a disproportionate economic advantage.

Taking this a step further, in a negotiated procedure, the contracting authority could negotiate with Tenderer A to see if they would be willing to reduce their overall offer to less than EUR 7,800, thereby making the total award more economical than Tenderer B's offer for the individual lot. If Tenderer A agrees to such a reduction, awarding the

[748] GWB (2023) § 97 (1)-(2); Burgi, Dreher and Opitz (n 651) para 33.
[749] GWB (2023) § 97 (1)
[750] See Section 4.3.1.

contract as a whole might appear to be the most cost-effective solution. However, this approach would fail to consider the interests of SMEs, which §97(4) GWB requires should be given primary consideration.[751]

To consider the interests of SMEs, one possible solution could be to reserve certain lots exclusively for SMEs, a highly debated approach within the EU, discussed in the next subsection. Without reserving lots for SMEs, another option is to limit the number of lots that can be awarded to a single tenderer. For example, in the previous cleaning service scenario, the contracting authority could specify in the contract notice that a maximum of two lots can be awarded to one tenderer or specify that only Lots A and B can be combined. This approach indirectly protects SMEs' interests by preventing a single bidder from winning the entire contract. While this solution is theoretically possible, it poses practical challenges. Contracting authorities may be reluctant to prioritise the interests of SMEs at the expense of a potentially less costly offer. The final section of this chapter will explore the economic incentives of contracting authorities in more detail.[752]

4.3.6 The possibility of reserving lots for SMEs[753]

Article 46 of Directive 2014/24/EU does not specify whether contracting authorities may reserve lots specifically for SMEs. However, Recital 36 suggests that certain lots can be reserved for sheltered workshops or social enterprises whose primary aim is

[751] §97 (4) does not simply state that the interests of SMEs shall be considered in public procurement procedures but stresses that 'shall be primarily taken into account'. See GWB (2023), §97 (4).
[752] See Chapter 8, Section 8.4.3.
[753] See Chapter 7 for a thorough discussion on reserved contracts for SMEs.

to support social and professional integration, in alignment with Article 20.[754] This reservation applies to economic operators where at least 30 per cent of the workforce consists of disabled or disadvantaged workers.[755] SMEs encompass a much broader scope of economic operators than the sheltered workshops defined in Article 20.[756] More importantly, reserving contracts exclusively for SMEs contradicts Article 173 (1) TFEU, which mandates that the development of SMEs must be encouraged within the context of open and competitive markets.[757] Reserving contracts exclusively for SMEs means protecting them from a competitive market and preventing large businesses from bidding for those lots. Thus, it is against Article 173 (1) TFEU.[758] Furthermore, reserving contracts for SMEs often results in reserving contracts for national SMEs or even local SMEs.[759] From an economic perspective, SMEs in other Member States might not have the capacity to participate in cross-border procurement even if they are eligible for reserved lots in another Member State.[760] Thus, lots cannot be reserved for SMEs unless they meet the criteria of sheltered workshops outlined in Article 20 Directive 2014/24/EU.[761]

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[754] Directive 2014/24/EU, recital 36.

[755] ibid.

[756] For the definitions of SMEs in the EU, see Chapter 2, Section 2.2.

[757] Arrowsmith, *The Law of Public and Utilities Procurement* vol 2 (n 683) 737, para 20-58, citing TFEU, art 173(1).

[758] ibid.

[759] Arrowsmith argues that reserving contracts for SMEs might favour national SMEs in practice, which is against the principle of non-discrimination. See Sue Arrowsmith, 'Rethinking the Approach to Economic Justifications under the EU's Free Movement Rules' (2015) 68 Current Legal Problems 307, 317. Steinicke expresses the same view, see Steinicke (n 670) 567.

[760] Large businesses are the main participants in cross-border procurement in the EU. See European Commission, *Study on the Measurement of Cross-Border Penetration in the EU Public Procurement Market: Final Report* (Prometeia SpA, BIP Business Integration Partners SpA, and Nova School of Business and Economics Lisbon, March 2021).

[761] In a recent case *Conacee*, the CJEU decided that Member States can add additional criteria to narrow down the scope of economic operators who are eligible to compete in reserved contracts under Article 20 of Directive 2014/24/EU. See Case C-598/19 *Conacee* EU:C:2021:231.

Although reserving lots for SMEs is inconsistent with EU law, there is a silver lining for SMEs under the lot division regime, provided by the lot-exempt rule in Article 5 (10) Directive 2014/24/EU.[762] This rule allows certain lots to be awarded without adhering to the Directive's full procedural requirements, provided specific conditions are met.[763] For works contracts, the estimated value of the lot must be less than EUR 1 million, and for supplies or services contracts, less than EUR 80,000.[764] Additionally, the aggregated value of these exempt lots cannot exceed 20 per cent of the aggregated value of all lots.[765] Arrowsmith argues that this exemption is intended to incentivise contracting authorities to divide contracts into smaller lots and encourage SME participation.[766] While this exemption does reduce the administrative burden on contracting authorities, it also means that the Directive's information disclosure requirements will not apply to these lots. As a result, economic operators from other Member States may not have access to information about these exempt lots, potentially turning them into *de facto* reserved lots for domestic or local SMEs. Nevertheless, these exempt lots remain subject to the principles of non-discrimination and equal treatment. If an economic operator from another Member State bids for an exempt lot, the contracting authority must evaluate it in an equal and non-discriminatory way with bids from domestic suppliers. However, given that the rules of

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[762] Directive 2014/24/EU, art 5(10).

[763] ibid. See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 472, para 6-122.

[764] ibid

[765] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 472 - 473, para 6-122 - 6-123. Arrowsmith argues that the value of the exempted lots shall not be disregarded when deciding whether the contract exceeds the threshold to apply the directive. For example, a contracting authority needs to procure construction work with an estimated value of EUR 5.2 million. The contracting authority decided to divide the contract into five lots, one of which was EUR 3.2 million and four of which was EUR 500,000. Based on Article 5 (8), all lots of this contract shall apply the rules in Directive 2014/24/EU, whereas two lots of EUR 500,000 can be exempted. The other three lots shall still apply the directive, even though the aggregate value of the three lots is lower than the EU threshold, the calculation shall take the overall value of all lots into consideration. See Directive 2014/24/EU, art 5(8).

[766] ibid.

Directive 2014/24/EU do not apply to these lots, the lack of publicly available information gives local and domestic economic operators a distinct advantage. Moreover, because the value of these lots is relatively low, large businesses may not be interested in bidding for them, leaving domestic or local SMEs as the primary beneficiaries under Article 5 (10) Directive 2014/24/EU.[767]

4.3.7 Summary

This section assessed Article 46 Directive 2014/24/EU from six key aspects: the scope of explanation for not dividing contracts, the methods of dividing contracts, lot limitations on tenders and awards, lot bundling, alternative bids, and the possibility of reserving lots for SMEs. The analysis reveals several challenges to achieving the goal of facilitating SME participation in public procurement. Firstly, contracting authorities retain significant discretion not to divide contracts, even in Member States where lot division is mandatory, such as France. Secondly, lot limitations, while beneficial for SMEs by fostering competition across multiple lots, remain optional for contracting authorities, leaving no obligation to limit the number of lots awarded to a single tenderer. Additionally, practices like lot bundling and alternative bids may discourage SMEs from bidding, as they attract large tenderers who can leverage economies of scale and reconstitute the divided contract into an entire one.

The national legislators need to strike a balance between value for money achieved through economies of scale and encouraging SME participation. In Germany, for example, the interests of SMEs are prioritised in public procurement procedures by

[767] Directive 2014/24/EU, art 5(10).

ensuring that contracting authorities cannot simply award all lots to a bidder proposing an overall lower price compared to individual lot offers unless there is a disproportionate advantage. Lastly, while reserving lots for SMEs is inconsistent with EU law unless the reservation is for sheltered workshops as defined in Article 20 Directive 2014/24/EU, SMEs could still benefit from the exemption rule in Article 5 (10), particularly domestic or local SMEs. This section also examined public procurement rules in France and Germany as examples to illustrate how these key aspects of lot division are designed. It identified a trend in France, where the approach has shifted away from a mandatory lot division to a 'divide or justify' approach, granting contracting authorities more discretion than in the past.

Both Arrowsmith and Trybus contend that the default 'divide or explain' approach established by Article 46 Directive 2014/24/EU is unlikely to lead to a significant change in the practices of contracting authorities and, consequently, may have little impact on SME participation in public procurement.[768] This chapter demonstrates that even a mandatory approach may not improve SME participation unless a Member State actively prioritises SME interests in the above-mentioned key aspects of lot division, such as by setting bid or award limits and prohibiting alternative bids. The decision to prioritise the interests of SMEs lies with national legislators and is linked not only to public procurement law but also to a broader context of small business policy in one country.[769] In France, the old CMP 2006 clearly stated that the primary objective of lot division was to promote the broadest competition rather than protecting

[768] See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 470, para 6-118, 470; Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 342.

[769] As discussed in Chapter 1, promoting SMEs in public procurement is regarded as a tool to facilitate SMEs' business environment. Also see OECD, *SMEs in Public Procurement* (n 18) 29.

the interests of SMEs.[770] Even though France adopted a mandatory approach to lot division, it has broadened the range of justifications available to contracting authorities for not dividing contracts. In contrast, in Germany, taking the interests of SMEs into account is a fundamental principle of the procurement system. Thus, it has stricter rules on contracting authorities to avoid dividing contracts and more limitations on alternative bids. This suggests a potential hypothesis: lot division is only effective in enhancing SME participation in public procurement when its design specifically accounts for SME interests, as demonstrated by the German approach.

The *EU Single Market Scoreboard (Access to Public Procurement)* includes two indicators to reflect SME participation and contract awards in public procurement: *indicator [7]* measures the proportion of contracts that include SMEs, while *indicator [8]* records the proportion of bids submitted by SMEs.[771] It is noteworthy that *indicator [7]* reflects the proportion of contracts in which SMEs are *included*, rather than those awarded to SMEs, which might present an inflated figure compared to the actual proportion of contracts awarded to SMEs.[772] In France, 66 per cent of bids were submitted by SMEs, with SMEs involved in 41 per cent of contracts.[773] In Germany, by contrast, 71 per cent of bids were from SMEs, and 61 per cent of contracts included SMEs.[774] *Indicator [9]*, which tracks the proportion of contracts divided into lots, reveals that France adopts lot division in 42 per cent of contracts, whereas Germany

[770] See CMP 2006, art 10.
[771] The reporting period of this report is from January 2022 to December 2022. See European Commission, 'Single Market and Competitiveness Scoreboard, Access to public procurement' (n 465).
[772] ibid. The report does not define the term ‘include’, which is not a recognised legal concept in EU public procurement law. It could, however, refer to contracts awarded to SMEs as prime contractors, as members of a consortium, or as subcontractors.
[773] European Commission, ‘Single Market and Competitiveness Scoreboard, Access to public procurement' (n 465).
[774] ibid.

applies it in only 18 per cent.[775] It seems that although lot division is employed far less frequently in Germany than in France, SMEs in Germany are more likely to bid for contracts and are awarded a higher proportion of them than their French counterparts. This may indicate that the German approach to lot division is, in fact, more effective in facilitating SME participation, or that Germany has adopted additional measures to encourage SME participation in public procurement. Notably, the reports submitted by France and Germany to the Commission on the monitoring and implementation of EU public procurement rules do not identify any additional SME-friendly measures adopted by Germany that France does not implement.[776] Therefore, it remains possible that the German approach to division into lots, prioritising SME interests, may yield better outcomes for SME participation in public procurement. This may also be attributed to the smaller sizes of public procurement contracts in Germany. In the study on administrative capacity in EU Member States conducted by the Commission, 18 per cent of total procurement in France was published on the TED, whereas in

[775] European Commission, 'Single Market and Competitiveness Scoreboard, Access to public procurement' (n 465). The contracts published on TED are mainly those with an expected value higher than the EU threshold. In France, the division into lots rule applies to all public procurement contracts under the public procurement code, whereas in Germany, the division into lots only applies to contracts with an expected value higher than the EU threshold. For a discussion on the public procurement law system in Germany, see Daniel Wolff and Martin Burgi, 'Scaling down the Cascade: A Critical Analysis of the Implementation of Directive 2014/23 into German Public Procurement Law' in Steen Treumer and Mario Comba, *Modernising Public Procurement* (Edward Elgar Publishing 2018) 112.

[776] Both of the two countries reported in 2024 that the following policy measures are in place: Policy initiatives launched to support SMEs participation in public procurement; Measures targeting SME participation in different techniques for aggregated procurement (framework agreements, dynamic purchasing systems, and centralised procurement activities); Measures targeting the participation of start-ups and scale-ups in public procurement; Guidelines for contracting authorities on the application of 'divide or explain' principle (concerning division into lots). The only difference is that Germany reported measures ensuring that payments for public contracts are made on time, especially in the case of SMEs. France did not report this measure, instead, it reported measures addressing the payments to subcontractors, which is not reported by Germany. See European Commission, 'Country Reports and Information on EU Countries' <https://single-market-economy.ec.europa.eu/single-market/public-procurement/country-reports-and-information-eu-countries_en> accessed 29 July 2024.

Germany this figure was only 6 per cent.[777] It indicates that a large proportion of contracts are below the EU threshold in Germany, and those contracts are already of a manageable size for SMEs, especially considering that German SMEs have relatively larger sizes on average.[778]

4.4 The effectiveness of lot division in increasing SME participation

The analysis in the previous section is based on the assumption that SMEs are more incentivised to participate in bidding processes when contracts are divided into smaller lots. In this section, that assumption is examined through a practical evaluation, using data and empirical evidence to assess the actual impact of lot division on both SME participation and contract awards to SMEs. Additionally, given that lot division is not mandatory in most countries and contracting authorities retain significant discretion in determining whether to divide contracts, it is crucial to analyse the factors that either motivate or discourage them from dividing a contract. Without active implementation by contracting authorities, the potential benefits of lot division for SMEs will remain unrealised.

[777] See European Commission, *Public procurement – Study on administrative capacity in the EU*, for the figure in Germany, see 'Germany' <https://ec.europa.eu/regional_policy/sources/policy/how/improving-investment/public-procurement/study/country_profile/de.pdf> accessed 09 August 2024; for the figure in France, see 'France' <https://ec.europa.eu/regional_policy/sources/policy/how/improving-investment/public-procurement/study/country_profile/fr.pdf> accessed 09 August 2024.

[778] See Chapter 2, Section 2.2.2.

4.4.1 Empirical evidence of the relationship between lot division and SMEs[779]

Intuitively, dividing large contracts into smaller lots encourages greater participation from SME bidders, as the more manageable contract sizes make bidding more accessible for SMEs.[780] Empirical evidence supports this, demonstrating a significant increase in the number of SME bidders when contracts are divided into lots.[781] Tátrai, Vörösmarty and Juhász further confirm that the overall number of bidders, not just SME bidders, increases when contracts are divided into lots.[782] Although their research does not specify whether the increase in bidders stems from SMEs or large businesses, they observe that SMEs tend to win more contract when the number of bids is either one or more than five.[783] Based on this, they explain that when there are more than five bids, most of those bids are likely from SMEs, which improves their chances of winning.[784] Similarly, the overall increase in bidders when contracts are divided into lots could primarily be attributed to a rise in the number of SME bidders.

The impact of lot division on the probability of SMEs winning contracts presents an ambiguous picture. The *EU Final Report on the Analysis of the SMEs' Participation in Public Procurement and the Measures to Support It* (hereinafter referred to as the EU Final Report), utilising TED data from 2011 to 2017, demonstrates a statistically

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[779] As explained in Chapter 1, in this thesis, SME participation only refers to their bidding rather than winning.

[780] Trybus, 'The Promotion of Small and Medium-sized Enterprises in Public Procurement: A Strategic Objective of the New Public Sector Directive?' (n 565) 262; de Bas P and others (n 68) 59. Also, technical and financial requirements will be less challenging if they are calculated against the value of a lot rather than a whole contract. The qualification requirements will be discussed in the next chapter.

[781] Hoekman and Taş (n 119) 384.

[782] Tünde Tátrai, Gyöngyi Vörösmarty and Péter Juhász, 'Intensifying Competition in Public Procurement' (2024) 24 Public Organization Review 237, 247. Their finding also finds that contracts divided into fewer lots are more likely to attract more bidders compared with contracts divided into an excessive number of lots.

[783] ibid.

[784] Tátrai, Vörösmarty, and Juhász (n 782) 251.

significant increase of approximately 4 per cent in the probability of SMEs winning contracts when they are divided into 2-19 lots.[785] However, an exception is when the contract value is less than EUR 100,000, where dividing contracts into 2-19 lots actually lowers the chance of SMEs winning.[786] When examining different types of contracts, the division of work contracts into lots shows a more significant positive correlation with SME contract awards compared to service and supply contracts.[787] This may be due to the higher value of work contracts, which are better suited to division in a way that maintains lot sizes appropriate for SMEs. This is further reinforced by data showing that when contracts are divided into more than 20 lots, the number of contracts awarded to SMEs decreases significantly in supply contracts.[788] Interestingly, Tátrai, Vörösmarty and Juhász found that contracts divided into fewer lots are more likely to attract a greater number of bidders compared to those split into an excessive number of lots.[789] Thus, contracting authorities shall avoid dividing contracts into an excessive number of lots, such as more than 20, when implementing lot division in order to preserve competition both among SMEs as well as overall competition.

However, contrasting evidence suggests that lot division can, in some cases, reduce SMEs' chances of winning contracts. Hoekman's study reveals a negative correlation

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[785] de Bas P and others (n 68) 63. The methodology used is a matching approach based on counterfactual logic. This means that they compared similar awards to handle the complexities arising from different contract types and values. In the analysis, they categorized contracts into two treatments: (i) using a 'few' lots (2-19) compared to no lots, and (ii) using 'many' lots (20+) compared to a group where a maximum of 19 lots were used.

[786] ibid.

[787] de Bas P and others (n 68) 61. In the research conducted by Tátrai, Vörösmarty and Juhász, it is found that supply contracts (lots) receive more single bids, whereas most construction work contracts (lots) receive more than three offers. See Tátrai, Vörösmarty and Juhász (n 782) 247.

[788] de Bas P and others (n 68) 61.

[789] Tátrai, Vörösmarty and Juhász (n 782) 248.

between the probability of an SME winning a contract and lot division.[790] An exception arises when the value of lots is lower than a specific threshold, EUR 23,469, at which point the probability of SMEs winning increases.[791] If the optimal value of a lot where SMEs are more likely to win contracts is capped at EUR 25,000, the total contract value would range between EUR 50,000 and EUR 475,000 when divided into 2-19 lots. Nonetheless, the EU 2019 Report demonstrates that even for contracts exceeding EUR 5 million, dividing them into 2-19 lots still results in an increase in the number of contracts awarded to SMEs, while dividing contracts into more than 20 lots correlates with a lower percentage of contracts awarded to SMEs.[792] These findings appear contradictory. The disparity may be attributed to differences in datasets or methodologies. Hoekman's study only includes contracts where at least an SME submitted a bid, raising a potential endogeneity issue; contracts in which SMEs participate might be more likely to be divided into lots. As a result, Hoekman's dataset may feature a greater proportion of contracts that are divided into lots. Additionally, Hoekman's study focuses primarily on the number of contracts awarded to SMEs rather than the total value of contracts awarded to SMEs.[793]

In contrast, the EU 2019 Report encompasses contracts with and without SME bidders. The data reveals that contracts are divided into lots, particularly in the range of 10 to 19 lots, and the aggregate value of contracts awarded to SMEs increased significantly.[794] However, the number of awards does not increase significantly when contracts are divided into lots. Furthermore, the type of contract plays a role. For work

[790] Hoekman and Taş (n 119) 393.
[791] ibid.
[792] de Bas P and others (n 68) 61.
[793] Hoekman and Taş (n 119).
[794] de Bas P and others (n 68) 61.

contracts, which typically have a higher value, dividing them into lots increases SMEs' share of winning by 6 per cent.[795] This suggests that while the number of contracts awarded to SMEs may not rise significantly, the overall value of contracts awarded to SMEs can increase when works contracts are divided into lots.

In another empirical study, Glas and Eßig found that the likelihood of an SME winning a bid is not significantly correlated with the lot division.[796] Although their research identified a positive correlation between lot division and SMEs' winning probability, this correlation was not statistically significant.[797] Thus, they rejected the hypothesis that lot division increases the likelihood of SMEs winning a bid.[798] The data sample in their study indicated that 77.8 per cent of contracts were divided into lots, with an average of 9.96 lots.[799] Thus, they argue that lot division, as a policy, is not effective in increasing the likelihood of SMEs winning bids.[800]

It is evident that the impact of lot division on SMEs' chances of winning contracts remains subject to conflicting findings. This inconsistency is likely due to differences in data samples and methodologies. For instance, if one study focuses on smaller firms, while another includes a higher proportion of medium-sized enterprises, the conclusion may vary. To better understand how lot division affects different categories of SMEs, more granular datasets are needed, containing information about the characteristics of SMEs. However, this remains a challenge because current data from

[795] ibid.
[796] Glas and Eßig (n 66) 73
[797] ibid.
[798] Glas and Eßig (n 66) 73.
[799] ibid 71.
[800] Glas and Eßig (n 66) 75.

TED only identifies whether a contract is awarded to an SME, without distinguishing between micro, small, and medium-sized ones.[801]

In conclusion, while exploring the relationship between lot division and the probability of SME winning contracts is valuable from an economic perspective and offers insights for stakeholders, this is not the primary objective of the legal framework. Article 46 Directive 2014/24/EU does not prescribe lot division with the aim of increasing SMEs' chances of winning contracts. As discussed in Section 4.2 the purpose of lot division within the EU framework is to improve SMEs' access to public procurement and to enhance their participation in the bidding process, without guaranteeing a proportion of contracts awarded to SMEs. Consequently, the absence of evidence showing an increase in SMEs' chances of being awarded contracts should not lead to the conclusion that lot division is not effective in achieving its intended objectives. More importantly, dividing contracts into lots increases SME participation, as evidenced by the rise in the number and value of contracts awarded to them. Without the division into lots, SMEs' access to public procurement may be impaired, leading to reduced participation. Given that the implementation of lot division depends largely on the discretion of contracting authorities, the next subsection examines the factors influencing contracting authorities in their decision to divide contracts into lots.

[801] Directive 2014/24/EU, annex V, PART D Information to be Included in Contract Award Notices. Member States are only required to report whether a contractor is an SME, rather than specifying whether the contractor is a small enterprise or a medium-sized enterprise.

4.4.2 The factors influencing contracting authorities to divide contracts into lots

Although Directive 2014/24/EU established lot division as the default approach across Member States, the flexibility inherent in this minimum harmonisation framework has allowed contracting authorities to maintain their existing practices unless a Member State imposes mandatory requirements.[802] The analysis has shown that, even if lot division is mandatory, as in France, contracting authorities still retain substantial discretion in deciding whether to divide a contract.

As Loader has pointed out, the primary objective for contracting authorities is value for money in practice.[803] No matter how well-designed the legal framework may be, SME participation in public procurement will remain stagnant if the practice of contracting authorities does not change accordingly. Contracting authorities are only likely to divide contracts when it serves their own interests unless legal obligations are strictly enforced. It is therefore important to investigate the factors that motivate contracting authorities to divide contracts into lots, and to explore ways of incentivising them to adopt this practice.

Flynn and Davis observe that, among various SME-friendly measures, the division of contracts into lots has been underutilised by contracting authorities, with the lowest level of compliance among public buyers.[804] One reason for this is the specialised knowledge of lot design that lot division requires, expertise that many contracting

[802] See Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 342.
[803] Kim Loader, 'The Challenge of Competitive Procurement: Value for Money Versus Small Business Support' (2007) 27 Public Money and Management 307, 313.
[804] For discussion of the divide between practice and policy, see Flynn and Davis (n 58) 568.

authorities may lack.[805] Additionally, evaluating tenders lot by lot imposes greater administrative costs than evaluating tenders for the entire contract.

Moreover, the risks of collusive behaviours among bidders in bidding for lots act as a deterrent for contracting authorities.[806] Collusion, also known as bid rigging, involves explicit agreements among bidders with the aim of not bidding at all or bidding in a way that they will not be competitive with other bidders.[807] Incumbent operators may agree to bid for specific lots at higher prices, leading to an inefficient outcome for the contracting authorities. Instead of benefiting from competitive pricing, contracting authorities may find themselves locked into arrangements where suppliers collude, undermining value for money. It has been argued that collusion among bidders can be mitigated through careful lot design, drawing on economic theories.[808] One approach is for the contracting authority to set the number of lots smaller than the number of anticipated participants in the bidding procedure.[809] By doing so, the likelihood that each participant will secure a lot is reduced, thereby diminishing the incentives for collusive behaviour.[810] Another perspective suggests that the number of lots should exceed the number of incumbent suppliers; those economic operators are mostly likely to bid.[811] If the number of lots matches the number of incumbents, these operators may effectively divide the contract among themselves, potentially discoursing smaller

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[805] ibid 568.

[806] Penelope Alexia Giosa, 'Division of Public Contracts into Lots and Bid Rigging: Can Economic Theory Provide an Answer?' (2018) 13 European Procurement & Public Private Partnership Law Review 30.

[807] Giosa (n 806) 30.

[808] Veronika Grimm and others, 'Division into Lots and Competition in Public Procurement' in Dimitri, Piga and Spagnolo (eds) (n 421) 168.

[809] ibid 282.

[810] Sanchez-Graells, *Public Procurement and the EU Competition Rules* (n 62) 13.

[811] Veronika Grimm and others (n 808) 169.

or weaker bidders, especially SMEs, from participating.[812] An additional method to prevent collusion is to introduce asymmetries between the lots and potential suppliers.[813] For instance, when potential suppliers have similar capacities, the contract could be divided into lots of varying sizes, creating a mismatch between the lots and suppliers' capacities. Conversely, when suppliers' capacities differ, dividing contracts into lots of similar sizes could also help deter collusive arrangements. While some suggest that reserving one lot for new entrants can effectively deter collusion among established bidders, such a practice may conflict with the EU principle of equal treatment.[814] As noted earlier, EU law only permits contracting authorities to reserve lots for sheltered workshops or social enterprises whose primary aim is to promote social and professional integration.[815]

In conclusion, successfully implementing lot division requires contracting authorities to possess a nuanced understanding of lot design and anti-collusion strategies. The additional administrative burden of evaluating a greater number of tenders also acts as a deterrent to lot division. Therefore, to encourage contracting authorities to divide contracts into lots, legislators and policymakers shall offer detailed guidance and training on effective lot design and methods to limit the administrative burden and counteract the risk of collusion.

[812] ibid.
[813] Veronika Grimm and others (n 808) 173, also see Giosa (n 806) 37.
[814] Giosa (n 806) 36.
[815] Directive 2014/24/EU, recital 36.

4.5 Conclusion

As discussed in Chapter 3, large contract sizes often act as significant barriers to SME participation in the public procurement market.[816] To address this challenge, dividing contracts into lots has been regarded as a solution across countries, especially within the EU, where Directive 2014/24/EU sets this as a default approach for all Member States. This chapter drew its analysis from Article 46 Directive 2014/24/EU, along with relevant legal rules in French and German public procurement laws. Previous literature has analysed the default 'divide or explain' approach outlined in Article 46 as being too lenient to achieve the goal of increasing SME participation.[817] This chapter argues that even a mandatory regime for lot division may fall short of achieving this goal. For example, in France, the scope of justifications for contracting authorities to avoid dividing contracts has expanded, and alternative bids, which tend to favour large companies, are permitted. In contrast, Germany has taken a stricter approach to lot division, prioritising SMEs' interests in the design of lots, which has proven more effective in enhancing SME participation.

This chapter also examined empirical evidence on the impact of lot division on SME participation and the number of contracts awarded. Although the impact of lot division on SMEs' chance of winning remains unclear, lot division is effective in encouraging more SMEs to submit bids in procurement processes. However, to achieve this effectiveness, contracting authorities need to be incentivised to implement the measure. From their perspective, dividing contracts into lots inevitably increases

[816] See Chapter 3, Section 3.3.2.

[817] See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 470, para 6-118, 470; Trybus, 'The Division of Public Contracts into Lots under EU Directive 2014/24/EU: Minimum Harmonisation and Impact on SMEs in Public Procurement?' (n 64) 342.

administrative costs, including the need to evaluate and manage multiple lots instead of a single contract, and may lead to higher overall costs. These factors naturally discourage contracting authorities from dividing contracts into lots in practice.

To conclude, while dividing contracts into lots can enhance SMEs' access to public procurement, its effectiveness is contingent upon certain conditions. Specifically, limiting the justifications for awarding combined lots or an overall contract and prohibiting alternative bids helps incentivise SME participation. As an SME-friendly measure, the division into lots is effective in increasing SME participation. It does not undermine other objectives of public procurement in the EU, most prominently, the objective of removing barriers in the Internal Market through the mandate of the non-discrimination principle. Striking the right balance between value for money, competition, and safeguarding SMEs' interests is a task for national legislators, as national public procurement systems may include such objectives.

Chapter 5 Managing the Qualification Process to Facilitate SME Participation in Public Procurement

5.1 Introduction

As discussed in Chapter 3, excessive qualification criteria are one of the primary barriers faced by SMEs when participating in public procurement.[818] Qualification criteria encompass various criteria proposed by contracting authorities that potential suppliers shall satisfy, such as a certain level of financial and technical capacity or prior experience in public procurement.[819] Due to their limited size, SMEs often encounter difficulties in meeting the financial capacity requirements, providing bid guarantees, or submitting records of past performance, particularly in circumstances where experience in public procurement is either required or preferred.[820]

Qualification criteria serve as a mechanism to exclude bidders who fail to meet them, thereby ensuring that contracts will be performed by qualified suppliers.[821] However, these requirements, often tied to economic capacity, tend to disproportionately challenge SMEs compared to larger businesses.[822] For instance, contracting authorities may impose excessively high annual turnover requirements relative to the estimated contract value, effectively excluding bidders with lower annual turnovers

[818] See Chapter 3; OECD, *SMEs in Public Procurement* (n 18) 37; Wittig (n 426) 20.
[819] See Carpineti, Piga, and Zanza (n 428) 19.
[820] See Chapter 3, Section 3.3.3; also see de Bas P and others (n 68).
[821] Dimitri Triantafyllou and Dimitri Mardas, 'Criteria for Qualitative Selection in Public Procurement: A Legal and Economic Analysis' (1995) 4 Public Procurement Law Review 145.
[822] See Chapter 3, Section 3.2.3.

from the competition.[823] This process also contains a risk that contracting authorities may abuse their discretion to favour or disadvantage certain economic operators during the qualification process.[824] For instance, large businesses with extensive experience in public procurement may be favoured at the qualification stage as contracting authorities tend to be risk-averse, as discussed in Chapter 3.[825]

The prevalence of restrictive qualification criteria is underscored by a survey conducted among contracting authorities in EU Member States, the US General Services Administration, and the Brazilian Department of Logistics and General Services.[826] This survey revealed that nearly all contracting authorities limit competition at the bidding stage through qualification criteria, with more than half adopting between three and five parameters to screen bidders.[827] Frequently used qualification criteria include financial and technical capacity requirements, legal eligibility to execute the contract, bank guarantees, and quality certificates.[828] While contracting authorities report that they consider factors such as promoting competition and facilitating SME participation when designing qualification criteria, these efforts are often insufficient to mitigate the challenges faced by SMEs.[829]

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[823] In this case, those companies whose annual turnover is less than this threshold cannot bid for the contracts, even though they might be able to propose an economically advantageous tender and perform the contract. The qualification process focuses on the bidders instead of the bids themselves. See Trybus, 'European Union Law and Public Procurement' (n 427).

[824] Treumer (n 429) 15.

[825] See Chapter 3, Section 3.4.2; also see Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74) 44.

[826] Carpineti, Piga, and Zanza (n 428) 18.

[827] ibid 18.

[828] Frequently used qualification requirements include (the order is from the most used to the least used based on the responses from surveyed contracting authorities): quality certificates, bank warranties, financial standing and financial dealings, specific budget revenue, technical qualifications, legal eligibility to execute the contract, no bankruptcy, and no tax debts. Carpineti, Piga, and Zanza (n 428) 18.

[829] ibid 18.

These selection criteria, while intended to ensure that contracts are performed by capable and reliable suppliers, may inadvertently disadvantage SMEs, limiting competition and diversity within the procurement process.[830] Recognising this issue, the World Trade Organisation Government Procurement Agreement Committee's *Best Practices for Promoting and Facilitating the Participation of SMEs in Government Procurement* highlighted the importance of proportionate qualification and selection criteria.[831] Similarly, the European Commission's *Code of Best Practices* emphasises the need for contracting authorities to ensure that selection criteria, particularly financial requirements, remain proportionate to the size and nature of the contract.[832] Reassessing and managing the formulation and application of selection criteria is thus crucial for reducing unnecessary barriers and creating a more equitable procurement environment that enables SMEs to compete effectively for public contracts. This chapter refers to such measures as managing the qualification process.

Beyond the difficulties posed by excessive qualification criteria, SMEs face the additional challenge of managing the administrative burden of preparing supporting documentation to verify compliance with these requirements.[833] These two dimensions are closely linked: even when qualification criteria are proportionate, complex verification requirements can effectively exclude SMEs who lack the administrative resources to manage the lengthy qualification process.[834] Similarly,

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[830] See Chapter 3, Section 3.2.3.

[831] World Trade Organization (WTO) Committee on Government Procurement, *Report of the Committee on Government Procurement on Best Practices for Promoting and Facilitating the Participation of SMEs in Government Procurement* (Decision of 9 October 2024) GPA/CD/6, 3.

[832] SEC (2008) 2193 final.

[833] See Chapter 3, Sections 3.3.3 and 3.3.6; also see European Commission, Green Paper on Modernisation of EU Public Procurement Policy: Towards More Efficient European Procurement Market, COM (2011) 15 final; Trybus and Andrecka (n 55) 231.

[834] See Chapter 3, Section 3.4.1.

streamlined verification procedures cannot fully address the barrier created by excessive qualification thresholds. This chapter evaluates approaches to managing the qualification process and assessing how they can be used to facilitate SME access to procurement opportunities effectively. The analysis focuses on the following key aspects of qualification: assessing financial capacity and past experience, as well as requiring financial guarantees. It further evaluates how to optimise the timing of qualification and verification, and establish appropriate shortlisting criteria that can effectively enhance SME participation. The analysis draws on both the Directive 2014/24/EU and the US Federal Acquisition Regulation (FAR), which, while sharing the common goal of facilitating SME participation, adopt distinct approaches to managing the qualification process.

5.2 Understanding Qualification Criteria in Public Procurement

Qualification criteria are established by contracting authorities to determine which companies are eligible to participate in a procurement procedure.[835] Unlike the evaluation of bids, which focuses on assessing the merits of tenders themselves, the qualification process fundamentally differs by evaluating the capability and reliability of the bidders.[836] Its primary objective is to ensure that suppliers possess the necessary ability to perform the contract, thereby safeguarding contracting authorities from unreliable contractors.[837] These qualification criteria serve as prerequisites for participation. They are predominantly binary rather than comparative, meaning that economic operators are either qualified if they satisfy the criteria or disqualified if they

[835] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 1183, para 12-01.
[836] Trybus, 'European Union Law and Public Procurement' (n 427) 13.
[837] ibid 14.

do not, without the need to compete over who meets the criteria the best.[838] Article 58(5) Directive 2014/24/EU mandates contracting authorities to express selection criteria (or 'conditions of participation') as minimum levels of ability of bidders.[839] Consequently, economic operators must meet these thresholds to be deemed qualified to bid for the contract.[840]

The qualification process under Directive 2014/24/EU comprises mainly two parts: verifying whether the economic operator is subject to exclusion under the grounds specified in Article 57 and assessing whether they satisfy the selection criteria set by the contracting authority.[841] The selection criteria encompass three main aspects: the suitability to pursue the professional activity, economic and financial standing, and technical and professional ability.[842] Although termed differently, selection criteria also function as exclusionary requirements to exclude economic operators that do not meet the selection criteria for a particular procurement procedure.

As discussed in Chapter 3, SMEs predominantly find the selection criteria more challenging than the exclusion grounds.[843] This is due to the intrinsic characteristics of exclusion grounds, which in US terminology are referred to as grounds for debarment or suspension.[844] Exclusion grounds evaluate whether economic operators

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[838] Treumer (n 429) 29.

[839] Directive 2014/24/EU, art 58(5).

[840] In procedures other than the open procedure, passing the thresholds is not enough to participate in bidding, only those invited economic operators can submit a bid. This process, termed 'shortlisting' reduces the number of bidders, which is a separate process from the qualification process. See Section 5.3.

[841] Directive 2014/24/EU, arts 57, 58.

[842] Directive 2014/24/EU, art 58(1). This chapter terms them as suitability, financial capacity, and technical capacity.

[843] Chapter 3, Section 3.2.3.

[844] 48 CFR § 9.406-1 regulates the causes that may lead to debarment. There is a difference between the US debarment and the EU exclusion grounds. EU exclusion grounds are mandatory. In the US, FAR 9.406-1 regulates that debarring officials have the responsibility to determine whether a debarment is in the government's interest. Thus, the existence of a cause for debarment does not necessarily lead

are conducting their activities in accordance with the law, including compliance with tax obligations, and address any serious deficiencies such as insolvency, criminal convictions, or other unlawful conduct.[845] They do not assess the financial and technical capacity of potential bidders, which SMEs may have inherent limitations compared to larger businesses, except in cases of insolvency, which will be addressed in Section 5.2.1.3. In contrast, selection criteria concern the precise levels of economic operators' financial and technical capacity,[846] aspects where SMEs may be at a comparative disadvantage due to their smaller size and resource constraints. Requirements for a minimum level of financial capacity, for instance, may include specific turnover thresholds or liquidity ratios that exceed what SMEs can realistically achieve. Additionally, the demand for past experience in public procurement can be particularly burdensome for some SMEs, especially newly established firms, as they may not have had prior opportunities to participate in such contracts, creating a cyclical barrier to entry. The provision of bid guarantees or other forms of financial security further exacerbates the challenges faced by SMEs, as these obligations can strain their limited financial resources.[847]

The US FAR uses different terminology from the 'qualification process', instead employing the 'determination of responsibility' to describe the process whereby

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to a potential contractor being debarred. 48 CFR § 9.402 clearly stipulates that debarment and suspension are discretionary actions and they are imposed only in the public interest for the government's protection and not for purposes of punishment.

[845] Triantafyllou and Mardas (n 821) 146. For example, Article 57 Directive 2014/24/EU lays down mandatory exclusion grounds that contracting authorities are required to exclude an economic operator when they meet one of those grounds. Article 57 (1) mainly includes reasons about whether an economic operator 'has been the subject of a conviction by final judgment'. Article 57 (2) stipulates that if the economic operator does not pay taxes or social security contributions. But when the economic operator has fulfilled its obligation to pay the taxes or social security contribution, then the contracting authority shall not use this as an exclusion ground.

[846] Triantafyllou and Mardas (n 821) 146.

[847] See Chapter 3.

contracting officers assess whether a business can be considered a prospective contractor, with FAR 9.103 (a) explicitly requiring that federal agencies only contract with responsible businesses.[848] According to FAR 9.104-1, the general standards of responsibility are not discretionary but obligatory, meaning all prospective contractors must comply with these standards to be deemed responsible.[849] The general standards include seven aspects, which can be categorised into four main aspects: financial capacity, technical capacity, satisfactory performance record, and integrity and business ethics.[850] This section analyses the qualification criteria rules from the aforementioned jurisdictions, with a particular emphasis on their impact on SMEs and the strategies contracting authorities can adopt to manage this process. By managing the qualification process, SMEs can compete with large businesses on a more level playing field.[851] It is important to note that the term 'qualification requirements' in FAR Part 9 pertains to products supplied by prospective contractors rather than bidders themselves.[852] This chapter focuses on the procedure through which contracting officers evaluate the qualification of bidders. For clarity, the term 'qualification process' is used consistently throughout this chapter, and the US FAR equivalent term is the 'determination of responsibility'.[853]

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[848] See 48 CFR § 9.103 (a). For an analysis, see John Cibinic, Ralph C Nash Jr and Christopher R Yukins, 'Chapter 4 – Contractor Qualification' in *Formation of Government Contracts* (4th edn, Wolters Kluwer 2011) 135.

[849] 48 CFR § 9.104-1.

[850] 48 CFR § 9.104-1. Beyond these mandatory general standards, contracting officers may also establish special standards if unusual expertise or specialised facilities are needed for a procurement demand. See FAR 9.104-2.

[851] Trybus and Andrecka (n 55).

[852] 48 CFR § 9.1 stipulates requirements for responsible prospective contractors, subpart 9.2 prescribes policies and procedures to determine qualification requirements for products. For example, as defined in 9.201, a qualified bidders list means a list of bidders whose products have been examined and tested, and these bidders have satisfied all applicable qualification requirements for that product.

[853] 48 CFR § Part 9.

5.2.1 The assessment of financial capacity

Financial capacity is a frequently used criterion by contracting authorities in the qualification process to ensure that potential bidders have the necessary resources to perform the contract.[854] Approaches to evaluating the financial capacity of bidders vary. In the EU, this assessment typically involves setting a minimum turnover requirement, which potential bidders must meet to qualify for participation in the procurement process. [855] However, contracting authorities tend to set an excessive turnover threshold to ensure that potential contractors possess robust financial capacity to execute the contract. [856] Such requirements often disadvantage SMEs, whose comparatively limited financial resources prevent them from meeting these criteria, thus excluding them from tender opportunities.[857] In contrast, the US FAR adopts a more flexible approach, relying on a discretionary evaluation of a supplier's financial viability. Contracting officers are less likely to impose specific financial thresholds; instead, they examine financial statements, key financial ratios, and other indicators of prospective contractors to determine their adequacy of financial resources on a case-by-case basis. This subsection will critically analyse the implications of these different approaches on SMEs' participation.

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[854] Arrowsmith *The Law of Public and Utilities Procurement* vol 1 (n 57) 1189, para 12-10.

[855] Directive 2014/24/EU, art 58.

[856] Recital 83 of Directive 2014/24/EU identifies overly demanding economic and financial standing requirements as obstacles to SME participation in public procurement. Also see Carina Risvig Hamer 'Article 58 Selection Criteria' in Steinicke and Vesterdorf (eds) (n 670) 646.

[857]Trybus and Andrecka (n 55) 234 citing *Conseil d'État*, 9 July 2007, Syndicat EGF-BTP, no 297711; Conseil d'État, 29 November 2006, *Agence nationale pour l'emploi*, no 290712.

5.2.1.1 The EU approach – minimum turnover requirement

In the EU, Article 58(3) Directive 2014/24/EU permits contracting authorities to require bidders to have a certain minimum annual turnover.[858] It is important to note that this provision is permissive rather than mandatory, but it mandates that all such requirements be related and proportionate to the subject matter of the contract, reiterating the principle of proportionality established in Article 18(1) Directive 2014/24/EU.[859] Contracting authorities have the discretion to set the minimum level of turnover to ensure that bidders possess the necessary economic and financial capacity to perform the contract. The turnover requirement is not confined to the company's total annual turnover; it can focus on the annual turnover in the specific area covered by the contract.[860] This approach presents two contrasting implications for SMEs. On the one hand, requiring a high minimum turnover, whether general or sector-specific, can be more difficult for SMEs to meet due to their typically smaller size and revenue, potentially excluding them from the bidding process.[861] On the other hand, while focusing on turnover in the specific area of the contract may initially appear to benefit SMEs that specialise in that field, it may still pose a barrier. SMEs, even when specialised, often have smaller operations and more limited turnover in specific sectors compared to large firms.

To mitigate SMEs' difficulty in meeting minimum turnover requirements, Article 58 (3) Directive 2014/24/EU imposes a quantitative limitation, stipulating that such requirements must not exceed twice the estimated contract value unless in exceptional

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[858] Directive 2014/24/EU, art 58(3).

[859] ibid, art 18(1).

[860] Directive 2014/24/EU, art 58(3).

[861] This has been discussed in Chapter 3, see Section 3.2.3. Also see Trybus and Andrecka (n 55) 234; Loader, 'SME Suppliers and the Challenge of Public Procurement: Evidence Revealed by a UK Government Online Feedback Facility' (n 461) 107.

cases.[862] This constraint demonstrates the principle of proportionality by ensuring that the financial criteria imposed on bidders are proportionate to the size and nature of the contract. This provision is mandatory, requiring Member States to incorporate this limitation into their national procurement law.[863] In doing so, it prevents contracting authorities from setting excessive turnover thresholds that could unjustifiably exclude SMEs from participation. Member States have the discretion to adopt even more restrictive measures on this matter, as long as it is compliant with the principles established in Article 18 (1) Directive 2014/24/EU.[864] For instance, a Member State may decide that the turnover requirement should not exceed the estimated value of the contract itself, thereby further easing access for SMEs.

Determining an appropriate and proportionate level of annual turnover represents a critical balance between contractor competence and market accessibility for SMEs. The European Commission's initial proposal for Directive 2014/24/EU suggested that the annual turnover threshold should not exceed three times the estimated contract value.[865] However, in the Directive, this cap was reduced to twice the estimated contract value.[866] This adjustment reflects a deliberate effort to balance the discretion of contracting authorities with the need to ease SMEs' difficulties in accessing public procurement opportunities.[867] By lowering the turnover cap, the Directive aims to prevent excessive financial thresholds that could exclude capable SMEs from

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[862] Directive 2014/24/EU, art 58(3).

[863] ibid.

[864] Directive 2014/24/EU, art 18(1).

[865] European Commission, 'Proposal for a Directive of the European Parliament and of the Council on Public Procurement' COM (2011) 896 final, 20 December 2011, 11.

[866] Directive 2014/24/EU, art 58(4).

[867] See European Parliament, 'Potential Impact on SMEs of Certain EP Amendments to Two Proposed Public Procurement Directives' (PE 507.505 IAAM-2013-1, 2013) 9. This report argued that reducing the turnover criteria from three times to two times theoretically increases the proportion of contracts that are accessible for SMEs.

participating in public tenders. However, it is also important to ensure that this cap would not be a standard requirement in procurement procedures, as contracting authorities still need to comply with Article 58 (1), which states that the turnover requirement shall be related and proportionate to the subject matter of the contract.[868] For example, in a small-value contract with low risk associated with the performance of the contract, twice the estimated contract value may be excessive for the contract's actual needs.[869]

In duly justified circumstances, contracting authorities may set a higher turnover requirement.[870] Such circumstances might involve risks related to the nature of the works, services or supplies.[871] This provision does not specify the scenarios where these special risks are involved.[872] Potentially, these risks may be associated with the performance of the contract, necessitating greater financial capacity from the bidder, such as long-term work contracts which involve a large amount of investment from the contractor.

When contracting authorities decide to impose a higher turnover requirement, they are obliged to record the main reasons for this decision in the procurement documents or in an individual report, as per Article 58 (3).[873] However, they are not required to provide justifications for the decision, and the reason can be stated after the contract is awarded.[874] Thus, it is doubtful that tenderers can challenge this decision in court to

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[868] Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 305.
[869] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 1193, para 12-15.
[870] Directive 2014/24/EU, art 58(3).
[871] ibid.
[872] Trybus and Andrecka (n 55) 235.
[873] Directive 2014/24/EU, art 58(3).
[874] This is a similar approach to division into lots. Article 46 Directive 2014/24/EU regulates that contracting authorities shall record the main reason for not dividing a contract. See Directive 2014/24/EU, art 46.

determine whether it is a 'duly justified case'.[875] The second paragraph of Recital 83 mirrors the stance in Recital 78 (2), which has been critiqued for overlooking the principle of effective judicial protection established in Article 47 of the EU Charter of Fundamental Rights and Article 19 (1) of the Treaty of the European Union, by exempting these decisions from administrative or judicial review.[876] As Arrowsmith suggests, while contracting authorities are granted a certain degree of discretion, judicial scrutiny remains essential to ensure that the authorities genuinely exercise this discretion based on the specifics of each case.[877] If decisions regarding an excessive turnover threshold are not subject to judicial oversight, not only would the principle of proportionality be undermined, but the principle of transparency would also be challenged.

As discussed in Chapter 4, Directive 2014/24/EU introduced an important measure to facilitate SME access to public procurement, specifically by dividing contracts into lots.[878] According to Article 58 (3), the turnover threshold shall be proportionate to the value of a specific lot, instead of the value of the whole contract.[879] The lot proportionality ensures that SMEs compete for lots without demonstrating financial capacity for the entire contract, which may include multiple lots beyond their reach. Prior to the enactment of Directive 2014/24/EU, the French highest administrative court (*Conseil d'État*) addressed the issue of proportionate turnover requirements in case no. 290712, ruling that such requirements must align with the value of specific

[875] Risvig Hamer (n 856) 654, para 32.
[876] Caranta (n 627) 428.
[877] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 1195, para 12-17. Also see Trybus and Andrecka (n 55) 235.
[878] See Chapter 4; also see Directive 2014/24/EU, art 46.
[879] Directive 2014/24/EU, art 58(3). This rule is referred to as 'lot proportionality' in this chapter.

lots rather than the overall value of the contract.[880] In this case, the contracting authority divided the contract into three lots valued at EUR 8,240,000, EUR 18,600,000, and EUR 5,400,000, respectively.[881] However, it required bidders to demonstrate an annual turnover of no less than the estimated value of all three lots (EUR 32,240,000), but the court held that this breached the competitive tendering obligations and annulled the procedure.[882]

This case was decided before Directive 2014/24/EU, which introduced specific rules under Article 58 (3) requiring that turnover requirements for contracts divided into lots be proportionate to the value of the individual lots.[883] While the turnover requirement for the largest lot in this contract (EUR 18,600,000) was less than twice its value, which could potentially comply with the cap set by Article 58 (3) Directive 2014/24/EU, the Court nonetheless deemed the approach restrictive to competition.[884] The judgment did not explicitly base its decision on the principle of proportionality or the consideration for SMEs. Instead, it focused on upholding the principle of competition, as established in Article L.551-1 of the French Administrative Justice Code.[885] While distinct, these issues are closely interlinked with each other. The principle of proportionality is to ensure that the financial criteria are not disproportionate to prohibit economic operators who do not possess such financial capacity from participating in public procurement, primarily SMEs. In turn, such exclusion impairs competition within the tendering process.

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[880] CE, 29 November 2006, *Agence nationale pour l'emploi, n° 290712*.

[881] ibid.

[882] CE *n° 290712* (n 880).

[883] Directive 2014/24/EU, art 58(3).

[884] CE *n° 290712* (n 880).

[885] Article L. 551-1 of the Administrative Justice Code allows interested parties to challenge breaches of publicity (transparency) and competitive tendering obligations before the contract is awarded. See *Code de justice administrative*, art L 551-1.

Article 58 (3) stipulates that if a bidder is awarded more than one lot, and several lots will be executed at the same time, the turnover requirement shall be modified accordingly.[886] However, this might raise a concern if a contracting authority assesses the financial capacity before evaluating tenders. When bidders are permitted to bid for multiple lots, the number of lots that a bidder will be awarded is uncertain. A solution could be postponing the timing of assessing the financial capacity of economic operators, which is discussed in Section 5.2.4. Another solution is requiring a turnover proportionate to the estimated value of all lots in the submitted tenders. However, this approach adds complexity to the qualification process for contracting authorities to assess. The question of choosing which approach is also related to the design of the lot division. If the contracting authority requires that bidders can only bid for one lot or will only be awarded one lot even if they bid for more than one lot, then it is feasible to evaluate their qualifications after tender evaluation, which guarantees their financial capacity to be proportionate to the value of the awarded lot. If the contracting authority decides that bidders can bid for and win an unlimited number of lots, it is proportionate to require bidders to have a financial capacity proportionate to the value of the lots that they bid for. This question is especially relevant for SMEs, as evidence shows SME participation increases when contracts are divided into lots.[887] An SME-friendly approach would be to postpone the timing of assessing/verifying financial capacity in this case. In that case, an SME does not have to possess a financial capacity proportionate to the value of the lots it bids for, but only proportionate to the lots that it will be awarded, as they might not be awarded all the lots they bid for.

[886] Directive 2014/24/EU, art 58 (3)

[887] See Chapter 4, Section 4.4; also see de Bas P and others (n 68) 63.

Although the lot proportionality rule is beneficial to SMEs, it poses challenges to contracting authorities in how they structure their procurement requirements. Authorities need to assess the financial requirements for each lot individually, which can add complexity to the procurement process. However, this effort can be balanced by the benefit of attracting more SMEs to participate in tendering. Nevertheless, contracting authorities might not perceive the more SME participation as a benefit to the procurement procedure, as they need to evaluate more tenders. Fundamentally, there is a mismatch of interests in SME policies in public procurement; contracting authorities may not gain direct benefits from these measures, but they bear the costs associated with measures to facilitate SME participation.[888] This will be further discussed in Chapter 8.

In relation to long-term contracts, Article 58 Directive 2014/24/EU does not clarify whether the turnover requirement should be proportionate to the annual value of the contract or its total value. Both Trybus and Arrowsmith contend that a balance needs to be struck, acknowledging that certain long-term contracts may necessitate substantial upfront investment in the performance phase; hence, limiting the turnover requirement to twice the annual contract value may not always be appropriate.[889] From the perspective of promoting SME access to public procurement, a turnover requirement set at twice the total contract value could present a barrier for them. While it is indeed essential to facilitate SME participation by limiting disproportionately high financial criteria, it is necessary to apply common commercial sensibilities. In practice, SMEs may not be well-suited for long-term contracts due to various factors, not least

[888] Contracting authorities may gain direct benefits when increased SME competition leads to lower procurement prices. For a further discussion, see Chapter 8, Section 8.4.3.
[889] Trybus and Andrecka (n 55) 235.

their limited access to financial resources, particularly long-term financing, compared to large firms.[890] As a result, SMEs are naturally positioned at a disadvantage in undertaking long-term contracts as prime contractors unless these contracts are divided into lots.[891] For the purpose of encouraging SMEs to participate in long-term contracts, dividing these contracts into smaller lots may be more effective than simply setting a cap on turnover requirements. If a long-term contract is not divided, an SME awarded the contract may still face significant challenges in securing the necessary financial resources for sustained performance. This situation not only places the contract at risk but could also expose the SME to potential financial distress.

5.2.1.2 The US approach – the ability to obtain

Listed as the first condition, FAR 9.104-1(a) requires that 'a prospective contractor must (a) have adequate financial resources to perform the contract, or the ability to obtain them'.[892] This is a mandatory requirement that all prospective contractors have to satisfy the financial adequacy, whereas, in the EU, contracting authorities have the discretion to decide whether they adopt a financial capacity requirement or not.[893] However, the US approach only requires an evaluation of the prospective contractor's

[890] SMEs might face higher interest rates or more severe guarantee conditions than large firms. See Alan Hughes, 'Finance for SMEs: A UK Perspective' (1997) 9 *Small Business Economics* 151; also see Rien Wagenvoort, 'Are Finance Constraints Hindering the Growth of SMEs in Europe?' (2003) 8(2) *European Investment Bank Papers* 23, 30.

[891] There are multiple ways to divide a contract into lots. Long-term contracts can be divided into lots based on different time phases. See Chapter 4, Section 4.3.2.

[892] 48 CFR § 9.104 (1)(a).

[893] The wording in Article 58 Directive 2014/24/EU is 'contracting authorities *may* impose requirements ensuring that economic operators possess the necessary economic and financial capacity to perform the contract'. See Article 58 Directive 2014/24/EU, emphasis added. Also see Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 1192, para 12-14.

qualification, rather than that of any bidder.[894] This implies that contracting officers do not assess the financial capacity of bidders before bid submission.[895] In general, contracting officers obtain information after a bid opening or receipt of offers.[896] The timing of the qualification and verification process will be discussed in depth in Section 5.2.4.

FAR 9.104-1 (a) adopts a flexible approach, allowing prospective contractors to demonstrate their ability to secure the necessary financial resources to perform a contract, even if they lack those resources at the time of bidding.[897] Both the financial and technical capacity assessments permit evidence that resources can be obtained.[898] To establish this 'ability to obtain resources', prospective contractors must provide 'acceptable evidence', such as a commitment letter from a bank for financing, rental agreements, purchase agreements, or contracts with suppliers for materials or equipment.[899] Such evidence must indicate that these arrangements will be in place by the time of the contract award to avoid delays or uncertainties.[900] Additionally, small businesses may fulfil these requirements through subcontracting arrangements, provided that they can furnish acceptable evidence of these commitments.[901] This flexibility allows small businesses to demonstrate their capacity to perform the contract by securing resources from external parties, thereby enabling them to qualify as

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[894] See 48 CFR § 2.101. A responsible prospective contractor means a contractor that meets the standards in FAR 9.104 (determination of responsibility).
[895] 48 CFR § 9.104-1 (a).
[896] 48 CFR § 9.105-1 (b) (1).
[897] ibid.
[898] 48 CFR § 9.104-1(e), 'have the necessary organization, experience, accounting and operational controls, and technical skills, or the ability to obtain them', also see FAR 9.104-1 (f) 'have the necessary production, construction, and technical equipment and facilities, or the ability to obtain them'.
[899] 48 CFR § 9.104-3 (a), emphasis added.
[900] ibid.
[901] 48 CFR § 9.104-3 (a).

responsible contractors. Such provisions promote more equitable competition, granting small businesses a fair opportunity to compete alongside larger, resource-abundant companies. Notably, by permitting evidence of resource access rather than requiring immediate possession, this rule lowers entry barriers and relieves small businesses of the need for substantial upfront investments.

Unlike the approach in Directive 2014/24/EU, the US FAR does not provide guidance on financial indicators or set a quantitative limitation for contracting officers.[902] Contracting officers have substantial discretion over the indicators and documents they use to assess a prospective contractor's financial capacity. In practice, there are several indicators frequently used by contracting officers, including the ratio of assets to liabilities, working capital, and credit ratings.[903] Given the substantial discretion conferred upon contracting officers, concerns may arise regarding procedural transparency. To address such concerns, bidders may submit protests to the Government Accountability Office (GAO) or the Court of Federal Claims (COFC).[904] However, the GAO does not review positive determinations of responsibility, as the determination that a prospective contractor's capability to perform a contract is

[902] See Section 5.2.1.1.

[903] Cibinic, Nash and Yukins (n 848) 138. For example, the General Service Administration (GSA) assessed a low bidder's financial data and concluded that this firm did not have sufficient working capital and its retained earnings showed a deficit. Moreover, the GSA noted that the potential contract value represented more than two and a half times the firm's prior fiscal year sales.

[904] The GAO has the authority to recommend the cancellation of a contract award and initiate a rebidding process; however, its decisions are not legally binding. Despite this, both agencies and bidders typically respect and adhere to GAO decisions, given the GAO's significant role as a primary venue for bid protests. Another major venue for bid protests is the Court of Federal Claims (COFC), which holds exclusive judicial jurisdiction over bid protests concerning government contracts. Generally, filing a protest at the COFC is a more time-consuming and costly process compared to a protest filed with the GAO. The GAO's authority to hear bid protests is established under the Competition in Contracting Act of 1984 (CICA), codified at 31 USC §3551-3557. The COFC's jurisdiction over bid protests is granted by the Tucker Act, specifically 28 USC § 1491(b).

primarily entrusted to the contracting officer's discretion.[905] Regarding a negative determination of responsibility, the GAO does not challenge it unless the contracting agency acted in bad faith or lacked a reasonable basis for the determination, since it essentially involves business judgment and allows for a great extent of discretion.[906] It is very rare when GAO sustain a protest challenging an affirmative determination of responsibility, unless 'the protester presents specific evidence that the contracting officer may have ignored information that, by its nature, would be expected to have a strong bearing on whether the awardee should be found responsible'.[907] However, if there is evidence showing that the contracting officer has considered all the negative information about one prospective contractor's responsibility but still made an affirmative determination of responsibility, the protester will likely be unable to challenge the determination.[908]

The discretionary evaluation of the financial capacity of bidders may prove burdensome for small businesses, as shown in Chapter 3. However, specific safeguards are incorporated into the responsibility determination framework, mandating referral of all non-responsibility determinations to the Small Business Administration (SBA).[909] Even if a contracting officer determines that there is insufficient evidence of responsibility for a small business, the contracting officer shall consult with the SBA, as mandated by the Small Business Act.[910] If the SBA issues a

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[905] GAO B-419088.4, 3.
[906] GAO, B-240655.
[907] GAO, B-408558; GAO, B-418266.4. The legislative basis is 4 CFR § 21.5(c).
[908] 'Pigs Do Fly: Bid Protest Challenging an Affirmative Determination of Responsibility Is Sustained by GAO' (*Smith Currie*, 30 October 2014) <https://www.smithcurrie.com/procurement-playbook/gao-issues-rare-sustain-of-a-bid-protest-challenging-an-affirmative-determination-of-responsibility/> accessed 12 November 2024.
[909] 48 CFR § 19.602-1
[910] 15 USC § 637(b)(7)).

COC, the contracting officer must either award the contract to the small business or cancel the solicitation, but only for reasons unrelated to responsibility.[911] This COC regime benefits small businesses that may otherwise be disadvantaged by contracting officers in the determination of responsibility procedure.[912] This will be discussed further in Section 5.2.2.2, where past experience requirements are involved in the determination of responsibility.

In summary, compared with setting minimum turnover requirements, the US FAR's approach entails a discretionary assessment of bidders' economic and financial capacity, which might enable a more accurate evaluation of potential contractors. The challenge of setting optimal turnover thresholds demonstrates the limitations of rigid requirements, as authorities must balance performance risk mitigation against potential participation reductions. Where contracting authorities might reasonably differ on whether twice or three times the estimated contract value represents an appropriate threshold, the arbitrary nature of such determinations becomes apparent. An economic operator with an annual turnover of 2.5 times the contract value might submit a superior tender compared to qualifying bidders, yet would be excluded from consideration under a three-times threshold requirement. Consequently, inflexible turnover requirements lack the adaptability necessary for optimal contractor selection, potentially excluding advantageous tenders from evaluation.

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[911] 48 CFR § 19.602-4 clearly stipulates, '[t]he contracting officer shall award the contract to the concern in question if the SBA issues a COC after receiving the referral. An SBA-certified concern shall not be required to meet any other requirements of responsibility. SBA COC's are conclusive with respect to all elements of responsibility of prospective small business contractors. Where SBA issues a COC, the contracting officer may decide not to award to that offeror for reasons unrelated to responsibility'.

[912] For a discussion, see Frederic T. Suss, 'Set-Asides and Certificates of Competency--Positive Programs for Small Business in Government Procurement' (1964) 29 Law & Contemp Probs 418.

Nevertheless, discretionary assessment methods also carry inherent risks, particularly regarding a lack of transparency that may facilitate abuse by contracting authorities.[913] To mitigate such risks, this approach requires enhanced disclosure obligations concerning qualification decisions. When sufficiently regulated, discretionary assessments may produce more effective results than the application of minimum requirements, as they provide a comprehensive view of economic operators' capabilities.[914] However, the discretionary approach incurs higher administrative costs and requires greater financial expertise from contracting officers to accurately assess bidders' financial capacity. While minimum standards offer greater transparency and predictability, a discretionary assessment may disadvantage SMEs, as contracting authorities may exhibit risk-averse preferences for larger businesses to minimise perceived financial exposure, as discussed in Chapter 3.[915]

Essentially, financial capacity assessments stem from contracting authorities' intention to ensure satisfactory contract performance by financially capable contractors. This approach aims to reduce the risk of default or underperformance resulting from insufficient financial resources. However, alternative mechanisms can ensure contract performance without imposing a rigid financial barrier on small bidders. For instance, under FAR 28.102, construction contracts exceeding USD 150,000 require performance and payment bonds from successful contractors, rather than bidders.[916] Performance bonds are usually included in the contract clauses, which take effect only after a contractor has been selected, thereby eliminating entry barriers at the bidding

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[913] Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 1196, para 12-18; also see Triantafyllou and Mardas (n 821) 146.
[914] Triantafyllou and Mardas (n 821) 152.
[915] See Chapter 3.
[916] 48 CFR § 28.103-4.

phase.[917] This approach facilitates SME participation whilst ensuring contracting authorities avoid financial losses from contractor non-performance. By mandating performance bonds for construction contracts exceeding specified thresholds, FAR 28.102 protects contracting officers against potential default or underperformance by contractors while avoiding excessively stringent criteria for determining responsibility. Performance bonds thus balance contractor reliability with broader SME access, fostering enhanced competition in the procurement market. This mechanism will be examined further in Section 5.2.3.

Beyond risk mitigation tools, the US FAR system also provides mechanisms to enhance the financial capacity of prospective contractors, such as the 'assignment of claims' under FAR Subpart 32.8, which permits contractors to use anticipated payments from a federal agency as collateral for a loan.[918] This facilitates contractors' access to credit from financial institutions while helping agencies avoid performance delays due to financing issues.[919] More importantly, this mechanism encourages companies to participate in government procurement, especially small businesses, by improving their access to financial resources. Under this arrangement, contractors may assign their right to contract payments directly to a bank as security for loans. The federal agency then pays the bank directly, with the bank remitting any surplus to the contractor after deducting loan principal and interest.[920]

In the EU, the assignment of claims is not explicitly addressed in EU public procurement directives, such as Directive 2014/24/EU. While contractors may assign claims under national law, such assignments do not enhance access to public

[917] 48 CFR § 28.103-4.
[918] 48 CFR § 32.8.
[919] ibid.
[920] 48 CFR § 32.8.

procurement opportunities, where adequate financial capacity must already be demonstrated at the bidding stage. As will be discussed in Section 5.2.4, Directive 2014/24/EU requires economic and financial standing to be assessed during the qualitative selection stage, prior to the evaluation of tenders.[921] Consequently, bidders cannot rely on the assignment of payment claims at this stage, since they do not yet know whether their tenders will be successful.[922]

5.2.1.3 Insolvency as an exclusion ground

A related issue to the financial capacity is whether a company in the insolvency process shall be excluded from a procurement process. Existing economic studies have shown that SMEs are more susceptible to bankruptcy or insolvency than large businesses.[923] SMEs fail in large numbers, partly due to the fact that they constitute the largest proportion of businesses, but also attributed to factors such as limited access to capital, a smaller workforce, and fewer resources compared with large businesses.[924] Thus, whether or not a potential bidder in the insolvency process will be excluded from a procurement procedure is particularly important for SMEs.

In the EU, insolvency or bankruptcy is listed as one of the exclusion grounds that can be referred to by contracting authorities to exclude an economic operator from the

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[921] Directive 2014/24/EU, art 58.

[922] See Section 5.2.3.1 for a case where a loan arrangement is required as a selection criterion.

[923] See Ronald Davis and others, *Micro, Small, and Medium Enterprise Insolvency: A Modular Approach* (Oxford University Press 2018); also see World Bank Group, *Report on the Treatment of MSME Insolvency* (World Bank, Washington, DC 2017) <https://hdl.handle.net/10986/26709> accessed 9 November 2024, 5.

[924] See Federico J. Díez and others, 'Insolvency Prospects Among Small-and-Medium-Sized Enterprises in Advanced Economies: Assessment and Policy Options' (IMF Staff Discussion Note SDN/2021/002, April 2021) <https://www.imf.org/en/Publications/Staff-Discussion-Notes/Issues/2021/03/25/Insolvency-Prospects-Among-Small-and-Medium-Sized-Enterprises-in-Advanced-Economies-50138> accessed 8 November 2024, 21.

procurement procedure.[925] According to Article 57(4)(b) Directive 2014/24/EU, Member States can choose to render it mandatory to exclude an economic operator that is in the insolvency proceedings or grant contracting authorities discretion to decide whether an economic operator in this situation shall be excluded.[926] Member States can also choose to provide opportunities for economic operators in insolvency proceedings. A Member State may require or provide the possibility that an economic operator will not be excluded if the contracting authority has established that the economic operator would be able to perform the contract.[927] Although a Member State can render this exclusion ground mandatory, contracting authorities still retain considerable discretion, as the criterion requires that 'the contracting authority has established' the economic operator's ability to perform the contract, rather than requiring the operator to provide evidence of such capability.[928] This amount of discretion given to contracting authorities raises the question of whether they would be willing to assess the capacity of an economic operator undergoing insolvency proceedings to perform a contract. Even if a contracting authority is willing to undertake such an assessment, the process would be inherently challenging. Economic operators in insolvency proceedings typically have multiple stakeholders,

[925] In the EU context, the term 'insolvency' is more often used than 'bankruptcy', for example, see Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) [2015] OJ L141/19. Article 57 (4) Directive 2014/24/EU used both terms to describe this exclusion ground and includes comprehensive coverage to accommodate potential differences in national laws among Member States. In the US, 'bankruptcy' is more often used than 'insolvency' in legislation, for example, see Bankruptcy Code, 11 USC § 101 et seq (2020).

[926] According to Article 57 (4) Directive 2014/24/EU, contracting authorities may exclude or may be required to exclude an economic operator from participation in a procurement procedure 'where the economic operator is bankrupt or is the subject of insolvency or winding-up proceedings, where its assets are being administrated by a liquidator or by the court, where it is in an arrangement with creditors, where its business activities are suspended or it is in any analogous situation arising from a similar procedure under national laws and regulations'. See Directive 2014/24/EU, art 57(4).

[927] ibid.

[928] Directive 2014/24/EU, art 57(4).

and their assets are subject to significantly greater uncertainty compared to firms not in insolvency. This heightened complexity complicates the evaluation of their ability to fulfil contractual obligations.

In the US, FAR does not regulate bankruptcy situations explicitly in the determination of responsibilities for prospective contractors. Based on bid protests decided by the GAO, initiating a bankruptcy proceeding does not necessarily result in a determination of non-responsibility.[929] Rather, it is considered one of the factors in the assessment of the financial capacity.[930] The GAO does not review affirmative responsibility determinations made by contracting officers, but limits its review to the process by which these determinations are made. For example, in case B-414748, the protestor argued that the awardee's involvement in ongoing bankruptcy litigation undermined their financial stability and should have led to a non-responsibility finding.[931] The GAO reviewed the determination process and concluded that the contracting officer had reasonably considered the bankruptcy litigation in the decision-making process, ultimately denying the protest.[932] Such cases highlight that being in a bankruptcy proceeding does not necessarily lead to an exclusion from the procurement procedure in the US FAR approach. This approach may offer benefits for SMEs in financial distress, enabling their continued participation in public procurement. The flexibility

[929] See GAO B-414748 (22 Aug 2017). For a discussion about this case, see Koprince McCall Pottroff LLC, Bankruptcy Pending, But Contractor Still Wins Award, <https://smallgovcon.com/gaobidprotests/bankruptcy-pending-but-contractor-still-wins-award/> accessed 11 November 2024.

[930] Cibinic, Nash and Yukins (n 848) 139.

[931] GAO B-414748 (n 929) 7.

[932] ibid. The contracting officer inquired with the awardee's current clients and confirmed that its pending bankruptcy litigation did not have impact on its contract performance. Also, based on the information from the Federal Awardee Performance and Integrity Information System, the awardee did not have a history of failing to pay its litigator. Thus, the GAO reasoned that the contracting officer reasonably considered the fact that the awardee was in a pending litigation.

afforded by the FAR reflects the understanding of the business lifecycle and the potential for recovery even during financial distress.[933] This could foster a more inclusive procurement environment where financial restructuring is not an immediate barrier to contract responsibility, thus encouraging SMEs to participate actively and seek recovery through procurement opportunities.

5.2.2 The assessment of past experience

In addition to financial capacity, technical capacity is a critical part of the qualification process in public procurement. When evaluating technical capacity, contracting authorities may require economic operators to have relevant past experiences as the means of proof for their technical capacity. Contracting authorities may impose three types of past experience requirements: a general requirement for relevant experience on similar projects in either the public or private sector; a specific requirement for experience in public procurement; and a requirement for prior experience with the same or specific contracting authorities. While the evaluation of past experience seeks to ensure reliability and minimise performance risks, it presents particular challenges for SMEs, especially newly established firms.[934] By their very nature, these firms often

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[933] The impact of bankruptcy on enterprises is widely discussed in bankruptcy law literature, for example, see Joseph E Stiglitz, 'Bankruptcy Laws: Basic Economic Principles' in Stijn Claessens, Simeon Djankov, and Ashoka Mody (eds), *Resolution of Financial Distress: An International Perspective on the Design of Bankruptcy Laws* (The World Bank 2001) 1, 2.

[934] The term 'newly established firms' refer to firms that are newly established without experiences in public procurement and limited experience in the private market. It differs from the term 'startups'. There is no legal definition of startups in either the EU or the US, and the usage of 'startups' varies widely. The report European Startup Monitor 2019/2020 refers to startups as companies younger than 10 years, and they have to have an innovative product or model and aim to scale up in size. See European Startup Monitor, *European Startup Monitor 2019 Report* (2020) 4 <https://www.europeanstartupmonitor2019.eu/EuropeanStartupMonitor2019_2020_21_02_2020-1.pdf accessed 14 November 2024> accessed 28 November 2024. In a UK report regarding innovation finance definitions, it refers to startups as companies that have been operating for less than two years, and are independently owned. See UK Government, 'Innovation Finance Definitions' (gov.uk, 8 June

lack an extensive portfolio of completed projects, leaving them at a distinct disadvantage when compared with more established competitors. In this section, the impacts of the different types of past experience requirements on SMEs, especially newly established businesses, will be explored. By analysing the relevant rules in the EU and the US, this section highlights the need for more inclusive approaches that balance the goal of ensuring technical reliability with the broader objective of fostering SME participation in public procurement.

5.2.2.1 Past experience as a means of proof – the EU approach

Under the old Directive 2004/18/EC, Article 48 specified the types of evidence that can be used to demonstrate technical capacity, such as a list of works accompanied by certificates of satisfactory execution completed within the past five years for construction contracts.[935] Directive 2014/24/EU largely retains this framework in Annex XII, continuing to emphasise past experience as a means of proving technical capacity.[936] Compared with Article 48 (2) (a) Directive 2004/18/EC, ANNEX XII Part II (2) Directive 2014/24/EU added that, when necessary to ensure an adequate level of competition, contracting authorities may also consider evidence of relevant works

2023) <https://www.gov.uk/government/publications/letter-to-the-prime-minister-on-investment-in-innovative-science-and-technology-companies/innovation-finance-definitions-html> accessed 28 November 2024. In the US, the usage of 'startups' is very limited, and 'small business' is more widely used in legal texts and policies. Thus, in this research, the term 'newly established businesses' will be used to refer to economic operators that are newly established with limited or no experience in public procurement, rather than 'startups'.

[935] For goods and services contracts, Article 48(2)(a) Directive 2004/18/EC allows contracting authorities to consider economic operators' past experience in working with a private purchaser. See Directive 2004/18/EC, art 48(2)(a); also see Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 370; Risvig Hamer (n 856) 654.

[936] Directive 2014/24/EU, art 58(4).

completed more than five years ago.[937] This provision implies that contracting authorities are not obliged to account for experience beyond five years unless it would enhance competition in the procurement process. While this adjustment demonstrates that legislators carefully consider the potential impact of past experience requirements on competition, it may still create challenges for SMEs.[938]

Usually, large undertakings may find it easier to produce extensive lists of relevant works completed within the prescribed period than SMEs. However, the reliance on such lists may not always reflect the requisite levels of specialisation or productivity in relation to the subject matter of the contract.[939] An SME with a high degree of specialisation in a particular area may, in some cases, outperform a larger, less specialised firm in meeting the specific demands of the contracting authority.[940] To address this potential disparity, it is important that contracting authorities assess such evidence in accordance with the principle of proportionality, as articulated in Article 58(1) of Directive 2014/24/EU, requiring that selection criteria remain 'related and proportionate to the subject matter of the contract.'[941] In this context, it is further argued that not only should the selection criteria proposed by contracting authorities comply with the principle of proportionality, but the evidence required must also adhere to this standard. This approach ensures that the selection process is appropriately

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[937] Directive 2004/18/EC, art 48(2)(a); Directive 2014/24/EU, annex XII Part II (2). Even under the old Directive, contracting authorities may consider an economic operator's experience from more than five years ago. See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 370.

[938] See European Commission, *Public Procurement for Innovation – Brochure for Public Buyers* (Publication Office of the European Union, 2023) <https://single-market-economy.ec.europa.eu/system/files/202302/Public%20procurement%20for%20innovation%20-%20brochure%20for%20public%20buyers.pdf> accessed 14 November 2024. This brochure encourages contracting authorities to use selection criteria that do not require bidders to have been in business for many years, such as qualifications, instead of certificates of satisfactory execution of contracts.

[939] Triantafyllou and Mardas (n 821) 153.

[940] ibid 153.

[941] Directive 2014/24/EU, art 58(1).

tailored to the contract in question and does not discriminate against SMEs or create barriers to their participation.

Under Article 48 (2) (a) Directive 2004/18/EC and Article 60 (4) Directive 2014/24/EU, it is beyond doubt that past experience can be utilised as evidence of the economic operators' technical abilities.[942] Both these provisions specify that if the past experience is in public procurement, the evidence shall be certificates of satisfactory execution issued by the competent authority; if in the private sector, the evidence may be the purchaser's certification or a declaration by the economic operator.[943] What remains doubtful is whether a contracting authority can establish past experience in public procurement as a selection criterion, in which case, past experience is no longer just a means of proof for technical abilities, but a selection criterion itself, similar to a minimum turnover requirement.[944]

As discussed in the previous subsection, any selection criterion shall be assessed whether it is 'related and proportionate to the subject matter of the contract'.[945] As mentioned at the beginning of this section, contracting authorities may establish three types of requirements regarding bidders' past experiences: experiences with specific public contracting authorities, with any public authorities, or experience with any purchaser (including private entities). Among them, requiring past experiences with

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[942] Directive 2004/18/EC, art 48 (2) (a); Directive 2014/24/EU, annex XII Part II (2). Both these provisions allow contracting authorities to consider economic operators' past experience in public procurement. For works contracts, it states that 'the competent authority shall submit these certificates to the contracting authority direct', when appropriate. For supplies and services contracts, the wording clearly states that experiences in either public or private might be considered, and it indicates that the means of proof differ in these two situations.

[943] ibid.

[944] If not a binary approach but a scoring approach, contracting authorities may grant more points to an economic operator who has experience in public procurement compared with one only with experience in the private market.

[945] Directive 2014/24/EU, art 58(1).

specific contracting authorities might be disproportionate as it limits the competition among their incumbent and prior contractors, and excludes other economic operators. This is detrimental to the diversity of suppliers, as it prohibits new entrants from competing for the contract. Similarly, if the past experience requirement is limited to a few contracting authorities in a specific Member State, this might be regarded as discriminatory against economic operators from other Member States, as domestic economic operators potentially have had more chances to work with domestic contracting authorities.

It is more complex when a contracting authority requires economic operators to have a certain amount of past experience in public procurement. For example, in *Commission v Italy* C-362/90, an Italian contracting authority imposed a requirement that 50 per cent of the suppliers' past deliveries must have been made to public authorities.[946] In that case, economic operators who have less than 50 per cent of their past deliveries to public authorities were not qualified to submit tenders in this procurement procedure.[947] Italy defended this requirement, arguing that a proven track record in public procurement offered a stronger guarantee of reliability than contracts with private purchasers.[948] However, Advocate General Lenz (AG Lenz) countered that this requirement constituted an 'exclusionary criterion', as it excludes tenderers who did not meet this past experience requirement, rather than serving as an assessment of the evidence (means of proof).[949] AG Lenz noted that the distinction between references to public and private entities primarily concerned the means of

[946] Opinion of Advocate General, Case C-362/90 *Commission v Italy* [1992] European Court Reports I-2353. See Arrowsmith, *The Law of Public and Utilities Procurement* vol 1 (n 57) 1224, para 12-50.
[947] Case C-362/90 *Commission v Italy* [1992] European Court Reports I-02353.
[948] ibid.
[949] Case C-362/90 (n 109).

proof, and this exclusionary criterion was clearly not provided for in Directive 77/62/EEC. [950] Although this is an old ruling under the Directive 77/62/EEC, the provisions regarding past experience in public procurement and the private market were kept in ANNEX XII Part II (2) Directive 2014/24/EU, which indicates that experience in public procurement can serve as evidence of technical abilities, but not as a qualitative selection criterion.[951]

In a more recent case, *Evropaïki Dynamiki v Commission* T-59/05, the applicant was a tenderer who was not awarded the contract and argued that it had more experience supplying the contracting authority (the European Commission) and other similar contracting authorities (other European institutions) in the past.[952] The Commission argued that past experience was not among the award criteria and thus not considered in the tender evaluation.[953] The CJEU upheld the Commission's argument and stated that considering an economic operator's past experience working with the same contracting authority or similar public authorities is not compliant with the principle of equal treatment and non-discrimination.[954] Although this case centred around whether past experience in public procurement can be considered in award criteria, it is beyond doubt that the principles of equal treatment and non-discrimination shall also be respected in the selection criteria.[955] Thus, it can be inferred that requiring economic

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[950] ibid; Council Directive 77/62/EEC of 21 December 1976 coordinating procedures for the award of public supply contracts [1977] OJ L13/1, art 23(1)(a). The court did not assess whether the past experience in public procurement requirements is appropriate due to the fact that the alleged infringement no longer existed by the deadline in the reasoned opinion. Thus, the court rendered the action inadmissible.

[951] Directive 2014/24/EU, annex XII Part II (2).

[952] Case T-59/05 *Evropaïki Dynamiki v Commission of the European Communities* [2010] ECR II-573, para 104.

[953] ibid.

[954] Case T-59/05 (n 952).

[955] Based on Article 18(1) Directive 2014/24/EU, principles of equal treatment and non-discrimination shall be upheld at any stage of a procurement procedure. See Directive 2014/24/EU, art 18(1).

operators to have worked with public authorities is also not consistent with the principle of equal treatment. This can also be argued from the competition perspective, as Article 18 (1) Directive 2014/24/EU stipulates that 'the design of the procurement shall not be made with the intention of […] artificially narrowing competition'.[956] Competition is artificially narrowed when a procurement procedure is designed with the intention to unduly favour or disadvantage certain economic operators.[957]

In *Jema Energy v Joint Undertaking Fusion for Energy* T-668/15, the CJEU mentioned that setting exceedingly demanding qualitative selection criteria could be regarded as artificially narrowing down competition.[958] Setting exceedingly demanding criteria may, in effect, reserve a contract for large economic operators, who would be the only ones able to satisfy such criteria.[959] Requiring past experience in public procurement favours those incumbent or previous contractors, and discriminates against economic operators who do not have experience in public procurement, which artificially narrows down competition only among incumbent or previous contractors.[960] This also applies

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[956] Directive 2014/24/EU, art 18(1). Sanchez-Graells has the same argument, that past experience requirements shall not distort competition in the market. See Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 307.

[957] Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 307.

[958] Case T-668/15. The judgment of this case is only available in Spanish and French, the author used Google Translate to translate the judgment into English. For a discussion of this case from the competition perspective, see Albert Sanchez Graells, 'Mixed views on General Court decision concerning claim of "artificial narrowing of competition" through too strict procurement selection requirements (T-668/15)', (How to Crack a Nut, November 14 2017) <https://www.howtocrackanut.com/blog/2017/11/14/general-court-decision-concerning-claim-of-artificial-narrowing-of-competition-through-too-strict-procurement-requirements-t-66815> accessed 05 December 2024.

[959] In this case, the contracting authority established a selection criterion that tenders should demonstrate an example of delivery of specific types of equipment in the past 5 years before the tender. The applicant was rejected as it could not meet this criterion and it challenged the proportionality of this requirement, and it argued that it also artificially narrowed competition. The Court reviewed this selection criterion and decided that it is transparent, and consistent with the principle of equal treatment. The Court did not discuss this criterion from a competition perspective but simply pointing out that exceedingly demanding selection criteria may artificially narrow down competition.

[960] Sanchez Graells has a similar opninion that such requirements have an effect of entrenching incumbent suppliers. See Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62)

to adding points for those economic operators who satisfy this requirement or detracting points for those who do not satisfy this requirement in the shortlisting process, which will be discussed in Section 5.3.[961]

In summary, in the EU, references to contracts performed in the past are intended to serve as evidence of an economic operator's technical capacity, rather than as a qualification criterion itself. Treating such references as a selection criterion can significantly discourage economic operators without past experience in public procurement, particularly newly established firms, which are predominantly SMEs. Therefore, if contracting authorities require specific past experience in public procurement, they should clarify that references to private contracts demonstrating an equivalent level of technical capacity will also be considered.

5.2.2.2 Satisfactory performances as a standard – the US FAR approach

Although different, a similar requirement to past experiences is a satisfactory record of contract performance.[962] In the US, this requirement has been a component of determining the responsibility of prospective contractors since 1984, when the FAR was promulgated.[963] FAR 9.104-1(c) requires that prospective contractors must have

309; also see Jeffrey V Butler and others, 'Past Performance and Entry in Procurement: An Experimental Investigation' (2020) 173 Journal of Economic Behavior & Organization 179.

[961] The only exception is a deficiency of past performance, which is established as an exclusion ground in Article 57(4)(g) Directive 2014/24/EU.

[962] When it comes to a past performance requirement, it usually refers to past performance records of public contracts, because it is more feasible for contracting authorities to get access to performance records for public contracts than contracts with private entities. Apart from the US evidence in the FAR, this can also be illustrated by Article 48(2) (a) Directive 2004/18/EC and ANNEX XII Part II (2) Directive 2014/24/EU, which mention certificates of satisfaction only in public contracts context. See Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 309.

[963] Department of Defense, General Service Administration, National Aeronautics & Space Administration, 'Establishing the Federal Acquisition Regulation' (Part 2 of 12), 48 Federal Register 42102 (September 19, 1983).

a ‘satisfactory performance record’.[964] Thus, all contracting officers are required to check the performance records of prospective contractors in the past. The practicality and efficiency of checking this requirement rely on an existing system where past performance records of contractors can be examined. Under FAR 42.15, federal agencies are generally required to record the performance of contractors for contracts with a value higher than USD 150,000 annually or at the time when a contract is completed on the Contractor Performance Assessment Reporting System (CPARS).[965] Federal agencies and contracting officers rely on CPARS to assess and review the past performance of prospective contractors when determining their responsibility.[966] Although CPARS is developed to facilitate contracting officers in examining prospective contractors’ past performance, this is only restricted to their experience in federal procurement, which implies their experience in the private market is not taken into account.

Under FAR 9.104-1 (c), having a satisfactory record of past performance is a general standard for responsibility determination itself, rather than as evidence for one’s technical capacity.[967] *Prima facie*, this is a more demanding requirement that excludes prospective contractors without experience in federal procurement. However, it is also clearly indicated that prospective contractors shall not be determined non-responsible solely based on a lack of relevant performance history.[968] Contracting officers shall

[964] 48 CFR § 9.104-1(c).

[965] 48 CFR § 42.1501 (b).

[966] ibid. Apart from the CPARS, contracting officers can also check a prospective contractor’ responsibility on SAM.gov under the ‘Responsibility/Qualification’ category of performance data.

[967] 48 CFR § 9.104-1 (c).

[968] The terms ‘nonresponsibility’ are used in the FAR to refer to a negative determination of responsibility. Although there were worries that many small businesses do not possess past experience in federal procurement, GAO researched a number of procurement decisions and found out only one offeror did not have experience in federal procurement, most of the bidders did. However, this does not provide a

assess other evidence to make the determination of responsibility. Similarly, in France, the 2006 Public Procurement Code explicitly prohibited contracting authorities from excluding bidders solely for lacking experience in public procurement, recognising that such a rule would unfairly disadvantage SMEs and new entrants.[969] In the currently effective 2019 Public Procurement Code, Article L2142-1 addresses participation conditions, emphasising the principle of proportionality.[970] While the Code itself does not explicitly reiterate this point, Article R2142-14 of Decree No. 2018-1075, a regulation issued to implement the Code, explicitly maintains the stance that a lack of references for similar contracts cannot, by itself, justify an elimination of a candidate in the qualification process.[971] This approach aims to provide a level playing field, allowing bidders without prior experience the opportunity to demonstrate their technical capacity in other ways. In practice, this rule does not motivate contracting officers to check past experiences because even if a bidder does not have past experience, the contracting officer has to use other evidence to assess their technical ability since they cannot exclude them solely based on a lack of experience in public procurement.[972] As for other criteria, contracting authorities can refrain from evaluating a tenderer as long as it does not satisfy that criterion, for example, a minimum turnover requirement. Those criteria are exclusionary requirements, whereas past experience

convincing picture as those businesses without experience in procurement might not be motivated to submit an offer, and they were not included in GAO's research. See Butler et al. (n 960) 180.

[969] CPM 2006, art 52. For a discussion on this rule, see Lichère (n 456) 53. This approach was maintained in Article 44 of the 2016 Decree No. 2016-360, which reiterated that while purchasers could require a sufficient level of experience, the lack of references for similar public contracts alone could not justify excluding a candidate. See *Décret n° 2016-360 du 25 mars 2016 relatif aux marchés publics, art 44.*

[970] Article L2142-1 CCP 2019 stipulates briefly about 'conditions of participation' only reiterating the principle of proportionality.

[971] Article R2142-14 CCP 2019 reiterates this rule that a lack of references in past experience of contracts in the same nature may not, in itself, justify the elimination of a candidate.

[972] Lichère (n 456) 53-54. The French approach also provides bidders with an opportunity to prove that they have improved their ability even if they have a bad performance record in the past.

is not one of them in both the US FAR and the EU public procurement rules. In the US FAR, the only exception to this rule is when a contracting officer adds a satisfactory performance record as a special standard, especially when a particular acquisition requires unusual expertise that can be demonstrated by a relevant performance history.[973]

As mentioned earlier, beyond the mandatory general standards established in FAR 9.104-1, contracting officers may also establish special standards if unusual expertise or specialised facilities are needed for a procurement demand.[974] When special standards are included in a procurement procedure, prospective contractors are not only required to satisfy the general standards but also the special standards. In practice, these special standards are termed 'definitive responsibility criteria'.[975]

If specific experiences are required in the determination of responsibility, small businesses with less experience or newly established businesses may be at a disadvantage. As discussed in Section 5.2.1.2, when a small business is deemed nonresponsible, the contracting officer must refer this matter to the SBA. If the SBA certifies that a small business satisfies general standards for responsibility, a COC will be issued to the small business. This protection scheme receives criticism from contracting officers, arguing that COCs issued by the SBA undermine their authority and discretion in determining the capacity of prospective contractors.[976] Contracting officers believe that the SBA 'consistently issues COCs for all matters referred to them',

[973] 48 CFR § 9.104-1 (c) and FAR 9.104-2.

[974] See 48 CFR § 9.104-2.

[975] The GAO defines DRCs as specific and objective standards established by an agency for use in a particular procurement to measure a bidder's ability to perform the contract. See GAO, B-271750 (July 24, 1996, 96-2 CPD ¶ 37). The SBA does not have to evaluate if a small business meets special standards to issue a COC.

[976] Suss (n 912) 433.

which, in effect, undermines the effectiveness of the general standards of responsibility.[977] The potential conflict is more obvious when a special standard for the determination of responsibility is involved. The question arises whether the SBA can certify that a small business satisfies the special standards when issuing a COC.

In a specific case, *Rukbat*, the purchasing agency, proposed a special standard based on a particular past experience in the procurement procedure.[978] The lowest bidder was a small business, which had satisfied the general standards of responsibility but did not meet the special standard, and it did not receive an affirmative determination of responsibility.[979] Since this is a matter related to a small business, it was referred to the SBA. The SBA declined to issue a COC and agreed with the contracting officer that the small business did not meet the special standard to be determined responsible; thus, the contract was awarded to the next lowest bidder, who was found responsible.[980] In a similar case, the purchasing agency required that prospective contractors provide two projects during which they repaired stonework of a certain size in a specific environment.[981] The lowest bidder was a small business and showed a successful performance history and expertise, but it failed to meet this special standard. The SBA examined this matter by requesting more information from the small business and issued the COC, however, without determining if the special standard is met.[982] As a result, the contract was awarded to this small business, and

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[977] See Jessica M Kidd and Nicole V Franing, *Effectiveness of Definitive Responsibility Criteria in Sealed Bidding for Heavy Construction Projects* (Naval Postgraduate School 2019) <https://www.nps.edu> accessed 14 November 2024.

[978] ibid. The purchasing agency required that prospective contractors demonstrate that it had experience in dredging in a tidally influenced environment and disposing of the dredged material using open ocean placement.

[979] Kidd and Franing (n 977) 54.

[980] ibid.

[981] Kidd and Franing (n 977) 55.

[982] ibid.

it successfully performed the contract.[983] From these two cases, it is clear that the SBA has substantial power in determining whether a small business should be held responsible or not.[984] This compensates for the fact that small businesses may fail to satisfy a satisfactory performance history in federal procurement as one of the general standards for responsibility, or when purchasing agencies may require specific experience as a special standard.

Apart from considering past performance history positively in the determination of responsibility, FAR 9.104-3 (b) also regulates that if a prospective contractor has a recent deficient performance in a public contract, it might be presumed non-responsible, unless the contracting officer decides that the circumstance was beyond the contractor's control.[985] Overall, contracting officers retain substantial discretion to determine how the information from past performances will be used.[986]

In summary, the use of past experience or past performance criteria in the qualification process in public procurement as part of the qualification process can present significant barriers for newly established businesses, which are mainly SMEs.[987] In the EU, it largely depends on national public procurement law and contracting authorities

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[983] Kidd and Franing (n 977) 55.

[984] Just as the GAO does not review the responsibility determination of contracting officers, the GAO does not review SBA's COC decisions either. The GAO can only review if there is a serious breach of the rules in the determination of the COC, based on the SBA's regulation in determining COCs. 4 CFR § 21.5 (b)(2) regulates that the GAO will not review the insurance of or refusal to issue certificates of competence by the SBA unless the protester is able to show evidence that the SBA failed to follow its regulations or failed to consider vital information. For SBA's regulation on COC, see 13 CFR § 125.5.

[985] 48 CFR § 9.104-3 (b). This is similar to the EU approach, where an economic operator might be excluded from a procurement procedure if it has a persistent deficiency in contract performance in public contracts it performed in the past. A contracting authority may exclude an economic operator from a procurement procedure if it has demonstrated significant or persistent deficiencies in the performance of a substantive requirement under a prior public contract, a prior contract with a contracting entity or a prior concession contract. Such deficiencies must have resulted in the early termination of the contract, the imposition of damages, or similar results. See Directive 2014/24/EU, art 57 (4)(g).

[986] Cibinic, Nash, and Yukins (n 848) 146.

[987] US SBA, 'Frequently Asked Questions' (n 4).

to ensure that the experience or performance requirement is proportionate, a good example is the French public procurement rules, which explicitly stipulate that contracting authorities shall not refrain from evaluating one bidder's qualification solely based on a lack of past experience in public procurement. As discussed in Section 5.2.2.1, past experience in public procurement shall be utilised as a means of proof for technical capacity, rather than a selection criterion in itself. Ensuring that requirements are proportionate and including private sector experience is key to creating opportunities for SMEs. In the US, a satisfactory performance record is a general standard for responsibility determination, but it is not an exclusionary requirement, meaning that contracting officers cannot exclude a prospective contractor simply due to a lack of a satisfactory performance record. While performance-based assessments can improve contractor reliability, they should not be used to exclude newly established or inexperienced bidders, and this would also undermine fair competition and diversity of suppliers.

5.2.3 Financial guarantees required by contracting authorities

Public procurement procedures often involve multiple types of financial guarantees, serving different purposes at various stages of the process. This section focuses on guarantees required by contracting authorities at the bidding stage. Such guarantees aim to ensure compliance and mitigate risks associated with the bidding process.[988] However, SMEs often face disadvantages in this respect: lacking established banking

[988] For example, contracting authorities may require bidders to provide a guarantee ensuring that they will not retract their offer if awarded the contract; failure to honour the offer may result in a financial penalty. See Robert H. Rumizen & Milton J. Socolar, 'Bid Guarantees in Federal Procurement' (1962) 18 Mil L Rev 99, 100.

relationships or sufficient collateral, they may struggle to obtain the guarantees demanded by contracting authorities, making this requirement a barrier to their participation.[989]

In competitive bidding, especially where bidders are unaware of other bidders' prices, there exists a risk of the selected bidder reneging on their offer.[990] To safeguard the integrity of the procedure and ensure the execution of the contract under the agreed terms, contracting authorities may require bidders to submit financial guarantees, which are termed bid guarantees.[991] These bid guarantees protect contracting authorities against additional costs arising from a bidder's withdrawal, particularly where the contract must be retendered.[992] Under a bid guarantee, a withdrawing tenderer compensates the contracting authority for the price difference between the lowest bid and the alternative offer selected.[993]

While bid guarantees reduce the risk of withdrawal, they increase costs for economic operators, potentially discouraging SMEs from participating in procurement procedures.[994] This reduction in competition may ultimately increase procurement costs for contracting authorities, not only due to a lack of competition, but also as bidders often factor the expense of acquiring guarantees into their offered prices.[995] Consequently, based on the principle of proportionality, bid guarantee requirement

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[989] See Chapter 3, Section 3.3.3; also see DCED (n 42) 18.

[990] Donavan Bezer, 'The Inadequacy of Surety Bid Bonds in Public Construction Contracting' (2010) 40 Public Contract Law Journal 87.

[991] ibid.

[992] Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 326.

[993] ibid.

[994] Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 326.

[995] Andreas R Engel and others, 'Managing Risky Bids' in Nicola Dimitri, Gustavo Piga and Giancarlo Spagnolo (eds), *Handbook of Procurement* (Cambridge University Press 2006) 334.

shall be evaluated against the actual risks of defaults and the potential damages.[996] For instance, in complex service contracts or negotiated procedures, where significant time and effort are invested in selecting the best offer, a bid guarantee may be justified. Conversely, in standardised goods procurement, where the withdrawal of the best tenderer may not result in substantial damages, requiring a bid guarantee may be unnecessary.

5.2.3.1 Financial guarantees in procurement procedures in the EU

In the EU, Directive 2014/24/EU does not explicitly regulate bid guarantees, although Annex IX.2(f) stipulates that in restricted and negotiated procedures, contracting authorities shall include information in the invitation to tender regarding 'economic and technical conditions, financial guarantees and information required from economic operators' in the contract notice.[997] This provision ensures the disclosure of relevant information, leaving the decision of whether to require financial guarantees at the discretion of the contracting authority. The wording, however, lacks clarity regarding the type of guarantees it encompasses.[998]

A notable case illustrating the application of financial guarantees is *INGSTEEL and Metrostav C-76/16*. In this case, the contracting authority required bidders to provide a bank statement (such as a loan agreement or credit facility agreement), ensuring the availability of EUR 3 million in financial resources to secure a performance bond upon

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[996] Sanchez-Graells also argues that bid guarantees should only be required when there is clear evidence of potential risks in contract performance. Sanchez Graells, *Public Procurement and the EU Competition Rules* (n 62) 327.

[997] Directive 2014/24/EU, annex IX.2(f)

[998] The EU Directives do not regulate performance bonds. In the US FAR, a performance bond is to ensure that when the contractor defaults, a bank can compensate the contracting authority for the loss due to the default. See 48 CFR § 28.001.

award.[999] This financial guarantee, distinct from traditional bid guarantees or performance bonds, was a preliminary financial arrangement to enable the bidder to secure a performance bond if it is awarded the contract. On the one hand, this requirement aims to assess the economic and financial standing of bidders; on the other hand, it requires bidders to provide a performance bond once their tender is selected. The unsuccessful bidder's failure to submit the required statement led to its exclusion, despite providing alternative evidence of financial capacity.[1000]

The main question referred by the Slovak Republic Supreme Court to the European Court of Justice (ECJ) was whether such guarantees were compatible with Article 47 (1)(a) and (4) of Directive 2004/18/EC, which sets rules for assessing bidders' economic and financial standing.[1001] Advocate General Campos Sánchez-Bordona (AG Campos) delivered an opinion that financial guarantees as selection criteria are compatible with Directive 2004/18/EC, as contracting authorities are given a certain degree of discretion to decide on the proof of bidders' economic and financial standing.[1002] AG Campos argues that Articles 44 and 47 Directive 2004/24/EU imply that evidence of economic and financial standing should refer to the duration of contract performance.[1003] The Court observed that Article 47 Directive 2004/18/EC did not explicitly permit contracting authorities to require a bidder to have access to the

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[999] Opinion of AG Campos Sánchez-Bordona in Case C-76/16 *INGSTEEL and Metrostav* [2017] ECLI:EU:C:2017:221, 15.

[1000] Case C-76/16 *INGSTEEL and Metrostav* [2017] ECLI:EU:C:2017:549, para 17-18. The unsuccessful bidder claimed that it was impossible to obtain a statement from a bank to grant it credit in the specified amount. It provided a bank statement showing that it had EUR 5 million in its bank account and also a sworn statement that it would keep EUR 3 million during the contract performance period. The unsuccessful bidder brought an action to the regional court to seek annulment of the decision to exclude it from the tendering procedure.

[1001] Opinion of AG Campos (n 999) para 22 (1).

[1002] ibid, para 41.

[1003] Opinion of AG Campos (n 999) para 44.

resources needed for contract performance throughout the contract's duration.[1004] However, the Court concurred with AG Campos that the contracting authority's assessment of a tenderer's economic and financial standing in a procurement procedure is intended to assure that the successful tenderer will have access to the resources relied upon for the entirety of the contract period.[1005] Nevertheless, it emphasised that it is the responsibility of the referring court to assess whether the 'extent of information and the competence' required by the contracting authority was related and proportionate to the subject matter of the contract, and whether the evidence submitted by the tenderer was sufficient to meet the requirement.[1006]

Critically, Sanchez Graells contends that the qualitative selection process serves for contracting authorities to evaluate information submitted by bidders and is not intended as a mechanism by which contracting authorities can secure financial rights for themselves.[1007] This thesis concurs with Sanchez Graells's argument. Firstly, neither Article 47 Directive 2004/18/EC nor Article 58 Directive 2014/24/EU suggests that selection criteria extend to assessing bidders' financial capacity over the period of contract performance.[1008] In the qualitative selection stage, both exclusion grounds and selection criteria are applied based on information relating to bidders' past operations, not their future performance. For instance, contracting authorities may verify whether bidders have duly paid taxes in the past, but cannot require them to

[1004] Case C-76/16 (n 1000) para 37.
[1005] ibid.
[1006] Case C-76/16 (n 1000) para 46. The referring court annulled the decisions made by the contracting authority. See Supreme Court of the Slovak Republic, *INGSTEEL and Metrostav v. Úrad pre verejné obstarávanie* [2017], <https://www.nsud.sk/data/att/c80/563819.e0d580.pdf> accessed 05 December 2024 para 76.
[1007] Supreme Court of the Slovak Republic (n 1006) para 76.
[1008] ibid.

make tax payments during the contract performance phase.[1009] It is not only technically challenging but also commercially unreasonable to extend the application of selection criteria to the contract performance stage. The contractor may, for example, subcontract parts of the contract, thereby reducing the financial resources needed to perform the contract independently. Imposing fixed financial capacity requirements throughout the performance period, regardless of the contractor's actual needs emerging during performance, is not a proportionate approach. However, such requirements may be included as contract clauses binding the successful contractor, rather than being imposed on all bidders at the selection stage.[1010]

Secondly, it is technically difficult for contracting authorities to ascertain whether a bidder maintains the same level of financial resources throughout the contracting performance period as at the time of the award. In *INGSTEEL and Metrostav C-76/16*, the contracting authority employed a special financial arrangement to ensure bidders' financial capacity during contract performance.[1011] This arrangement, however, was not commonly used in the commercial market.[1012] After ECJ's preliminary ruling, the referring court noted that the 'loan guarantee agreement' at issue was not legally defined, and that the bank involved did not accept the concept of this 'loan guarantee

[1009] Directive 2014/24/EU, art 57(2).

[1010] Case C-76/16 (n 1000). The European Commission argued that such financial requirement covering the contract performance period shall be evaluated as a contract clause, under Article 26 Directive 2004/18/EC. Sanchez Graells agrees with the Commission on this point, see Albert Sanchez-Graells, 'ECJ Allows Contracting Authorities to Require Performance Bonds as Selection Criteria (C-76/16)' (How to Crack a Nut, 17 July 2017) <https://www.howtocrackanut.com/blog/2017/7/17/ecj-allows-contracting-authorities-to-require-performance-bonds-as-selection-criteria-c-7616> 08 December 2024.

[1011] Supreme Court of the Slovak Republic (n 1006) para 83.

[1012] ibid.

agreement'.[1013] Moreover, banks seldom provide statements guaranteeing a loan to ensure contract performance before the contract is awarded.[1014]

Finally, requirements for financial guarantees, whether in the form of loan arrangements or bank guarantees, tend to restrict competition. In particular, they disproportionately discourage the participation of SMEs, which face greater obstacles in obtaining such guarantees compared with large businesses.[1015] In fact, in *INGSTEEL and Metrostav C-76/16*, only one tenderer satisfied the financial guarantee requirement, resulting in that tenderer being awarded the contract and effectively eliminating competition at the evaluation stage.[1016]

In conclusion, while the EU public procurement rules do not explicitly regulate financial guarantees, such requirements set by contracting authorities must comply with Article 18 (1) Directive 2014/24/EU, namely the principles of equal treatment and non-discrimination. Any requirement must also be transparent and proportionate and not designed to artificially narrow competition.[1017] As demonstrated in *INGSTEEL and Metrostav C-76/16,* the application of the special financial guarantee led to only one tenderer meeting the requirement, thereby eliminating competition during the tender evaluation.[1018] More specifically, such requirements pose significant difficulties for

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[1013] Supreme Court of the Slovak Republic (n 1006) para 77.

[1014] ibid para 73.

[1015] On this point, Sanchez Graells argues that the financial guarantee requirements shall be subject to the principle of competition established in Article 18 (1) Directive 2014/24/EU, namely, if these requirements constitute artificial narrowing of competition. See Albert Sanchez-Graells, 'Can a Requirement to Furnish Financial Guarantees (Performance Bonds) Be Considered a Selection Criterion Based on Economic and Financial Standing (C-76/16)?' (How to Crack a Nut, 23 March 2017) < https://www.howtocrackanut.com/blog/2017/3/23/can-a-requirement-to-furnish-financial-guarantees-performance-bonds-be-considered-a-selection-criterion-based-on-economic-and-financial-standing-c-7616> accessed 05 December 2024.

[1016] Case C-76/16 (n 1000).

[1017] Directive 2014/24/EU, art 18(1).

[1018] Case C-76/16 (n 1000).

SMEs, undermining one of the intended objectives of Directive 2014/24/EU, which is to facilitate SME participation in public procurement markets.[1019]

5.2.3.2 Bid guarantees and performance bonds in the US FAR

In contrast to the EU approach, which leaves decisions on financial guarantees to the discretion of Member States and contracting authorities, the US FAR prescribes requirements for bid guarantees and performance bonds. Consequently, contracting officers have limited discretion regarding the imposition of such requirements. Bid guarantees serve as a form of financial security, ensuring that bidders do not withdraw their offers within the period specified for acceptance and that they will execute the contract and furnish the required bonds if awarded.[1020] These required bonds generally include both performance bonds, which safeguard the government against a contractor's failure to meet contractual obligations, and payment bonds, which ensure that subcontractors and suppliers are properly remunerated.[1021]

FAR 28.101-1(a) explicitly states that contracting officers 'shall not require a bid guarantee unless a performance bond or both a performance bond and payment bond is also required.'[1022] This provision demonstrates the limited discretion agencies have in imposing bid guarantee requirements. Moreover, where performance and payment

[1019] Directive 2014/24/EU, recital 2.

[1020] 48 CFR § 28.001. It also defines that a bond is a written instrument executed by a bidder or contractor, and a surety company, to assure fulfilment of the bidder or contractor's obligations to the contracting authority. If the obligation of the bidder or contractor is not met, the bond assures payment, to the extent specified, of any loss sustained by the contracting authority.

[1021] Performance bonds ensure the performance and fulfilment of the contractor's obligations under a contract. Payment bonds ensure payments to subcontractors and suppliers after performing the contract. See 48 CFR § 28.001. Under 48 CFR § 28.102-1, performance bonds are obligatory for construction contracts with a value exceeding USD 150,000.

[1022] 48 CFR § 28.101-1 (a).

bonds are mandated, a bid guarantee must also be required unless doing so would not be in the best interest of governments in a specific acquisition.[1023] Performance and payment bonds are required for construction contracts exceeding USD 150,000, as established in the Miller Act.[1024] For non-construction contracts, agencies shall not require performance and payment bonds unless necessary to safeguard the government's interests.[1025]

The detailed regulation on bid guarantees and performance bonds is designed to protect contracting agencies from unreliable contractors.[1026] However, as discussed in this section, imposing a bid guarantee at the bidding stage may discourage the participation of small businesses, given their more limited access to financial resources. According to the US GAO, small businesses are subject to more stringent requirements in securing financial guarantees compared to larger competitors.[1027] For instance, one in three of the small businesses was required to provide collateral to surety companies, whereas only one in six of the large firms faced a similar requirement.[1028]

To alleviate the difficulties of obtaining guarantees, the SBA operates a Surety Bond Guarantee Program (SBGP) to assist small businesses unable to obtain such guarantees independently.[1029] The SBA acts as a reinsurer for surety companies or

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[1023] 48 CFR § 28.101-1 (a), (c).

[1024] 40 USC ch 3132, subchapter III, Bonds.

[1025] For example, when a contractor will be provided government property or funds to perform the contract. See 48 CFR § 28.103-1.

[1026] Rumizen and Socolar (n 988) 100.

[1027] US GAO, Fact Sheet for Congressional Committees: Small Business Construction Firms' Access to Surety Bonds (June 1995) 27.

[1028] ibid.

[1029] This programme has been active since 1971, when the National Defense Authorization Act was published. The SBA set eligibility requirements for such guarantees. For an introduction to this programme, see CRS, 'SBA Surety Bond Guarantee Program' (updated July 8, 2022, R42037) <https://crsreports.congress.gov> accessed 07 December 2024.

banks, enabling these entities to issue guarantees to small businesses that would otherwise struggle to access them.[1030] Small businesses that satisfy the eligibility criteria for the SBGP can obtain the bid guarantees required by the procuring agency and participate in the bidding process.[1031] The success of the SBGP is evidenced by increasing numbers of assisted small businesses, with approximately 1,675 supported in 2021.[1032]

By offering a structured and flexible framework, the US FAR approach attempts to balance the need for financial assurances with the objective of supporting small businesses.[1033] Nevertheless, the inherent rigidity of statutory requirements may continue to pose challenges for small businesses, highlighting the balance between ensuring reliable contractual performance and supporting small businesses in the federal procurement market.

5.2.4 The timing of qualification and verification in procurement procedures

The timing of the qualification procedure can influence the willingness of SMEs to participate in public procurement. When contracting authorities assess the qualifications of potential bidders at the outset, restricting tender submissions solely to those who have already met certain criteria, SMEs may be deterred from competing. This reluctance stems from the initial costs associated with obtaining certificates or

[1030] 13 CFR § 115.12.

[1031] 13 CFR § 115.13. The eligibility criteria include the status of a small business and good character and reputation. This small business in need shall certify that a bond is expressly required by the bid solicitation or the original contract, and this bond is not obtainable on reasonable terms and conditions without SBA's guarantee. Under this scheme, in the event of a default, the SBA reimburses the surety company for up to 90 percent of the losses incurred. See 13 CFR § 115.31(a).

[1032] CRS 'SBA Surety Bond Guarantee Program' (n 1029) 17.

[1033] See Chapter 7.

other qualification documents from public authorities or securing a bid guarantee.[1034] Such costs, or administrative burdens, are incurred without any certainty of winning the contract, thereby discouraging SMEs with limited resources from entering the competition.[1035] In contrast, a more SME-friendly approach is to defer the qualification assessment until after the tender is selected. By evaluating the qualifications of the successful tenderer, contracting authorities eliminate the need for SMEs to make substantial financial investments upfront. However, permitting any economic operator to bid for the contract without an initial qualification assessment may increase the burden on contracting officers, who may need to evaluate a large number of tenders.[1036] Thus, it is a balance of reducing administrative burdens for bidders, especially SMEs, and ensuring the efficiency of the procurement procedures.

In the EU, the qualification process occurs before the evaluation of tenders.[1037] The only exception is the open procedure, in which contracting authorities can evaluate qualifications and tenders simultaneously or even evaluate tenders first.[1038] In other procedures, the qualification process is typically conducted before the evaluation of tenders, and only qualified bidders are given the opportunity to submit a bid.[1039]

To mitigate the initial administrative burden on economic operators, Directive 2014/24/EU requires contracting authorities to accept the European Single Procurement Document (ESPD) as preliminary evidence of compliance with selection

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[1034] As discussed in Chapter 3, the enormous time and cost associated with the procurement procedure is one of the main barriers that SMEs face to getting access to the procurement market. Nicholas and Fruhmann (n 126) 336.

[1035] Di Mauro, Ancarani, and Hartley (n 466) 379.

[1036] Abby Semple, 'Can We Have Evidence-Based Procurement Policy?' (3 March 2015) <https://procurementanalysis.eu/can-we-have-evidence-based-procurement-policy/> accessed 7 October 2024.

[1037] Directive 2014/24/EU, art 58.

[1038] Directive 2014/24/EU, art 27.

[1039] For example, see Directive 2014/24/EU, art 28 (2).

criteria.[1040] The ESPD functions as a self-declaration, postponing the obligation to provide certificates or supporting documentation until the winning tenderer is identified.[1041] Recital 84 Directive 2014/24/EU highlights that the qualification process often involves a substantial number of certificates, posing an administrative and financial burden on bidders, particularly SMEs with limited financial and human resources.[1042] In an ESPD form, economic operators declare whether they have any exclusion grounds and satisfy all selection criteria proposed by the contracting authority.[1043] By using ESPD forms, bidders do not submit certificates and supporting documents related to exclusion and selection criteria to the contracting authority.[1044] Under Article 59 Directive 2014/24/EU, contracting authorities are required to accept ESPD self-declarations from economic operators, and they will verify the supporting documents of the tenderer to whom they will award the contract.[1045] As a result, the timing of the verification is postponed until the tender is selected.

In essence, the introduction of ESPD separates the qualification process into two parts: the first part is bidders self-certifying their qualification status, and the second part is contracting authorities verifying the evidence of the successful bidder's qualification.[1046] Nevertheless, contracting authorities retain the discretion to ask tenderers at any point during the procedure to provide all or part of the supporting documents.[1047] This, in particular, applies to procedures which include a shortlisting process, such as in restricted procedures, where only qualified candidates will be

[1040] Directive 2014/24/EU, art 59.
[1041] ibid.
[1042] Directive 2014/24/EU, recital 84.
[1043] ibid.
[1044] Directive 2014/24/EU, recital 84.
[1045] Directive 2014/24/EU, art 59 (4).
[1046] ibid.
[1047] Directive 2014/24/EU, art 59 (4).

invited to tender.[1048] The ESPD approach appears to reduce administrative burdens for bidders, particularly SMEs, in the qualification process. However, evidence from the European Commission's *Report on the ESPD survey* suggests that not all suppliers find the system convenient to use.[1049] It has been reported that ESPDs are excessively lengthy forms that can only be completed manually, as they are not integrated with national systems.[1050] Additionally, some contracting authorities continue to require certificates and supporting documents from all bidders, undermining the intended objective of the ESPD.[1051] Moreover, the ESPD functions solely as a self-declaration form, meaning that bidders are still required to satisfy the qualitative selection criteria at the time of completing an ESPD. As a result, the primary benefit of the ESPD is reducing the burden on contracting authorities by deferring the verification process, rather than actively facilitating SME participation by providing them with additional time to prepare for qualification.

A more SME-friendly approach would involve contracting authorities evaluating only the successful bidder's qualifications. Postponing the qualification process in this way would encourage all interested economic operators to submit bids, providing them with additional time to prepare and meet the required standards before the tender is awarded.

The US FAR adopted this approach, where contracting officers determine the responsibility of the selected tenderer, referred to as the 'prospective contractor', only after the tender evaluation process.[1052] FAR 9.103 stipulates that contracting officers

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[1048] Directive 2014/24/EU, art 65 (2).

[1049] European Commission, *Report on the ESPD Survey.* (Publications Office 2020) <https://data.europa.eu/doi/10.2873/697154> accessed 8 October 2024, 9.

[1050] ibid.

[1051] European Commission, *Report on the ESPD Survey* (n 1049) 9.

[1052] 48 CFR § 9.103.

must make an affirmative determination of responsibility before awarding a contract, and the act of signing the contract constitutes a positive determination of responsibility for the prospective contractor.[1053] If the prospective contractor is found to be non-responsible, the contracting officer shall make a determination of non-responsibility and reject the offer.[1054] Notably, the timing of the responsibility determinations is explicitly set as 'before awarding the contract' rather than before evaluating tenders.[1055] According to FAR 9.105-1(b)(1), contracting officers are instructed to collect responsibility-related information promptly after bid openings or receipt of offers.[1056] Generally, they are directed to request information only from the 'low bidder' or 'those offerors in range for award', rather than from all bidders.[1057] This approach not only encourages greater participation from small businesses by reducing administrative burden during the tendering process but also accommodates scenarios when a bidder may lack sufficient financial resources at the time of bidding but plans to secure the necessary funding through mechanisms such as the assignment of claims to a bank, as discussed in Section 5.2.1.2.[1058]

There are instances under the FAR where contracting officers may need to obtain responsibility-related information before issuing a request for proposals (RFP). For example, in negotiated procedures, particularly those involving research and development, FAR 9.105-1(b)(1) allows contracting officers to gather such information during the pre-solicitation phase.[1059] This practice enables contracting officers to

[1053] ibid.
[1054] 48 CFR § 9.105-2.
[1055] 48 CFR § 9.103.
[1056] 48 CFR § 9.105-1(b)(1).
[1057] ibid.
[1058] See Section 5.2.1.2.
[1059] 48 CFR § 9.105-1(b)(1).

better understand the capabilities of potential suppliers, refine procurement requirements, and ensure that the eventual RFP is aligned with market conditions. Nevertheless, this procedure of obtaining information is to facilitate drafting RFPs but not to determine bidders' responsibility.

In summary, the timing of the qualification process is crucial, as it directly impacts the participation of economic operators and influences the willingness of SMEs to bid. The argument that assessing tenders from all interested bidders imposes excessive costs on contracting authorities is valid if there is indeed a high volume of tenders. However, according to the report published by the European Court of Auditors in 2023, the average number of bidders decreased from 5.7 to 3.2 from 2011 to 2021 in the EU.[1060] Thus, it is worth considering deferring the qualification assessment process till the tender evaluation. It also reduces the burden of contracting authorities when they only evaluate the successful bidder's qualification instead of all interested bidders. While this approach is more SME-friendly, it raises concerns that the winning bidder may have strong incentives to manipulate qualification documents, given that passing the qualification check is the final step before the contract award. [1061] Whether qualifications are checked only for winners or for all bidders, the risk of fraudulent documents remains. This can be mitigated by including fraud in the exclusion grounds or reporting in a shared system, allowing other public authorities to assess this information and employ a reputation-based scheme to manage the risk of fraud.

[1060] European Court of Auditors, 'Special Report: Public Procurement in the EU: Less Competition for Contracts Awarded for Works, Goods, and Services in the 10 Years up to 2020' (Special Report No 17/2021, 2021) 19.

[1061] Pedro Telles, 'Qualitative Selection and Exclusion of Economic Operators in Portugal' in Burgi, Trybus, and Treumer (eds) (n 429) 105, 119.

To conclude, selection criteria or general standards for responsibility are also exclusionary requirements, except for the past experience requirement. These criteria are binary, whereby contracting authorities will decide if economic operators pass or fail. However, there are situations where qualifications of bidders are evaluated in a ranking system. In the EU, contracting authorities may use selection criteria and other criteria in restricted procedures and procedures involving negotiation to reduce the number of bidders.[1062] This is a process where SMEs might be at a disadvantage, which will be discussed in the next section.

5.3 The Shortlisting Process in Procurement Procedures

As discussed earlier, the qualification process usually establishes a minimum threshold that all economic operators must meet to be deemed qualified. However, in certain procurement procedures, not all qualified economic operators are eligible to submit tenders.[1063] This process of selecting from among the qualified candidates is referred to as the shortlisting process, or reducing the number of qualified candidates to be invited to participate.[1064] Unlike the selection criteria, Directive 2014/24/EU does not strictly regulate the shortlisting criteria, thereby affording Member States and contracting authorities substantial discretion, provided that the criteria are objective and non-discriminatory.[1065] In principle, shortlisting decisions shall not be made

[1062] Directive 2014/24/EU. arts 28-29,

[1063] In the EU, these procedures are restricted procedures, competitive procedures with negotiation, competitive dialogue procedures and innovation partnerships. See Directive 2014/24/EU, title II, ch 1.

[1064] Directive 2014/24/EU, art 65 (2).

[1065] ibid.

subjectively by contracting officers, and they shall not discriminate against economic operators from other Member States.

In practice, shortlisting often involves a ranking system, wherein those ranked highest are subsequently invited to tender.[1066] For instance, in Portugal, contracting authorities rank candidates from the best to worst based on the selection criteria, and the highest-ranked candidates are invited to tender.[1067] In restricted procedures, contracting authorities are required to invite a minimum of five candidates.[1068] However, this ranking process tends to disadvantage smaller economic operators or those with less experience in public procurement, as the ranking system is based on selection criteria, which often relate to economic capacity, thereby inherently favouring larger businesses. This ranking system also requires more transparency and scrutiny, especially concerning the scoring methodology and how points are allocated for past experience. Particularly, experience in public procurement, which could unfairly benefit large, experienced contractors or incumbent contractors, as discussed in Section 5.2.2.

A lack of transparency or clarity in shortlisting criteria further exacerbates the difficulties SMEs face in accessing public procurement opportunities. The challenge posed by the shortlisting process to SMEs seems to be overlooked by Directive 2014/24/EU. This thesis argues that the shortlisting process shall be regulated in compliance with Article 18 (1). A ranking system based on selection criteria can act as a significant deterrent for SMEs seeking to access public procurement opportunities,

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[1066] Albert Sanchez-Graells, Luke R.A. Butler, and Pedro Telles, 'Exclusion and Qualitative Selection of Economic Operators under Public Procurement Procedures: A Comparative View on Selected Jurisdictions' in in Burgi, Trybus, and Treumer (eds) (n 429) 245, 272.

[1067] *Código dos Contratos Públicos* (Decreto-Lei No 18/2008, as amended by Decreto-Lei No 111-B/2017) (Portugal) art 181; Telles (n 1055) 124.

[1068] Decreto-Lei No 18/2008, art 164 (1); Directive 2014/24/EU, art 65 (2).

and this approach artificially narrows competition, a practice prohibited under Article 18 (1) Directive 2014/24/EU.[1069]

According to the second paragraph of Article 18 (1) Directive 2014/24/EU, competition is artificially narrowed 'when the design of the procurement is made with the intention of unduly favouring or discouraging certain economic operators.' [1070] When a shortlisting process ranks economic operators based on the extent to which they meet selection criteria, it inherently favours large businesses and discriminates against SMEs, given that selection criteria are often minimum levels of economic and technical capacity. One approach to mitigate this disadvantage is to consider non-discriminatory, alternative shortlisting methods that do not solely rely on ranking by economic capacity or size of the bidders. For example, in France, contracting authorities have the option to draw lots from qualified candidates to determine which are invited to tender.[1071] This approach is argued to be more effective in managing the risks of corruption and preferential treatment, as it minimises the potential for biased decision-making.[1072] More importantly, it provides equal opportunities for SMEs to participate in public procurement.

The primary objective of a procurement procedure is to select the best bid, rather than the best bidder.[1073] From this perspective, the details of bidders are almost irrelevant in a procurement procedure.[1074] This thesis concurs with this argument; as long as bidders meet the qualification requirements, the specifics thereof shall not be overly

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[1069] Directive 2014/24/EU, art 18(1).

[1070] ibid.

[1071] Sanchez-Graells, Butler, and Telles (n 1066) 273.

[1072] ibid.

[1073] Pedro Telles et al., 'Simplified Open Procedure Guidance' (Bangor University, 2014) 5<https://www.telles.eu/content/files/s/simplified-open-procedure-guidance.pdf> accessed 09 November 2024.

[1074] ibid.

emphasised, as doing so might compromise a transparent and competitive system. Therefore, to facilitate SME access to public procurement, the shortlisting process shall be conducted in a transparent and equitable manner for all economic operators, such as through a random selection process (drawing lots) from all qualified candidates. If a contracting authority decides to opt for a ranking method, inviting a minimum number of SMEs shall be permitted to counterbalance the disadvantage SMEs face in the ranking process. In fact, the 2006 French Public Procurement Code permitted contracting authorities to set a minimum number of SMEs to be invited in the restricted, negotiated, or competitive dialogue procedures.[1075] However, the *Conseil d'Etat* annulled those provisions in judgment n° 297711, arguing that such SME quotas would violate the principle of equal treatment and non-discrimination.[1076] The *Conseil d'Etat* argued that setting a minimum number of SMEs to be invited to tender makes the size of enterprises a selection criterion, which is not always linked to the subject matter of the contract.[1077] Such a requirement, it held, unduly favoured certain economic operators based on size alone, which is discriminatory and inconsistent with the fundamental principle of equal treatment.[1078] However, several points are worth discussing regarding this judgment: firstly, shortlisting criteria and selection criteria serve distinct purposes, with only the latter required to be related to the subject matter of the contract.[1079] Shortlisting criteria need only be objective and non-discriminatory, as discussed earlier in this section.[1080] Secondly, if a preference for smaller enterprises is considered discriminatory and incompatible with the principle

[1075] Lichère (n 456) at 55 citing Conseil d'État, 9 July 2007, *Syndicat EGF-BTP*, n° 297711.
[1076] ibid.
[1077] Lichère (n 456) at 55 citing *Syndicat EGF-BTP*, n° 297711.
[1078] ibid.
[1079] Directive 2014/24/EU, art 58.
[1080] For example, see Directive 2014/24/EU, art 65 (2).

of equal treatment, then one could similarly scrutinise a shortlisting process that ranks all qualified bidders based on their economic capacity, which inherently favours larger economic operators. Consequently, this process is not consistent with the principle of equal treatment, although inviting larger economic operators to submit bids may be considered a pursuit of value for money or efficiency. To adhere to the principle of equal treatment, contracting authorities should implement strict rotation or alternative methods to guarantee that all qualified economic operators are afforded an equal opportunity to submit a bid.[1081]

In the US, there is no direct equivalent to the shortlisting process in the EU; however, a similar approach is found in the negotiation procedures outlined in Part 15 of the FAR.[1082] Contracting officers typically exchange information with the industry before receiving proposals from interested parties.[1083] This information exchange process helps contracting officers to identify 'viable competitors', who are subsequently invited to submit proposals. However, even if a business is informed that it is not considered a viable competitor, it may still submit a proposal once the procurement process begins.[1084] This aspect of the FAR appears to foster a more level competitive landscape, as during the information exchange phase, contracting officers lack comprehensive details about potential bidders. Consequently, their assessment of which competitors are viable may be flawed. Allowing small businesses that might not

[1081] Arrowsmith, Linarelli, and Wallace Jr., (n 19) 62.

[1082] 48 CFR § pt 15.

[1083] 48 CFR § 15.200. This information exchange might take forms of conferences, public hearings, publishing presolicitation notices etc. The presolicitation notice provides 'a general description of the scope or purpose of the acquisition and invites potential offerors to submit information that allows the government to advise the offerors about their potential to be viable competitors.'

[1084] In the EU, for example, in competitive procedure with negotiation, only those economic operators invited by the contracting authority may submit an initial tender, same as the competitive dialogue procedure, see Directive 2014/24/EU, arts 29-30.

initially appear to be viable competitors the opportunity to participate can help ensure a more inclusive and competitive procurement process.

5.4 Conclusion

As identified in Chapter 3 of this thesis, excessive qualification criteria pose significant barriers for SMEs seeking access to public procurement opportunities.[1085] This chapter evaluates the main criteria involved in the qualification evaluation process in both the EU and US federal procurement systems, and discusses how to manage the qualification process to facilitate SME participation. The analysis specifically focuses on the four aspects of the qualification process: the assessment of financial capacity, past experience, bid guarantees, and the timing of the qualification process. Moreover, this chapter also discussed the process of reducing the number of potential bidders, termed the shortlisting process, as SMEs are often at a disadvantage in this process.

The analysis demonstrates that both EU Directives and the US FAR have adopted measures to manage the qualification process, thereby alleviating the challenge posed by excessive qualification criteria and administrative burden on SMEs. In the EU, efforts have been made to improve SME access to public procurement, notably by capping the minimum turnover requirements imposed by contracting authorities and introducing the ESPD as a self-declaration mechanism at the qualification stage, with the verification of qualifications postponed until the selection of the successful bid.[1086] Yet the effectiveness of these measures remains contested.[1087] The ESPD, in

[1085] See Chapter 3, Section 3.2.3.
[1086] Trybus and Andrecka (n 55).
[1087] European Commission, *Report on the ESPD Survey* (n 1049) 9; European Court of Auditors (n 1060).

particular, has been criticised for its complexity and length, and not all Member States have integrated it into their e-procurement systems.[1088] Where such integration is lacking, completing the ESPD remains a manual task, whereas comparable national forms can often be automatically filled in from existing databases, making them considerably more user-friendly.[1089] A survey conducted by the European Commission found that 10 per cent of respondents considered the ESPD to have hindered their access to procurement opportunities.[1090] Additionally, contracting authorities retain the discretion to demand supporting evidence at the bidding stage, thereby undermining the intended simplification.[1091] Consequently, there is little empirical evidence that the ESPD has substantially reduced administrative burdens or facilitated SME participation in EU procurement.

The US FAR adopts a more direct protection regime for small businesses. A central feature is the statutory COC mechanism administered by the SBA. When a contracting officer determines that a small business is non-responsible, whether on grounds of financial capacity or past performance, the matter must be referred to the SBA. The SBA has the authority to overturn such a determination by issuing a COC, which obliges the contracting authority to award the contract to the small business. This safeguard prevents contracting officers from excluding small businesses unfairly at the qualification stage. Responsibility determinations under the FAR also illustrate the discretionary role of contracting officers, who assess financial resources and technical ability on a case-by-case basis rather than by applying rigid thresholds. Although past performance is a relevant factor, the FAR explicitly provides that a prospective

[1088] European Commission, *Report on the ESPD Survey* (n 1049) 4.
[1089] ibid 9.
[1090] European Commission, *Report on the ESPD Survey* (n 1049) 9.
[1091] Directive 2014/24/EU, art 59(4).

contractor cannot be determined non-responsible solely based on a lack of past performance in federal procurement. This rule is particularly important for newly established businesses, the majority of which are small businesses. Taken together, these features present a regime that combines administrative discretion with safeguards for small businesses to ensure they are not unfairly treated during the determination of responsibility (evaluation of qualification).

Although establishing an EU-wide regime to protect the interests of SMEs in the qualitative selection process, akin to the US FAR approach, is challenging, Member States may adopt measures that support SMEs provided that such measures comply with the principles set out in Article 18 (1) Directive 2014/24/EU and general principles of EU law. For instance, when Directive 2014/24/EU was transposed into UK law through the Public Contracts Regulations 2015, Section 111 prohibited the use of pre-qualification questionnaires for contracts below the EU thresholds.[1092] This reform, inspired by Lord Young's recommendations, was viewed as a significant step towards facilitating SME participation in public procurement.[1093] By doing so, the UK facilitated greater SME access to the procurement market while remaining aligned with the EU principles of equal treatment and non-discrimination. [1094] The subsequent Procurement Act 2023 retained this prohibition, further solidifying the commitment to removing procedural barriers for lower-value contracts, which are predominantly undertaken by SMEs.[1095] Furthermore, as the qualification process assesses bidders'

[1092] Public Contracts Regulations 2015, s 111.

[1093] Lord Young, *Enterprise for All: The Relevance of Enterprise in Education* (Cabinet Office, 2014) 8 <https://www.gov.uk/government/publications/report-on-small-firms-2010-to-2015-by-lord-young> accessed 9 December 2024.

[1094] For a discussion about the UK's qualification regime in public procurement, see Luke Butler, 'Exclusion, Qualification and Selection in the UK under the Public Contracts Regulations 2015' in Burgi, Trybus, and Treumer (eds) (n 429) 189, 218.

[1095] Procurement Act 2023, s 85(1).

qualifications rather than the bids themselves, it does not compromise the objective of achieving value for money or fostering competition. Moreover, this approach may enhance competition by enabling SMEs to access procurement opportunities without deterring larger businesses. Conversely, dividing large contracts into lots may discourage large businesses from participating where individual lot values are too low or where lot bundling is restricted. A comparison of SME-friendly measures will be discussed in Chapter 8.

Despite the positive steps in Directive 2014/24/EU in facilitating SME participation, challenges remain in the shortlisting process, where contracting authorities reduce the number of economic operators invited to submit bids. There is a lack of specific guidance for this process in Directive 2014/24/EU. In practice, the shortlisting process often incorporates a ranking system based on bidders' economic capacity, which can produce discriminatory outcomes by selecting qualified economic operators with higher annual turnovers or more experience in public procurement. This chapter contends that such practices deviate from the aim of the qualitative selection process, which permits contracting authorities to assess whether bidders possess sufficient capacity to perform a contract, rather than ranking them on general capabilities. In practice, the risk-averse nature of contracting authorities often results in a preference for larger, more established and experienced businesses.[1096] To counteract this bias, alternative approaches, such as the French model, where contracting authorities may draw lots among qualified economic operators, offer a more equitable solution. By levelling the playing field for SMEs who meet qualification requirements, such

[1096] See Chapter 3, Section 3.3.2.

practices encourage SMEs to participate in public procurement and uphold the principles of equal treatment and proportionality.

Chapter 6 Providing Bid Preferences for SMEs in Public Procurement Award Procedures

6.1 Introduction

Price evaluation preferences, commonly referred to as bid preferences or marginal preferences, are mechanisms through which governments intentionally favour specific suppliers during public procurement award procedures.[1097] Such mechanisms involve artificially adjusting bid evaluations to provide certain suppliers with an advantage; for example, a 5 per cent price preference allows a favoured bidder to win a contract provided that their bid does not exceed the lowest bid by more than 5 per cent. Unlike the other two SME-friendly measures discussed in Chapters 4 and 5, bid preferences do not reduce entry barriers encountered by SMEs in government procurement. Rather, they operate as a preferential measure, or termed SME-favouring measure, aiming to enhance the chance of winning for SMEs by offering them a price evaluation advantage during tender evaluation.[1098]

This chapter examines bid preferences as an SME-friendly measure intended to support SMEs by increasing their participation and securing contract awards. It aims to assess whether this measure has effectively achieved the intended objectives without undermining other objectives of public procurement law. It does so by critically examining three distinctive national frameworks: Brazil, the US, and South Africa. These jurisdictions exemplify divergent rationales and design strategies for bid preferences. Brazil operates an economically oriented framework primarily designed

[1097] Marion (n 128) 1591.

[1098] Burgi (n 48) 284. As the for distinction between facilitative (SME-fair) measures and preferential (SME-favouring) measures, see Chapter 1, Section 1.2.2.

to support micro and small enterprises (MSEs)[1099], employing detailed statutory mechanisms such as the fictitious-tie bid preference and regional preference schemes.[1100] Conversely, the US federal approach applies bid preferences selectively through the Historically Underutilised Business Zones (HUBZone) programme, explicitly aiming at regional socioeconomic revitalisation, complemented by broader approaches to support small businesses at the state level, notably in California.[1101] In contrast, the bid preference system in South Africa is explicitly integrated into a broader constitutional and legislative framework promoting socioeconomic transformation through targeted empowerment of historically disadvantaged individuals, closely aligned with the Broad-Based Black Economic Empowerment (BBBEE) initiative.[1102]

Through this examination, the chapter elucidates how differing legislative contexts and policy goals of bid preferences shape SME participation and success within public procurement. Additionally, it identifies the advantages and limitations of each approach, providing insights into the implementation of bid preferences across different legal, economic, and social contexts. Ultimately, this examination contributes to the thesis's overarching objective of evaluating measures that facilitate SME success in securing public contracts. It adds another 'technique' that favours SMEs to the discussion, thereby contributing to the overall identification of best practices and

[1099] For a definition of MSEs in Brazil see Chapter 2, Section 2.4.

[1100] Cesar Pereira and Rafael Wallbach Schwind, 'Public Procurement in Brazil Access for Foreign Suppliers and Compatibility with International Procurement Practices' in Aris Georgopoulos, Bernard Hoekman, Petros C. Mavroidis (eds), *The Internationalization of Government Procurement Regulation* (Oxford University Press 2017) 358.

[1101] See Section 6.3.

[1102] See Section 6.4.

necessary conditions for successful implementation, which will be discussed in Chapter 8.

6.2 Bid Preferences for MSEs in Brazil

The support for MSEs is constitutionally enshrined in Brazil, with Article 170(IX) of the Federal Constitution, granting preferential treatment to MSEs as part of the broader economic order, thereby giving such measures in public procurement a constitutional foundation.[1103] Complementing this, Article 179 imposes obligations on all levels of government to adopt favourable treatment for MSEs to reduce administrative burdens confronting MSEs.[1104] Although these provisions do not explicitly address public procurement, they form a constitutional foundation for the adoption of preferences for MSE bidders in government procurement procedures. This foundation was later operationalised through a complementary Law, No. 123, of December 14, 2006 (LC 123/2006), which established the National Statute of Micro and Small Sized Companies.[1105] Its amendments, LC 147/2014, introduced specific mechanisms to support MSEs in areas such as taxation, administrative procedures, and public procurement.[1106]

Article 1 LC 123/2006 authorises differentiated and favoured treatment for MSEs with the explicit aim of promoting economic and social development at the municipal and regional levels.[1107] This provision underscores that preferential treatment for MSEs is

[1103] Federal Constitution of Brazil, art 170 (IX).
[1104] ibid art 179.
[1105] LC 123/2006.
[1106] ibid.
[1107] LC 123/2006, arts 1, 47.

not only about enterprise support, but also about bolstering local economies and social development.[1108] LC 123/2006 introduced a range of MSE supportive measures covering taxation, administrative simplification, access to credit, and public procurement.[1109] Specifically, a number of SME-friendly measures were incorporated in public procurement.[1110] Among these, the fictitious-tie bid preference, allowing MSEs to match or improve bids within a 10 per cent margin (5 per cent in electronic auctions), was mandatory.[1111] By contrast, other measures, such as reserving contracts valued at up to BRL 80,000, or reserving quotas in contracts of divisible goods, were framed initially as discretionary for contracting authorities.[1112] The 2014 reform (LC 147/2014) broadened and strengthened this regime by rendering those discretionary measures mandatory and introducing a local and regional bid preference of up to 10 per cent for MSEs that are located in the same region as the contracting authority.[1113] Accordingly, it is evident that Brazil predominantly uses bid preferences to support MSEs in public procurement, diverging from the EU's approach of dividing

[1108] Valeria Guimaraes De Lima e Silva, 'Treatment of small businesses in public procurement in Brazil', (2011) Public Procurement Law Review 4, 123.

[1109] LC 123/2006; also see ILO Regional Office for Latin America and the Caribbean, Policies for the formalisation of micro and small enterprises in Brazil (2014) <https://www.ilo.org/publications/policies-formalization-micro-and-small-enterprises-brazil> accessed 18 June 2025.

[1110] For an overview of the treatment of MSEs in public procurement under LC 123/2006, see Silva (n 1108).

[1111] LC 123/2006, arts 44, 45.

[1112] LC 123/2006, art 48.

[1113] *Lei Complementar n 147, de 7 de agosto de 2014* (LC 147/2014). One of the major reforms is mandatory reserved contracts. Before 2014, reserved contracts are not mandatory, after LC 147/2014 was enacted, items with a value lower than BRL 80,000 must be reserved for MSEs, which means large businesses are prohibited from bidding for those contracts. Interestingly, the difference between the Brazilian approach and the US approach is, Brazilian rule requires the items with a value lower than a certain threshold to be reserved for MSEs, but the US approach examines the value of the contracts, instead of individual items. This is very important as contracting authorities may bundle a few items together to exceed the threshold. However, under LC123/2006 (as amended) art 48, up to 25 per cent small portion (lots) of large contracts can be reserved for MSEs if applicable. Thus, apart from the bid preferences, the Brazilian model of SME-friendly procurement also combines both reserved contracts in the US and division into lots in the EU. For a comparison of different approaches across jurisdictions selected in this thesis, see Chapter 8, Section 8.3.

large contracts into lots and the US regime of reserved contracts.[1114] Preliminary observations on jurisdictional approaches will be presented in Chapter 8.[1115]

Brazil's adoption of a new public procurement statute, Law No. 14,133/2021, marked a significant reform, repealing Law No. 8.666/1993 and modernising procurement procedures.[1116] The new procurement law maintains the preferential treatment of MSEs, largely by incorporating and reaffirming the regime established under the complementary law LC 123/2006.[1117] While consolidating prior rules, Law No. 14,133/2021 also places increased emphasis on principles of efficiency, transparency, and innovation.[1118] The current legal framework seeks to strike a balance between the traditional procurement objectives of public procurement, such as value for money and competition, with the constitutionally endorsed goal of fostering MSE participation.[1119] The following section discusses the two main bid preference rules for MSEs, fictitious-tie preferences and bid preferences for local MSEs.

6.2.1 Fictitious-tie bid preferences for MSEs

Under Article 44 and Article 45 LC 123/2006, MSEs are granted a conditional advantage in what is termed a fictitious tie (*empate ficto*).[1120] A tie in this context is fictitious, which is legally deemed to exist when an MSE's bid is not the lowest but comes within a certain margin of the lowest bid. Specifically, when an MSE submits a

[1114] See Chapters 4 and 7.
[1115] See Chapter 8.
[1116] *Lei No 14.133, de 1 de abril de* 2021 (Brazil) (Law No 14.133/2021).
[1117] ibid art 4.
[1118] Law 14.133/2021 (n 15) art 5.
[1119] Teixeira (n 280) 9.
[1120] LC 123/2006, art 44.

bid that is up to 10 per cent higher than the lowest bid in most procurement procedures, or up to 5 per cent higher in electronic reverse auctions (*pregão*), the MSE may be invited to match the lowest bid before the contract is awarded.[1121]

Article 44 of LC 123/2006 mandates the application of this preference, while Article 45 sets out the procedural sequence for its implementation. This mechanism is intended to enhance the competitiveness of bids from MSEs without incurring additional cost on the contracting authority. If the MSE agrees to match or offer a lower price than the lowest bid, the contract will be awarded to the MSE at the adjusted price.[1122] Should the lowest eligible MSE decline to exercise this right, the opportunity is sequentially extended to the next highest-ranked MSE within the statutory margin.[1123] Only if no eligible MSE accepts will the contract be awarded to the original lowest bidder.[1124] Importantly, the preference does not guarantee contract award to an MSE based solely on its size. The MSE bidder must still offer the most competitive price, ensuring that the contracting authority pays no more than it would have in the absence of the preference. As such, the so-called fictitious tie provides MSEs with a form of bid preference that operates within a competitive framework, ensuring that this preference does not undermine value for money of a procurement procedure.

Law No. 14.133/2021 reaffirmed the fictitious-tie preference for MSEs in Article 4, while introducing important limitations.[1125] Notably, Article 4(1) excludes contracts with an estimated value exceeding the statutory ceiling for the annual gross revenue of

[1121] According to Law 14.133/2021 art 28, public procurement methods include reverse auction, competitive procurement, contest, auction, competitive dialogue.
[1122] LC 123/2006, art 45, I.
[1123] ibid art 45, II.
[1124] LC 123/2006, art 45, I.
[1125] Law 14.133/2021, art 4.

small enterprises, as defined in LC 123/2006.[1126] In addition, Article 4(2) stipulates that fictitious-tie preferences do not apply to MSEs that have executed a public contract exceeding that annual revenue threshold within the same calendar year as the procurement process.[1127] These limitations ensure that the fictitious-tie bid preference is confined to MSEs that genuinely require support, thereby excluding those that, by virtue of securing large contracts, no longer need this form of competitive advantage.[1128]

Furthermore, Article 48 LC 123/2006 mandates exclusive bidding for MSEs in procurement contracts valued below BRL 80,000, which is essentially a reserved contracts scheme.[1129] In such cases, the application of fictitious-tie preferences becomes redundant, as all potential bidders are MSEs. Accordingly, the fictitious-tie bid preference is primarily applied to contracts valued between the statutory threshold for reserved contracts (BRL 80,000) and the revenue ceiling of MSEs (BRL 4.8 million).[1130]

The contract value limitation gains further significance when compared with other jurisdictions. In the EU public procurement framework, Article 58 (3) Directive 2014/24/EU prohibits contracting authorities from requiring economic operators to have an annual turnover exceeding twice the estimated contract value, except in duly justified cases.[1131] Prior to Directive 2014/24/EU, contracting authorities were able to

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[1126] ibid art 4(1). Based on LC 123/2006, art 3, the upper threshold for a small business's annual gross revenue is BRL 4.8 million. Also see Chapter 2, Section 2.4.

[1127] Law 14.133/2021, art 4 (2).

[1128] Regarding the relation between contract value and SME-friendly measures, see Chapter 8, Section 8.3.1.

[1129] LC 123/2006, art 48. For a discussion on reserved contracts, see Chapter 7.

[1130] The current annual revenue threshold for a small enterprise in Brazil is BRL 4.8 million. See Chapter 2, Section 2.4.

[1131] Directive 2014/24/EU, art 58(3).

impose turnover thresholds significantly higher than the contract value, effectively excluding many SMEs from participation.[1132] Article 58 (3) Directive 2014/24/EU thus functions to restrict the use of excessive financial thresholds, thereby facilitating access for SMEs.[1133] However, contracting authorities may, at their discretion, require economic operators to meet a turnover threshold above the contract value. In contrast, the Brazilian rule recognises that MSEs may submit bids for contracts exceeding their annual revenue, but it removes the entitlement to fictitious tie preferences in such cases. For instance, a small business with an annual turnover of BRL 4.6 million may bid for a contract estimated at BRL 5 million but will not be eligible for the fictitious-tie preference. In the EU context, a small business with an annual turnover lower than the estimated contract value might not be qualified to submit a bid if the contracting authority sets a turnover requirement exceeding the contract value, under Article 58 (3) Directive 2014/24/EU.[1134] The Brazilian approach thus maintains a broader scope of participation for MSEs while limiting the use of fictitious-tie bid preferences to lower-value contracts where the participation of MSEs is more feasible, and less likely to strain their capacity to perform or to match the price offered by the lowest bids in such contracts. Chapter 8 will discuss the connection between contract value and specific SME-friendly measures.[1135]

[1132] For a discussion of the minimum turnover requirement in EU public procurement framework, see Chapter 5, Section 5.2.1.

[1133] See Directive 2014/24/EU, art 58 (3); also see Chapter 5, Section 5.2.1.1.

[1134] Directive 2014/24/EU, art 58 (3).

[1135] See Section 8.4.1.

6.2.2 Bid preferences for local MSEs

In addition to the fictitious-tie preferences, LC 147/2014 introduced a geographically based bid preference aimed at supporting MSEs located in proximity to the contracting authority.[1136] The amended Article 48 LC 123/2006 authorises the application of a margin of preference of up to 10 per cent in favour of MSEs established in the same local area or region as the contracting authority.[1137] Unlike the fictitious-tie preferences, which require an eligible MSE to match the lowest bid in order to secure the award, this provision permits the award of a contract to a local MSE even where its price is marginally higher, without the necessity of matching the lowest bid.[1138] Nevertheless, this measure is discretionary with conditions rather than mandatory: contracting authorities may apply it to benefit MSEs located in the same region when there is an expectation that the preference advances the statutory objectives of fostering local and regional economic and social development.[1139] This local preference mechanism closely resembles the price evaluation preference granted to HUBZone small businesses within the framework of US federal procurement.[1140] In both instances, eligible MSEs are provided with a pricing advantage during the bid evaluation process. However, it is important to note that the HUBZone bid preference is mandatory, as detailed in Section 6.3.1. For the clarity and convenience of the discussion, this type of bid preference is termed traditional bid preferences in this Chapter.

Compared with the fictitious-tie preferences, traditional bid preferences for local MSEs may increase the costs of contracting authorities, as they may result in awarding the

[1136] LC 123/2006, art 48, §3º.
[1137] ibid.
[1138] LC 123/2006, art 48.
[1139] ibid.
[1140] See Section 6.3.1.

contract to a higher-priced local MSE bidder, instead of the lowest bid. In such cases, the price difference between the lowest bid and the winning bid from a local MSE can be regarded as a premium for promoting local MSEs and economic development. Given that bid preferences for local MSEs may increase the costs of contracting authorities, their application is subject to certain conditions.[1141] First, there must be a sufficiently competitive pool of local or regional MSEs qualified to bid for the contract.[1142] This is defined as the presence of at least three qualified local or regional MSEs willing to bid.[1143] This requirement is designed to ensure that the preference does not unduly restrict competition. Where fewer than three such enterprises are available, the application of the preference is deemed unjustified.[1144] This reflects a cautious balance between promoting local MSEs and preserving competition within the procurement process. In addition, Article 49 (III) LC 123/06 prohibits the preferences for MSEs when it is not advantageous to the public administration or is detrimental to the contract, but the wording of this limitation is rather vague.[1145]

It is important to note that fictitious-tie preferences for MSEs are mandatory, whereas traditional bid preferences for local MSEs are applied at the discretion of contracting authorities.[1146] The distinction likely reflects the differing impacts these mechanisms have on value for money. Fictitious-tie preferences do not increase the procurement costs, as the selected MSE must match the lowest bid.[1147] In contrast, traditional bid

[1141] LC 123/2006, art 48.
[1142] ibid art 49(II).
[1143] LC 123/2006, art 49(II).
[1144] ibid.
[1145] LC 123/2006, art 49(III).
[1146] ibid.
[1147] 'Procurement costs' here only consider the price for the goods, services, or works procured. It does not account for potential indirect costs that may arise from underperformance, which will be discussed at the end of the chapter.

preferences may result in the contract being awarded to a bidder with a higher price. Whether the use of traditional bid preferences in practice has effectively achieved the intended objectives will be examined in the next section.

6.2.3 The effectiveness of using bid preferences to support MSEs

The impact of fictitious-tie bid preference on MSE participation and contract awards has been proven to be limited.[1148] Barbosa and Silva found no 'beneficial and significant effect', suggesting that a fictitious-tie preference neither helped nor hindered MSEs' competition in public procurement.[1149] Although Barbosa and Silva provide valuable analysis on empirical data, their choice of case study significantly limits the conclusion that can be drawn regarding the effectiveness of fictitious-tie bid preferences.[1150] According to the data collected by Barbosa and Silva, MSEs were already winning 99.85 per cent of the contracts for the procurement of foodstuffs; based on the number of contracts, the room for further improvement was negligible.[1151] Consequently, the study is arguably susceptible to selection bias, as it does not assess the impact of the legislation in scenarios where MSEs encounter genuine barriers to entry and competition. This also implies that in sectors where MSEs have a more

[1148] Felipe José Ansaloni Barbosa and Wendel Alex Castro Silva, 'Overview on the participation and contracting of micro and small enterprises in online procurement of foodstuffs: case study of *Centro de Preparação de Oficiais da Reserva de Belo Horizonte* (Reserve Officer Training Center of Belo Horizonte) in the period from 2007 to 2015' (2017) 140 *Revista do TCU* 84; Paulo R C Reis and Sandro Cabral, 'Public procurement strategy: the impacts of a preference programme for small and micro businesses' (2015) 35(2) Public Money & Management 103, 108.

[1149] See Barbosa and Silva (n 1148).

[1150] The study examined data of procurement by Centro de Preparação de Oficiais da Reserva de Belo Horizonte (CPOR), specifically analysing foodstuff procurements over a defined period (2007–2015). See Barbosa and Silva (n 1148).

[1151] ibid. During the period from 2007 to 2015, items won by MSEs were 858 and only 3 items won by medium and large companies. This could be due to the fact that most items have a relatively low value, less than R 80,000.

dominant share of contracts, the use of SME-friendly measures may not significantly increase their participation, an issue discussed in Chapter 8.[1152] Moreover, when the lowest bidder is an MSE, a fictitious-tie bid preference does not apply.[1153] A more robust assessment would require examining sectors with historically low MSE participation, where the use of bid preferences could potentially improve their participation.

Similarly, Reis and Cabral have found that the fictitious-tie bid preference did not increase MSEs' probability of securing contracts.[1154] Conversely, the correlation between the use of a fictitious-tie bid preference and MSEs' probability of winning is negative, indicating that MSEs could not match or offer a lower price than the lowest bid.[1155] Reis and Cabral explained that MSEs may lack the capacity to bid aggressively to lower their bid price.[1156] It is noteworthy that the contracts sampled in this study were conducted through reverse auction, which applies a 5 per cent fictitious-tie bid preference.[1157] Consequently, MSEs are afforded the opportunity to match prices when their bids are not more than 5 per cent higher than the lowest bid. In other procedures where the preference is set at 10 per cent, it may be more challenging for MSEs to match the lowest bid.

The design of the Brazilian procurement system is a balancing act among different objectives. Article 5 Law No. 14.133/2021 includes over twenty principles, and Article 11 mandates four objectives, including the selection of the most advantageous tender,

[1152] See Section 6.3.1.
[1153] LC 123/2006, art 48.
[1154] Reis and Cabral (n 1148) 105.
[1155] ibid.
[1156] Reis and Cabral (n 1148) 105.
[1157] LC 123/2006, art 45, §3.

equal treatment and fair competition, cost efficiency, and innovation and sustainable national development.[1158] *Prima facie*, bid preferences for SMEs might appear inconsistent with equal treatment and fair competition, but both free competition and preferential treatment for MSEs are general principles of the economic activity under Article 170 of the Brazilian Constitution. This constitutional provision effectively carves out a justified exception to the equality of bidders, recognising that treating inherently unequal bidders identically may perpetuate structural monopolies.[1159] In contrast, a temporary asymmetry in treatment may create more equity and incentivise market competition.[1160]

Moreover, evidence indicates that the impact of preferential measures introduced by LC 123/2006 on the cost of contracting authorities has been modest.[1161] If calibrated carefully, a bid preference provided to MSEs may enhance value for money through competition from a larger number of bidders.[1162] Thus, preferential treatment for MSEs does not undermine other principles of public procurement in Brazil.

6.3 Bid Preferences for Small Businesses in the US

Section 6.2 examined the application of bid preferences for MSEs in Brazil, where such measures are primarily motivated by economic considerations, namely,

[1158] See Law 14.133/2021, arts 5, 11.
[1159] Brazilian Constitution, art 170.
[1160] See Chapter 1, Section 1.2.1.
[1161] Reis and Cabral (n 1148).
[1162] See Sandro Cabral, Paulo Ricardo da Costa Reis, and Adilson da Hora Sampaio, 'Determinantes da participação e sucesso das micro e pequenas empresas em compras públicas: uma análise empírica' ('Determinants of Participation and Success of Micro and Small Enterprises in Public Procurement: An Empirical Analysis') (2015) 50 Revista de Administração (São Paulo) 477.

supporting MSEs or stimulating regional economies by awarding contracts to locally based firms.[1163] Similarly, in the US, bid preferences are used to promote a range of socioeconomic goals, including supporting HUBZone small businesses in federal procurement through a 10 per cent price evaluation preference, and supporting local small businesses through bid preferences in government procurement at the state level. [1164] At their core, bid preferences are intended to empower particular categories of businesses, whether defined by their size, geography, or origin of production, in order to confer broader socioeconomic benefits.[1165]

In contrast to the reserved contracts regime for small businesses in general, only small businesses located in the HUBZones are eligible for the price evaluation preference (bid preference) in open competition, with some state procurement systems extending bid preferences to all small businesses.[1166] Chapter 7 will present a comprehensive analysis of reserved contracts regime for small business in US federal procurement. This section examines both the HUBZone price preference programme and selected state-level bid preference schemes, with a particular emphasis on California's model, which is notable for its longevity and the substantial empirical evidence available regarding its implementation and effects.[1167]

[1163] See Section 6.2.

[1164] Marion (n 128) 1592.

[1165] See Chapter 2, Section 2.3; Chapter 7.

[1166] For an up-to-date overview of state-level preferences in public procurement see National Association of State Procurement Officials (NASPO), 'State Preference Repository' <https://www.naspo.org/research-and-innovation/state-preference-repository/> accessed 13 May 2025; also see Yuhua Qiao, Khi V Thai and Glenn Cummings, 'State and Local Procurement Preferences: A Survey' (2009) 9 Journal of Public Procurement 371.

[1167] Qiao, Thai and Cummings (n 1166).

6.3.1 Price evaluation preferences for HUBZone small businesses

Under the Small Business Act and the FAR, the price evaluation preferences for certified HUBZone small businesses are the only currently authorised and active price preference among federal small business programmes.[1168] Together with reserved contracts and subcontracting requirements, price evaluation preference forms one component of the HUBZone programme, which offers a margin of preference to certified small businesses operating in areas with high poverty, low income, or high unemployment.[1169]

6.3.1.1 HUBZone small business bid preference

Defined and certified by the Small Business Administration, HUBZone small business concerns are small businesses who are at least 51 per cent owned and controlled by US citizens, a Community Development Corporation, an agricultural cooperative, an Alaska Native Corporation, a Native Hawaiian organization, or an Native American Indian tribe, they should also have their principal office located in a HUBZone and at least 35 per cent of their employees living in a HUBZone.[1170] To be eligible for

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[1168] Although the Department of Defense previously applied a similar preference for small disadvantaged businesses (SDB), this was discontinued following the Federal Circuit's decision in *Rothe Development Corp. v. Department of Defense*, which found the measure lacked a sufficient remedial justification. See *Rothe Development Corp v Department of Defense* 545 F 3d 1023 (Fed Cir 2008). To qualify as an SDB, a business must be at least 51 per cent owned and controlled by one or more individuals who are socially and economically disadvantaged. According to 48 CFR § 124.103, socially disadvantaged individuals are mainly those who have been subjected to racial or ethnic prejudice or cultural bias within American society. The Federal Circuit held that the bid preference for SDBs did not meet the constitutional requirement of demonstrating a compelling governmental interest. Specifically, it failed to show sufficient evidence of prior discrimination that would warrant a race-based remedial measure.

[1169] 15 USC § 657a.

[1170] 13 CFR §126.103 also includes an 'attempt to maintain' requirement, which requires that the HUBZone small business shall maintain this 35 per cent of employees residing in a HUBZone situation

HUBZone programmes, small businesses must obtain and maintain certification from the SBA, recertifying every three years, and there is no fixed limit on the duration of participation so long as the business continues to satisfy the SBA's eligibility criteria.[1171]

FAR 19.1307 mandates that, in full and open competition, offers from certified HUBZone small businesses receive a 10 per cent price evaluation preference.[1172] Specifically, the contracting officer adds a factor of 10 per cent to the price of all offers from large businesses to give HUBZone small businesses a competitive edge. In the event of a tie, namely, where application of the 10 per cent price evaluation preference renders a HUBZone small business bid equivalent to that of a large business, FAR 19.1307(d) provides that the contract shall be awarded to the HUBZone small business.[1173] The price evaluation preference does not apply when the lowest, responsive, and responsible offeror is a small business.[1174] For instance, if a small business offers a lower bid than this HUBZone small business bidder, the contracting authority shall refrain from adding the 10 per cent to the lowest bid from the small business.[1175] It demonstrates a delicate balance between different categories of small businesses' interests, which will be further discussed in Chapter 7.[1176]

According to FAR 19.1307, the 10 per cent price evaluation preference for HUB Zone small business concerns shall be used in full and open competition in government

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during the performance of the contract, and if there is less than 20 per cent of employees residing in a HUBZone, this HUBZone business fails to maintain this requirement. See 13 CFR § 126.

[1171] ibid.

[1172] 48 CFR § 19.1307.

[1173] 48 CFR § 19.1307 (d).

[1174] 48 CFR § 19.1307.

[1175] 48 CFR § 19.1307(b)(2).

[1176] See Chapter 7, Section 7.3.

procurement, which implies that this price preference does not apply in reserved contracts for small businesses or any specific category of socio-economic small businesses, which is a statutory exception to open and full competition.[1177] Apart from that, FAR 19.1307 (a) also stipulated three scenarios where the price evaluation preference shall not be used: 'where price is not a selection factor so that a price evaluation preference would not be considered', or 'where all fair and reasonable offers are accepted (e.g. the award of multiple award schedule contracts)', or 'for the reserved portion of a solicitation for a multiple-award contract'.[1178]

6.3.1.2 The implementation and effectiveness of bid preference for HUBZone small businesses

As part of the HUBZone programme, bid preferences for HUBZone small businesses aim to improve and revitalise the economic situation of HUBZones, more specifically increasing job opportunities, capital investment, and economic development, through supporting them in getting access and winning federal procurement contracts.[1179] Among these objectives, increasing the employment rate is at the core, and this policy encourages small businesses to operate in those distressed areas so that they will

[1177] See 48 CFR § 6.101.

[1178] See 48 CFR § 19.1307.

[1179] See FAR 19.13, for the performance of certified HUBZone small businesses in federal procurement, see SBA, 'Fiscal Year 2024 Annual Performance Report' <https://www.sba.gov/sites/default/files/2025-02/FY24%20SBA%20APR-2025-0123-508.pdf> 49; R. Corinne Blackford, 'The SBA's Historically Underutilized Business Zone (HUBZone) Program' (CRS IF12428, 15 June 2023) <https://crsreports.congress.gov> accessed 13 May 2025; R. Corinne Blackford, 'Small Business Administration HUBZone Program' (CRS Report R41268, 14 February 2025) <https://crsreports.congress.gov> accessed 13 May 2025.

create job opportunities in these areas, especially by requiring that at least 35 per cent of their employees reside in HUBZones.[1180]

Although the HUBZone programme also aims to boost the small business community, the main objective is to revitalise certain distressed areas.[1181] The objective is to enhance these HUBZones to facilitate their recovery from distress, thereby prompting a consideration of the ongoing status of HUBZone small business certification. Unlike women-owned small business (WOSB) or service-disabled veteran-owned small business (SDVOSB) programmes, HUBZones programmes aim to improve the situation of HUBZones. As a result, once a Hubzone loses its status, small businesses operating there may no longer benefit from the HUBZone programme and lose their certification as a HUBZone small business. To prevent abrupt disruptions for those businesses, the areas that are no longer HUBZones will be labelled as redesignated areas, and previous certified HUBZone small businesses will have three additional years to benefit from this programme.[1182] The support for HUBZone small businesses is more economically driven, as it is not based on their individual socioeconomic attributes or any past discrimination they may have faced, but instead on the potential positive influence these small businesses can have on the economy of those HUBZones.

Regarding the effectiveness of the HUBZone programme, particularly the price evaluation preference, the data concerning participation and successful awards of HUBZone small businesses does not provide a conclusive indication. At the federal

[1180] 13 CFR § 126.
[1181] HUBZone programme is place-based contracting assistance program with a primary objective to increase job creation and capital investment in distressed communities. See 15 USC § 657a.
[1182] 13 CFR § 126.103.

government level, the statutory spending target for HUBZone small business concerns is 3 per cent, and in practice, this goal has never been achieved from 2006 to 2023.[1183] Among the four categories of small businesses, HUBZone small businesses have the lowest level of participation in government procurement.[1184] One possible explanation is that the number of HUBZone small businesses is lower than that of other categories of small businesses. As of 8 May 2025, there are 4,532 businesses certified as HUBZone small businesses, compared to 15,613 for WOSB and 28,432 for SDVOSB, respectively.[1185] Over the years, the proportion of contracts awarded to WOSBs has consistently remained below 5 per cent, which is comparable to the percentage allocated to SDVOSBs.[1186] When examining the total value of contracts awarded to small businesses across socioeconomic categories, HUBZone firms may, on average, receive a higher value per business than others, even though the federal government's overall 3 per cent spending target for HUBZone contracts has not yet been met.

Secondly, regarding which component of the HUBZone programme has proven more successful in supporting HUBZone small businesses in securing more contracts, the evidence is not entirely clear either. Among the three components of HUBZone programmes, namely sole-source awards, HUBZone set-asides (reserved contracts),

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[1183] See Chapter 7, Section 7.3.5; also see SBA, 'Scorecard details Government-Wide Performance-2022' <https://www.sba.gov/federal-contracting/contracting-data/small-business-procurement-scorecard/scorecard-details?agency=GW&year=2022> accessed 16 August 2025.

[1184] The target for the overall federal government to contract with small business is 23 per cent, specifically, with small disadvantaged business (SDBs) is 5 per cent, with women-owned small business (WOSB) is 5 per cent, with service disabled veteran-owned small business (SDVOSB) is 5 per cent, and with HUBZone small business is 3 per cent. For a discussion of spending targets and how the performance of federal agencies, see Chapter 7, Section 7.3.5.

[1185] Blackford, 'Small Business Administration HUBZone Program' (n 1179). See SBA Dynamic Small Business Search (DSBS) (last modified 08 May 2025) <https://dsbs.sba.gov/search/dsp_dsbs.cfm> accessed 13 May 2025; also see Robert Jay Dilger, 'Small Business Administration HUBZone Program' (updated 24 May 2021, CRS Report R41268) <https://crsreports.congress.gov> accessed 24 May 2023.

[1186] For a discussion of spending targets and the performance of federal agencies, see Chapter 7, Section 7.3.5.

and 10 per cent price evaluation preferences, the price preference is mandatory for all contracting officers to implement in open and full competition, with a few exceptions.[1187] Regarding sole-source awards and set-asides, multiple categories of small businesses are eligible for such contracts, and the contracting officer possesses the discretion to reserve a contract for all small businesses or for one or more specific categories of small businesses.[1188] Consequently, HUBZone small businesses are not always prioritised above others.[1189] In contrast, other categories of small businesses are not granted bid preferences in federal procurement. Therefore, this 10 per cent bid preference appears to be the most dedicated preference for HUBZone small businesses.

Nevertheless, evidence indicates that the majority of HUBZone small businesses are awarded contracts through reserved contracts, rather than through price preferences.[1190] Contracts awarded to them due to price evaluation preferences only account for 0.63 per cent of all contracts awarded to HUBZone small businesses.[1191] Interestingly, most contracts are awarded through 'other applicable small business program'(57.92 per cent) and 'open competition with other firms' (24.21 per cent).[1192] Based on the data presented in Table 6.1, it appears that HUBZone small businesses derive greater benefits from small business set-asides compared to the specific HUBZone programme.[1193]

[1187] 15 USC § 657a.
[1188] See Chapter 7.
[1189] ibid.
[1190] Dilger (n 1185) 2.
[1191] ibid.
[1192] Dilger (n 1185) 2.
[1193] See Table 6.1.

Types of the procedure	HUBZone Small business set asides	Sole-source awards for HUBZone Small businesses [1194]	Price evaluation preference for HUBZone Small businesses	Open competition with other businesses[1195]	Other applicable small business preference programmes[1196]
Total value (billion)	1.9	0.095	0.0725	2.8	6.7

Table 6.1 Types of procedures of contract awarded to HUBZone small businesses[1197]

This evidence may be attributable to the fact that contracting authorities use small business preference programmes more frequently than the open and full competition procedure, where the bid preference for HUBZone small businesses is mandated. Another potential explanation is that HUBZone small businesses may not be able to offer a competitive bid, even with a 10 per cent bid preference, which suggests that they are not as competitive as other bidders. However, this does not account for why HUBZone small businesses have successfully secured contracts when the price preference is not used. Most likely, the explanation is that contracting officers rarely use open and full competition, which is mandated by bid preference. As a result, the impact of price evaluation preferences on HUBZone small businesses is uncertain.

Although it appears that HUBZone small businesses do not significantly benefit from the price evaluation preference, it affords them the opportunity to compete with all

[1194] 15 USC § 657a(c)(2)(A) allows sole-source contract without competition for HUBZone Small businesses. This seems to achieve a higher value than the price evaluation preference channels.
[1195] It is important to note that this is not the 'full and open competition' procedure, because if it is a 'full and open competition' procedure, HUBZone Small businesses are eligible for the 10 per cent price preference. Instead, 'open competition with other firms' may include reserved contracts for all small businesses, or GSA Schedules etc.
[1196] There are overlaps among different small business programmes, a HUBZone SB could also be a WOSB, or also a VOSDSB, thus, HUBZone Small businesses can also benefit from other SB programmes as long as they are eligible. See Chapter 7, Section 7.4.1.
[1197] Data is extracted from Dilger (n 1185) 2.

other firms, including large businesses, as opposed to reserved contracts, where they only compete among themselves or with other small businesses.[1198] However, among all certified HUBZone small businesses, only a small proportion receive substantial federal contracts, while the majority receive a much more limited value of contracts.[1199] The 2013 SBA Office of Inspector General (OIG) audit report revealed that twelve businesses accounted for 94 per cent of the federal contract value awarded to 357 HUBZone-certified firms during the period from July to December 2012.[1200] What is more concerning is that three of these twelve businesses failed to meet the requirements for HUBZone certification, which is partly attributable to the self-certification process conducted prior to November 2007.[1201] Overall, fewer than one-third of HUBZone areas have businesses that have won federal contracts, and only 4 per cent of those areas have achieved annual HUBZone contract revenue exceeding $100 per capita.[1202] These findings suggest that many HUBZone areas derive minimal benefit from the programme. Therefore, it is challenging to assert that the bid preference has effectively fulfilled its intended objectives. Given that federal agencies do not frequently use this bid preference, the likelihood that it may undermine the

[1198] For a detailed analysis of reserved contracts, see Chapter 7.

[1199] See GAO, 'Small Business Administration: Status of Efforts to Address Previous Recommendations on the HUBZone Program' (GAO-09-532T, March 25 2009) <https://www.gao.gov/assets/gao-09-532t.pdf> accessed 17 May 2025. The GAO argues that while the HUBZone programme can have positive economic effects if properly implemented, its benefits are highly uneven. In this report, there are almost no impact of HUBZone programme in about two-thirds of the HUBZones.

[1200] SBA, 'Performance Audit Report 14-03: Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications' (Novemebr 19, 2013) <https://www.sba.gov/document/report-14-03-audit-report-14-03-opportunities-exist-further-improve-quality-timeliness-hubzone-certifications> accessed 17 May 2025, 1.

[1201] ibid.

[1202] Dilger (n 1185) 28.

objectives of the federal procurement system, which prioritises best value alongside a balance of policy objectives, is minimal.[1203]

6.3.2 Bid preferences for small businesses in California

Although at the federal level, bid preferences only apply to HUBZone small businesses in open and full competition procedures, some states provide bid preferences for small businesses in award procedures.[1204] According to the State Preference Repository published by the National Association of State Procurement Officials (NASPO), there are mainly five types of bid preferences: in-state/local preference, reciprocal preference, tie bid preference, and vendor-based price preferences.[1205] A bid preference for small businesses is regarded as a vendor-based price preference, which is granted to small businesses because of their small size or individual socioeconomic characteristics.[1206] While many states have implemented bid preferences, these often target specific subcategories of small businesses, such as those owned by women or veterans.[1207] California has the most established state-level preference programmes for certified small businesses in state-funded procurement contracts.[1208] The 5 per cent bid preference for certified small businesses is codified

[1203] 48 CFR § 1.102. Also see Chapter 7, Section 7.3.1 for a discussion on principles and objectives of federal procurement.

[1204] NASPO (n 1166). In-state/local preference aims to encourage bidders/businesses to stay in a certain state, which is similar to the bid preference for local MSEs in Brazil. Reciprocal preferences are provided by a state in order to match a preference given by another state. Tie-bid preferences are used when there is a tie between an in-state bidder and a out-of-state bidder the former will be treated preferentially. Vendor-based price preferences or set-asides are preferences for small businesses or socioeconomic small businesses, which is the focus of this chapter.

[1205] ibid.

[1206] NASPO (n 1166).

[1207] ibid.

[1208] NASPO (n 1166).

in California Government Code 14838 (b)(1), which was established under the Small Business Procurement and Contract Act (SBPCA), enacted in 1978.[1209] This section focuses on California due to its longevity, comprehensive scope in the bid preference for small businesses, and extensive empirical evidence on the effect of these preference programmes.[1210]

6.3.2.1 Bid preferences for small businesses in California state procurement law

Section 14836 (b) of the California Government Code (CGC) stipulates that the state should support small businesses to the maximum extent to ensure that they secure a fair proportion of government procurement contracts.[1211] This mandate is similar to the 15 USC § 631(a) Small Business Act, with the same goal of ensuring small businesses secure a fair portion of public procurement contracts, which will be discussed in Chapter 7 in detail.[1212]

Under CGC Section 14838 (b)(1), when awarding contracts based on the lowest responsible bid that meets specifications, certified small businesses benefit from a 5 per cent bid preference.[1213] Practically, this means that for assessment purposes alone, the bid of such an entity is adjusted downward by 5 per cent to determine whether it ranks as the lowest bid. For instance, if a large business submits a bid of

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[1209] California Government Code (CGC) § 14838(b)(1); Small Business Procurement and Contract Act (California Government Code §§14835 – 14843) (US, California).

[1210] ibid; Elena Krasnokutskaya and Katja Seim, 'Bid Preference Programs and Participation in Highway Procurement Auctions' (2011) 101 American Economic Review 2653, 2654.

[1211] CGC § 14836 (b). With regards to the definition of small businesses, it is required that their principal office is located in California, and their officers, who are domiciled in California, and the number of employees shall not exceed 100, and the average annual gross receipts shall not exceed USD 10,000,000. See Section 14837 (d)(1) California Government Code.

[1212] See Chapter 5, Section 5.3.

[1213] CGC § 14838 (b)(1).

USD 100,000 and a certified small business bids USD 104,000, the latter is treated as having bid USD 98,800 for evaluation purposes. If the small business is successful, it is awarded the contract at its actual bid price of USD 104,000. In procurement procedures where a best-value criterion is used, which includes more factors than price, a 5 per cent scoring advantage is similarly applied to small businesses.[1214] As the price difference between the original lowest bidder and the awarded small business is absorbed by the state contracting authority, a maximum preference limit of USD 50,000 is imposed on any bid.[1215] This restriction aims to prevent an undue increase in costs for substantial contracts to facilitate small business participation.

6.3.2.2 The effect of bid preference on small businesses and contracting authorities in California

The effect of a bid preference on small and large businesses will depend on the magnitude of the preference.[1216] If the preference is set too low, small businesses may lack the motivation to submit bids, while large businesses might continue their usual bidding behaviour or adopt a more aggressive stance. Conversely, if the bid preference is excessively high, small businesses will be more motivated to participate and have a greater likelihood of winning; however, large businesses may lose interest in bidding altogether. The effects of a bid preference on small businesses include two aspects, on the one hand, the potential effect of a bid preference on small businesses who have participated in bidding, the potential effect is whether the bid preference

[1214] CGC § 14838 (b)(2) requires that 'the preference to small business or microbusiness shall be 5 percent of the highest responsible bidder's total score'. See Section 14838 (b)(2) California Government Code.

[1215] CGC §14838(b)(1)-(4).

[1216] Krasnokutskaya and Seim (n 1210) 2654.

could increase the probability of them being in awarded the contract; on the other hand, a bid preference may encourage those small businesses who have never participated in bidding before to enter bidding.

In 2007, Marion observed that under California's 5 per cent price preference, the value of contracts awarded to small businesses increased by 20 per cent, and the proportion of small business contractors in all contractors increased.[1217] They are more likely to win in auctions with a bid preference for them than in auctions without one.[1218] Similarly, Krasnokutskaya and Seim found a significant increase in small business participation and winning probability due to the 5 per cent price preference.[1219] Moreover, there is an increase in small business profits due to the bid preference, varying between 5 per cent and 16 per cent (with an average increase of 10.4 per cent).[1220] Although the number of large bidders in these procedures decreased, the total number of bidders in the procurement market remained largely stable, which suggests that the increase in small business participation effectively offsets the decrease in large business participation.[1221] The recent data further confirms the increase in small business participation, which constitutes 25.58 per cent of the total government procurement value in California 2023-2024.[1222] The statutory small business contracting goal in California was formally introduced through Assembly Bill 2019, which codifies a 25 per cent small business contracting goal.[1223] It is the sixth

[1217] Marion (n 128). However, this effect is marginal, as only the results of 5 per cent of auctions were altered, which means, in most cases, small businesses could have won without the bid preference, or that large businesses remain the lowest bidder.
[1218] Marion (n 128) 1600.
[1219] Krasnokutskaya and Seim found that a price preference significantly increases both their participation and their probability of winning contracts. Krasnokutskaya and Seim (n 1210) 2681.
[1220] ibid 2681.
[1221] Krasnokutskaya and Seim (n 1210) 2679; also see Marion (n 128).
[1222] See California Consolidated Annual Report, Fiscal Year 2023-2024, 2.
[1223] See Assembly Bill 2019 (2022 Regular Session) (California).

time (nonconsecutively) that the small business contracting goal is exceeded within 10 years.[1224]

Krasnokutskaya and Seim also found that bid preferences are more effective in contracts where small businesses traditionally struggle to participate, which is, contracts with a low small business participation rate, compared to contracts where small businesses are already well-represented.[1225] This reinforced the hypothesis that this chapter proposed in Section 6.2.3, that bid preferences may be more beneficial in contracts where small businesses are less represented and redundant in contracts where small businesses are already strong players.[1226]

As for the effect of bid preference on contracting authorities in terms of procurement costs, there is nuanced evidence. Intuitively, granting a 5 per cent bid preference to small businesses may increase public procurement costs, since higher-priced bids can prevail over lower-cost ones within the scope of the preference. However, McAfee and McMillan demonstrate that the government could minimise procurement costs by selecting an optimal preference level.[1227] Following McAfee and McMillan's theoretical analysis, Corns and Schotter find that a 5 per cent bid preference would increase competition and lower the procurement costs, whereas a 10 per cent or 15 per cent preference would increase the procurement costs.[1228] This demonstrates that granting

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[1224] See Office of Small Business and DVBE Services, Department of General Services, 'California Consolidated Annual Report, Fiscal Year 2023-2024' <https://www.dgs.ca.gov/-/media/Divisions/PD/OSDS/Certification/CAR/202324-Consolidated-Annual-Report042125.pdf> accessed 17 May 2025.

[1225] Krasnokutskaya and Seim (n 1210) 2678.

[1226] See Section 6.2.3.

[1227] R Preston McAfee and John McMillan, 'Government Procurement and International Trade' (1989) 26 Journal of International Economics 291.

[1228] Allan Corns and Andrew Schotter, 'Can Affirmative Action Be Cost Effective? An Experimental Examination of Price-Preference Auctions' (1999) 89 American Economic Review 291.

a bid preference to a certain group of bidders will not necessarily increase the costs, might even lower the costs; what matters the most is the size of the preference.

In practice, Marion examined hundreds of California highway construction auctions and compared outcomes between state-funded projects where the 5 per cent preference was applied, and similar federally-funded projects where the 5 per cent preference was not applied.[1229] Marion found that the average winning bid on state-funded contracts was about 3.8 per cent higher than on comparable federal-funded procurement contracts without bid preferences.[1230] However, the 5 per cent bid preference for small businesses does not represent the only distinction between state-funded and federally funded contracts, implying that the 3.8 per cent cost increase may be attributable to additional factors beyond the bid preference for small businesses.[1231]

Later research by Krasnokutskaya and Seim in 2011 built on Marion's study with a more structural econometric analysis of California's highway auctions, accounting for bidder behaviour changes induced by the preference.[1232] By modelling firms' entry and bidding decisions, Krasnokutskaya and Seim simulated procurement decisions under scenarios with and without the bid preference.[1233] They find that if the participation of large businesses and small businesses remains fixed, meaning that their participation decisions do not change, regardless of whether there is a bid preference for small

[1229] Marion examined procurement auctions conducted by California Department of Transportation (Caltrans). Caltrans provides a bid preference for small businesses in auctions for road construction contracts. See Marion (n 128).
[1230] ibid.
[1231] Marion (n 128).
[1232] Krasnokutskaya and Seim (n 1210).
[1233] ibid.

businesses or not, the costs of the contracting authorities remain unchanged.[1234] When participation decisions are endogenous, meaning that large businesses and small businesses change their participation in response to a bid preference, the 5 per cent preference only increased California's highway procurement costs by less than 1 per cent, which suggests that the cost impact of bid preference is much smaller than Marion's estimate.[1235] In a similar study, Rosa used data from New Mexico and found that using a 5 per cent bid preference only led to an approximate 1.2 per cent increase in procurement costs, suggesting that such preferences can achieve policy objectives with relatively modest efficiency losses.[1236]

6.3.3 Summary

Both the 10 per cent bid preference for HUBZone small businesses in federal procurement and 5 per cent bid preference for small businesses in California are intended to bolster their participation and success in public procurement. The existing empirical evidence indicates the California scheme has been effective, while the HUBZone price preference's impact has been more limited. Although the extent of the bid preference (10 per cent) is larger in the HUBZone programme, it has not been used frequently by federal agencies. Instead, they primarily use reserved contracts to

[1234] Krasnokutskaya and Seim (n 1210).

[1235] ibid 2656. An increase of approximately 0.5 per cent in most procurement contracts. There is an estimated 0.23 per cent cost increase with a large bid preference, which suggests that bid preferences only incur minor changes in procurement costs when bidder participation is held fixed.

[1236] Benjamin Rosa, 'Resident Bid Preference, Affiliation, and Procurement Competition: Evidence from New Mexico' (MPRA Paper 68759, University Library of Munich 2016) <https://mpra.ub.uni-muenchen.de/68759/1/MPRA_paper_68759.pdf> accessed 17 May 2025.

meet the 3 per cent contracting goal with HUBZone small businesses, although this goal has never been achieved.[1237]

Regarding the impact of bid preferences on contracting authorities, both the HUBZone preference and California's preference for small businesses may induce extra costs, as contracting authorities would award the contract to a slightly higher bid. However, the cost increase is moderate, as large businesses (non-favoured bidders) tend to bid more aggressively in those auctions where a bid preference is granted to small businesses.[1238] The price difference between tenders submitted by small businesses and large businesses tend to be larger in procedures where small businesses are provided a bid preference.[1239] As estimated by Corn and Schotter, a well-calibrated preference can spur enough additional competition from small businesses to maintain low prices, effectively balancing equity and efficiency.[1240] However, if the preference is too large, especially more than 10 per cent, the value for money of a procurement procedure may be compromised.[1241] As McAfee and McMillan highlighted, if the profits of those favoured bidders are more desired than the profits of the unfavoured bidders, the additional costs of this redistribution may be justified.[1242] In this case, it is not a legal question nor an economic question, but more of a policy decision whether or not to do this redistribution of welfare, which could be observed in the use of bid

[1237] See Chapter 7.

[1238] Ian Ayres and Peter Cramton, 'Deficit Reduction Through Diversity: How Affirmative Action at the FCC Increased Auction Competition' (1996) 48 Stanford Law Review 761.

[1239] As Marion has observed, in auctions without the bid preference, small businesses bid 1.6 per cent higher than large businesses, but 3.1 per cent higher than large businesses in auctions with a bid preference for small businesses. This suggests that in auctions with a bid preference for small businesses, large businesses bid more aggressively, and small businesses bid less aggressively. See Marion (n 128).

[1240] Corns and Schotter (n 1228)

[1241] ibid.

[1242] McAfee and McMillan (n 1227).

preferences in South Africa to compensate historically disadvantaged individuals, as discussed in Section 6.4.

6.4 Bid Preferences in South Africa Preferential Procurement System

Before the democratic transition in South Africa in 1994, public procurement contracts were primarily accessible to large and established businesses, which were predominantly white-owned, due to the discriminatory policies and socio-economic structures entrenched by the Apartheid regime.[1243] Consequently, small businesses, particularly those owned by historically disadvantaged individuals (HDIs), notably black entrepreneurs, faced significant barriers in securing public contracts.[1244] In response to these historical inequalities among different races, the 1996 Constitution explicitly recognises public procurement as a crucial strategic instrument for addressing past inequalities resulting from apartheid and advancing economic transformation.[1245] These objectives were later formalised through the Broad-Based Black Economic Empowerment (BBBEE) Act 2003.[1246] At the same time, the

[1243] Under apartheid, government subsidies and procurement favoured white-owned businesses and excluded black-owned businesses, reinforcing racial inequalities. For an overview of the concentration of economic resources and business ownership under the apartheid regime, see Nicola Nattrass and Jeremy Seekings, *Class, Race, and Inequality in South Africa* (Yale University Press 2005).

[1244] See Bolton (n 17) 194. In Preferential Procurement Regulations (PPR) 2001, HDIs are defined as South African citizens '(1) who, due to the apartheid policy that had been in place, had no franchise in national elections prior to the introduction of the Constitution of the Republic of South Africa,1983 (Act No 110 of 1983) or the Constitution of the Republic of South Africa,1993 (Act No 200 of 1993); and / or (2) who is a female; and / or (3) who has a disability'. However, in PPR 2011, the definition of HDIs was deleted, instead, the focus was mainly on BBBEE and bidders' contribution to specific goals correspond to specific BBBEE levels. See Preferential Procurement Regulations (PPR), 2001, GN R725 in GG 22549 of 10 August 2001; PPR, 2011, GN R502 in GG 34350 of 8 June 2011.

[1245] Constitution of the Republic of South Africa, 1996 (South Africa Constitution) s 217(1).

[1246] See Bolton (n 17); Lerato Shai, Comfort Molefinyana and Geo Quinot, 'Public Procurement in the Context of Broad-Based Black Economic Empowerment (BBBEE) in South Africa—Lessons Learned for Sustainable Public Procurement' (2019) 11 Sustainability 7164, 7184; Christian Helmrich, 'Equality-

Constitution ensures that procurement activities shall be conducted in a manner that is 'fair, equitable, transparent, competitive, and cost-effective'.[1247] Nevertheless, in recognition of the unique historical context, Section 217 (2) permits an exception to these principles by allowing preferential procurement to protect or advance individuals or groups disadvantaged by unfair discrimination. This provision affirms that addressing inequality is a legitimate constitutional objective of public procurement in South Africa.[1248] The Preferential Procurement Policy Framework Act (PPPFA) of 2000 operationalised this constitutional mandate through a structured, point-based tender evaluation system, which will be discussed in Section 6.4.1.[1249]

It is essential to note that there is no standalone statutory preference explicitly designed for SMEs in the public procurement system in South Africa. Although there is a legal definition of SMEs in the National Small Business Act 102 of 1996, this definition was not referred to in the PPPFA or BBBEE.[1250] Rather, the BBBEE proposed two categories of SMEs: exempted micro enterprises (EMEs) and qualifying small enterprises (QSEs), and the procurement regulations adopted these new definitions of SMEs.[1251] Preferences explicitly granted through procurement procedures generally target HDIs and economic empowerment goals linked to correcting historical racial inequalities.[1252] Consequently, SMEs benefit from

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Oriented Horizontal Policies in South African Public Procurement' (2015) 1 African Public Procurement Law Journal 70 <http://applj.journals.ac.za/pub/article/view/7> accessed 18 March 2025.

[1247] South Africa Constitution s 217(1), (2).

[1248] ibid.

[1249] The PPPFA remains in force as the PPA 2024 has been enacted but is not yet in operation.

[1250] See National Small Business Act 102 of 1996 as amended by National Small Enterprise Amendment Act 21 of 2024 (South Africa); also see Chapter 2, Section 2.5.

[1251] For the detailed size criteria of EMEs and QSEs, see Chapter 2, Section 2.5.

[1252] BBBEE Codes of Good Practice, paras 4–5 (South Africa).

preferential procurement primarily when they also qualify as EMEs or QSEs against the BBBEE criteria.[1253]

6.4.1 Bid preferences in the PPPFA

The PPPFA is a short piece of legislation, containing only six sections.[1254] Section 2 (1) (b) PPPFA establishes a point-based system utilised during the tender evaluation stage to balance price considerations with socio-economic policy objectives.[1255] Under this framework, tenders are evaluated according to two primary criteria: price and contribution to specific goals.[1256]

While the later-enacted BBBEE legislation explicitly aims at racial transformation and economic empowerment of black South Africans, the specific goals under the PPPFA framework initially provided a broader approach that could accommodate various policy objectives, potentially overlapping but distinct from what became formalised through BBBEE.[1257] Section 2 (1) (d) (i) PPPFA stipulates that specific goals may include contracting with persons historically disadvantaged by unfair discrimination based on race, gender, or disability.[1258] Moreover, specific goals may also include 'implementing the programmes of the Reconstruction and Development Programme',

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[1253] ibid.

[1254] PPPFA.

[1255] PPPFA, s 2(1)(d)(i).

[1256] Section 2 (1)(d)(i) PPPFA stipulates that specific goals may include contracting with persons historically disadvantaged by unfair discrimination based on race, gender, or disability. Section 2 (1) (c) PPPFA stipulates that higher-priced tenders score fewer points on a pro-rota basis. To illustrate the calculation process, PPR 2011 provides that the points are calculated based on the difference between the tender and the lowest acceptable tender. P (points) = 80 * (1- (Pt-Pmin)/ Pmin). See PPPFA, s 2(1)(d)(i); PPR 2011 s 5.

[1257] PPPFA, s 2(1)(d)(i).

[1258] PPPFA, s 2(1)(d)(i).

which include policies to boost the SME sector.[1259] Section 2 (2) PPPFA requires that 'any goals contemplated in subsection 1 (e) must be measurable, quantifiable and monitored for compliance'.[1260] To ensure transparency, any specific goal used to evaluate tenders has to be clearly specified in the invitation to submit a tender.[1261] For procurement contracts above a prescribed threshold, 90 points are allocated for price and 10 points for contribution to a specific goal.[1262] For contracts below this threshold, the system awards 80 points based on price and 20 points for specific goals, reflecting a greater emphasis on achieving socio-economic transformation in lower-value contracts.[1263] In this system, price remains the dominant factor in tender evaluation, carrying 80 or 90 per cent of the available points.[1264]

The identification and measurement of contributions to specific goals are elaborated in the Preferential Procurement Regulations (PPR) 2001.[1265] After the BBBEE Act was enacted, PPR 2011 was updated to include more linkage to bidders' BBBEE status.[1266] The BBBEE Code of Good Practice classify enterprises according to their contribution levels, ranging from Level One (highest) to Level Eight (lowest).[1267] A company's level reflects its contribution to empowering historically disadvantaged groups through criteria such as black ownership, management control, skills development, enterprise development, and socio-economic investment.[1268] Thus, a Level One BBBEE

[1259] PPPFA, s 2(1)(e).
[1260] PPPFA, s 2(2).
[1261] PPPFA, s 2(1)(e).
[1262] ibid.
[1263] PPPFA, s 2(1)(b).
[1264] PPPFA, s 2(1)(b).
[1265] PPR 2001, pt 2.
[1266] See PPR 2011, s 10.
[1267] BBBEE Code of Good Practices, paras 4-5.
[1268] ibid.

contributor, which demonstrates the highest level of empowerment compliance, would secure the maximum points available for the 'specific goals' criterion, 20 points in an 80/20 evaluation and 10 points in a 90/10 evaluation.[1269] Similarly, a Level Two contributor receives slightly fewer points, for example, 19 points under the 80/20 scoring system, effectively obtaining 95 per cent of the maximum 'specific goals' points.[1270]

Since BBBEE was enacted, the BBBEE level has been a leading indicator of whether specific goals could be achieved.[1271] The BBBEE Act and its associated Codes of Good Practice explicitly distinguish enterprises based on ownership structure and annual revenue.[1272] For instance, enterprises fully owned by black individuals typically qualify as Level One contributors.[1273] The only exception is EMEs, which are defined as enterprises with an annual revenue of R10 million or less, irrespective of ownership, and they automatically receive a minimum BBBEE status of Level Four.[1274] If an EME is owned by black individuals, it can be qualified for a higher BBBEE level. EMEs and Qualifying Small Enterprises (QSEs), which have an annual revenue between R10 million and R50 million, qualify for Level One status if they are 100 per cent black-owned, whereas those at least 51 per cent black-owned qualify as Level Two contributors.[1275]

[1269] BBBEE Code of Good Practices.

[1270] ibid.

[1271] See John Derek Taylor and Kishore Raga, 'Preferential Procurement: A Case Study of South Africa' (Paper presented at the 4th International Public Procurement Conference, Seoul, South Korea, 26–28 August 2010) <https://www.ippa.org/ippc4_proceedings2.html> accessed 17 April 2024.

[1272] BBBEE Code of Good Practices, para 2.

[1273] ibid.

[1274] BBBEE Code of Good Practices para 2.

[1275] Ibid para 2.

The structure of the point-based preferential procurement system underscores an intentional prioritisation of racial economic empowerment, emphasising the advancement of black ownership and management, rather than solely supporting small businesses or SMEs irrespective of racial ownership.[1276] Nonetheless, the PPPFA provides an exception by ensuring EMEs, even if white-owned, retain a baseline status of Level Four, enabling them to secure a substantial portion of the points allocated to the specific goals during tender evaluation.[1277] This design strategically integrates both small enterprise development and black economic empowerment objectives, but places more emphasis on rectifying racial inequalities resulting from the legacy of apartheid.[1278]

In practice, the implementation of the point-based system is not satisfactory. The problems are broadly of two types: a problem with the point-based evaluation system itself, and the problems with the emphasis on BBBEE. BBBEE evaluation has overly broad and multi-dimensional criteria, including ownership for 25 points, management control for 19 points, skills development for 20 points plus 5 bonus points, supplier development for 40 points, and socio-economic investment for 5 points.[1279] Consequently, large businesses, predominantly white-owned businesses, may also achieve Level One contributor status through high scores in supplier or skills development, so that they often secure preferential points.[1280] Thus, the intended objective of empowering historically disadvantaged people is largely compromised.

[1276] Shamila Singh, Lindiwe Nkwe and Anis Mahomed Karodia, 'An Analysis of the Preferential Procurement Regulations: A Case Study of the Department of Communications, Pretoria (South Africa)' (2015) 5 Oman Chapter of Arabian Journal of Business and Management Review 90.
[1277] BBBEE Code of Good Practices, para 2.
[1278] Bolton (n 17).
[1279] BBBEE Code of Good Practices.
[1280] Shai, Molefinyana and Quinot (n 1246).

6.4.2 The recent development of preferential procurement in the 2024 Public Procurement Act

Aligned with Section 217 (2) Constitution, the primary purpose of the Public Procurement Act 2024 (PPA 2024) is not only to regulate public procurement but also to establish a framework to implement preferential procurement.[1281] Notably, the PPA 2024 explicitly acknowledges that previously existing procurement legislation has constrained the advancement of historically disadvantaged persons or groups, implying inherent limitations in the point-based system with bid preferences. [1282] Especially, the enactment of the PPA 2024 signifies a transformation in the approach to preferential procurement, moving from a traditionally point-based evaluation method towards a regime emphasising prequalification criteria and reserved contracts (set-asides).[1283] This shift reflects legislators' recognition of the inherent complexities and weaknesses of the point-based system established under the PPPFA. [1284] Such complexities include ambiguous criteria, susceptibility to fronting, and limited impact in promoting the sustainable economic development of businesses owned by historically disadvantaged people.[1285]

[1281] PPA 2024.

[1282] Emphasis added. PPA 2024, Preamble.

[1283] See PPA 2024, ch 4. This transition can be traced back to PPR 2017, which, for the first time, introduced mechanisms explicitly allowing contracting authorities reserving contracts for certain types of businesses and using prequalification criteria to protect certain types of businesses from broader competition. See PPR 2017 in GG 40553 of 20 January 2017, s 3-4. For a commentary on PPR 2017, see Geo Quinot, 'The Third Wave of Preferential Procurement Regulations in South Africa' <http://hdl.handle.net/10019.1/107494> accessed 31 December 2024, 857, 862.

[1284] PPA 2024, Preamble.

[1285] Bolton (n 17).

Under the new set-aside rule, an organ of a state can decide to restrict the competition only among a certain category of bidders, which can be understood as a reserved contracts regime or an additional pre-qualification requirement, where bidders not satisfying the pre-qualification criteria are excluded from this competition.[1286] When the draft of the 2017 PPR was published and opened for public comment, an intriguing case emerged wherein Afribusiness NPC, a non-profit organisation, submitted an application contending that the Minister of Finance exceeded the powers conferred upon it by Section 217 Constitution, as the 2017 PPR introduced a method utilising prequalification criteria to ensure that certain contracts were exclusively accessible to specific groups businesses.[1287] For instance, the prequalification criteria might include a minimum BBBEE status level of contributor for the tenderer, or require subcontracting at least 30 per cent of the contract to an 'EME or QSE that is at least 51 per cent owned by black people'.[1288] The Supreme Court decided that organs of state have the discretion to implement any stipulated prequalification criteria, as they are compliant with the Procurement Act and Section 217 Constitution. Consequently, businesses that benefited from the old regime might no longer have access to certain contracts in the new regime.[1289]

Although the 2022 PPR did not incorporate reserved contracts, the PPA 2024 emphasises the utilisation of set-asides to facilitate preferential procurement, marking a significant transition from the original point-based bid preference system to reserved contracts.[1290] Both the 2022 PPR and PPA 2024 appear to weaken the consideration

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[1286] See PPA 2024, ch 4.
[1287] *Minister of Finance v Afribusiness NPC* [2022] ZACC 4, paras 8, 108–110.
[1288] See BBBEE Code of Good Practices.
[1289] *Minister of Finance v Afribusiness NPC* [2022] ZACC 4, para 91.
[1290] PPA 2024, ch 4.

of BBBEE, as organs of state are not required to consider BBBEE, but they can still take the BBBEE status level into account in their preference point scoring.[1291] The 2022 PPR allows contracting authorities to consider other specific goals in their procurement processes.[1292] This means, for example, that a department could designate that a certain percentage of its contracts in a year, or specific tenders, are open only to businesses with a defined minimum HDI ownership or to small black-owned enterprises. The new regime will provide contracting authorities with more discretion regarding the policy objectives they intend to achieve and the form of preference they choose.[1293] The effect of the new regime under PPA 2024 is yet to be observed, as it is still not in force as of August 2025.[1294]

6.4.3 The effectiveness of point-based preferences

It is evident that in South Africa, the promotion for SMEs through public procurement is not based on their economic attributes, but rather on social attributes, except for microenterprises. For example, it has been argued that white women-owned small businesses are not empowered compared with black women-owned small businesses.[1295] The primary objective of the preferential procurement is to provide

[1291] ibid; PPR 2022 in GG 47452 of 4 November 2022.
[1292] PPR 2022.
[1293] Pippa Reyburn, Yana van Leeve, and Sibongile Sibeko, 'New Preferential Procurement Regulations will give state organs more discretion to implement their own procurement policies' (ENSight) <https://www.ensafrica.com/news/detail/6438/new-preferential-procurement-regulations-will> accessed 18 April 2024.
[1294] PPA 2024, s 69(1).
[1295] Maritz (n 294) 76.

advantages to individuals and enterprises historically subjected to discrimination, rather than to develop the SME sector per se.

However, concerns have been raised that preferential procurement policies may disproportionately favour established businesses, including those that were once disadvantaged but no longer face systemic barriers. Accordingly, it has been suggested that the eligibility for such programmes shall be based on businesses' performance in procurement and be time-limited.[1296] Consequently, after a few years of benefiting from the programme, they are expected to graduate from the programme, an approach that the US adopted in one of the small business programmes, which will be discussed in Chapter 7.

Such concerns are not unique to South Africa or to bid preference systems; similar issues will be discussed in Chapter 7 in relation to reserved contracts for small businesses in the US federal procurement system.[1297] From an economic perspective, providing preferences to certain business groups risks creating perverse incentives, whereby beneficiaries may have limited motivation to grow beyond the eligibility thresholds, thereby remaining perpetually dependent on preferential treatment.[1298] From a social perspective, the challenge is even greater, as certain social attributes of the preferential group do not change over time, unlike economic size. Thus, some enterprises in the preferential group may become sufficiently experienced and competitive to succeed without assistance. Continued eligibility under these

[1296] Alejandro Simone and Vybhavi Balasundharam, 'Public Procurement in South Africa: Issues and Reform Options' (IMF Selected Issues Paper SIP/2023/041, International Monetary Fund 5 May 2023) <https://www.elibrary.imf.org/view/journals/018/2023/041/article-A000-en.xml> accessed 17 May 2025, 12. This aspect will be explored further in the Chapter 8.

[1297] See Chapter 7.

[1298] ibid.

circumstances may hinder newly established businesses, particularly those truly in need of support but unfamiliar with complex procurement systems, from accessing opportunities.[1299]

Although the preferential procurement regime has arguably contributed to the redistribution of economic opportunities between racial groups, significant criticisms persist.[1300] Preferential procurement, especially linked with the BBBEE policies, has often been regarded as facilitating the 'enrichment of the few', benefitting primarily the black middle class and large black-owned businesses, rather than fostering broader socioeconomic equality.[1301] As noted, 'the state budget would appear far more distributive in racial terms but far less redistributive in socioeconomic terms'.[1302] It could be due to the reason that the criteria for benefiting from the point-based preferences can be manipulated by large businesses and individuals who do not need support, whereas those who are in need of support, often represented by MSEs, might find it difficult to navigate the point-based system.

Enforcement measures within the preferential procurement framework primarily target the issue of 'fronting', a practice in which black individuals are used as nominal shareholders in companies effectively controlled by white owners, allowing such companies to illegitimately benefit from preferential treatment.[1303] These observations reveal the inherent risks associated with bid preference systems, including the risks of window-dressing and fronting. Such risks undermine the true purpose of preferential

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[1299] See Chapter 8, Section 8.4.2.

[1300] Geo Quinot, 'Promotion of Social Policy through Public Procurement in Africa' in Geo Quinot and Sue Arrowsmith (eds), *Public Procurement Regulation in Africa* (Cambridge University Press 2013).

[1301] Nattrass and Seekings (n 1243) 344.

[1302] ibid, 365.

[1303] Bolton (n 17) 212.

procurement, increasing doubt on whether the policies genuinely enable disadvantaged businesses to become more competitive.

Moreover, given the complexity of the preference points system, small bidders owned by historically disadvantaged individuals, especially those with limited resources, may struggle to navigate the rules or may be discouraged from seeking to benefit from them at all. In this respect, simpler mechanisms such as reserved contracts may be better suited to supporting those bidders, as the complexity of bid preference frameworks can sometimes allow larger, established businesses to manipulate the system to their advantage. The comparison between the reserved contract and bid preferences will be further developed in the Conclusion chapter.

6.5 Conclusion

Preferential procurement measures inherently introduce an element of unequal treatment, necessitating careful balance with fundamental public procurement principles such as transparency, proportionality, fairness, and value for money.[1304] This chapter examines different approaches to granting bid preferences, drawing on selected national examples, and highlights the complex interplay between preferences for certain categories of bidders and broader socioeconomic policy objectives.

Brazil's approach provides an important starting point, as its bid preferences prominently emphasise economic objectives through explicit support for MSEs, rather than addressing historical inequalities based on race or socioeconomic background.

[1304] Marion (n 128).

Significantly, Brazil imposes clear thresholds on contract value eligible for preferential treatment, reflecting a deliberate policy design intended to mitigate the risks to performance standards and cost efficiency associated with awarding large contracts to potentially less-experienced MSEs. Empirical evidence suggests that MSEs, while benefiting from increased market participation, may indeed increase the risk of contract underperformance or default, underscoring the importance of balancing support for MSEs with other objectives such as value for money.

The US experience of HUBZone bid preference and state preferences for small businesses, illustrated by California's 5 per cent preference, highlights the varied effectiveness of bid preferences. California's bid preference has successfully increased small business participation and their likelihood of winning contracts. In contrast, the federal HUBZone programme applies to limited scenarios, and its overall impact on enhancing participation of HUBZone small businesses has been minimal.

The preferential procurement system in South Africa, initially reliant on a point-based mechanism linked explicitly to redressing historical discrimination and promoting BBBEE, faced considerable practical limitations. Despite fostering greater participation among historically disadvantaged enterprises, administrative complexities and fronting by large businesses undermined its transformative potential. The recent shift in the PPA 2024 toward reserved contracts or prequalification criteria represents a conscious legislative recognition of these shortcomings, suggesting a deeper acknowledgement that bid preferences alone are insufficient without

complementary structural adjustments, which will be discussed further in the Conclusion Chapter.[1305]

The analysis demonstrates that bid preferences, on their own, rarely operate as comprehensive policy instruments capable of achieving the objectives of supporting SMEs or advancing broader socio-economic goals. Without complementary measures, preferences risk being captured by a small group of experienced firms, sometimes large companies fronting as eligible businesses, or entrenched SMEs within the beneficiary group. For the majority of SMEs lacking prior procurement experience, a preference at the evaluation stage does not lower the entry barriers faced by SMEs, such as large contract size and excessive qualification criteria.[1306] Bid preferences become more effective when combined with targeted facilitative measures that address structural obstacles faced by the intended beneficiaries. Such measures include dividing large contracts into lots, reducing bureaucratic and compliance burdens, and tailoring qualification criteria to enable smaller bidders, as discussed in Chapters 4 and 5. The selection and combination of such measures will be further examined in Chapter 8.

[1305] See Chapter 8, Section 8.5.
[1306] See Chapter 3.

Chapter 7 Reserving Contracts for Small Businesses in Public Procurement

7.1 Introduction

Previous chapters examined three distinct measures aimed at reducing entry barriers or granting preferences in tender evaluations for SMEs. As the concluding chapter on SME-friendly measures, this section concentrates on reserved contracts, which constitute the most robust form of protection for SMEs, compared with the other three measures analysed in this thesis. A comparison of these four measures will be discussed in Chapter 8.[1307]

Reserved contracts have been adopted in a few jurisdictions, but the scope of beneficiaries in such regimes differs due to various objectives.[1308] For example, in the EU, reserved contracts are strictly limited to sheltered workshops or social enterprises and economic operators whose main aim is to integrate disabled and disadvantaged persons socially and professionally.[1309] This represents the use of reserved contracts to achieve social objectives through awarding public procurement contracts to those limited economic operators. Brazil also has a reserved contracts regime for micro and small enterprises (MSEs), but its scope is much more restricted and relatively new, having been included in LC 147/2014.[1310] Among all the jurisdictions that have

[1307] See Chapter 8, Section 8.4.

[1308] Xinyue Xue, 'Empowering Small Businesses: The Impact of Reserved Contracts in U.S. Federal Procurement' (SAPIENS Working Paper July/2024) <https://sapiensnetwork.eu/empowering-small-businesses-the-impact-of-reserved-contracts-in-u-s-federal-procurement-working-paper-series/> accessed 16 June 2025.

[1309] Directive 2014/24/EU, art 20.

[1310] Chapter 6, Section 6.2; also see LC 123/2006 (amended by LC 147/2014), art 48.

incorporated reserved contracts in public procurement law, the US maintains the most extensive set-aside programme for small businesses, accompanied by various set-aside programmes for socioeconomic small businesses.[1311] This chapter focuses on US federal procurement, in view of its long-standing policy and extensive experience with reserving contracts for small businesses.[1312]

The objective of this chapter is to assess whether reserved contracts (or 'set-asides') effectively achieve the intended objectives, and if they undermine other objectives in federal procurement.[1313] Section 7.2 traces the historical development and underlying purpose of small business set-asides. Section 7.3 examines the regulatory framework of reserving contracts for small businesses in US federal procurement. Section 7.4 then evaluates whether the reserved contracts regime has, in practice, achieved the objectives identified in Section 7.2, and the balance between SME support and other objectives in federal procurement, such as competition, value for money, and efficiency. While the Federal Acquisition Regulation (FAR) refers to 'set-asides', academic literature usually uses the term 'reserved contracts'.[1314] This chapter uses these two terms interchangeably.

[1311] Kirkwood (n 106) 311; John Linarelli, 'The Limited Case for Permitting SME Procurement Preferences in the WTO Agreement on Government Procurement' in Sue Arrowsmith and Robert D Anderson (eds), *The WTO Regime on Government Procurement: Challenge and Reform* (Cambridge University Press 2011) 444.

[1312] The focus on federal rather than state set-aside programmes has been explained in Chapter 1, Section 1.4. For state and local set-aside programmes, see George R. LaNoue, 'Split Visions: Minority Business Set-Asides' (1992) 523 Annals of the American Academy of Political and Social Science 104, 110.

[1313] See Section 7.3.1.

[1314] See 48 CFR § pt 19. In the FAR, the term 'reserves' refers specifically to reserved contracts under Multiple Award Contracts (MACs), which differ from reserved contracts in the general sense. This distinction is examined further in Section 7.3.2.3.

7.2 The Purpose of Small Business Set-asides

Promoting small business participation in federal procurement has been a longstanding policy objective and a bipartisan endeavour in the US since the mid-20th century.[1315] The origin of small business set-asides can be traced back to the Second World War and the Korean War, during which small businesses struggled to sustain their operations due to limited access to capital, contracts, and resources.[1316] In response, Congress enacted the Defense Production Act of 1950, establishing the Small Defense Plants Administration to assist small businesses in securing federal procurement opportunities.[1317] Following the conclusion of the Korean War, Congress enacted the Small Business Act (the Act) in 1953, establishing the Small Business Administration (SBA) as a statutory agency and consolidating federal small business support within a standing institutional framework, subject to ongoing congressional oversight.[1318]

Section 631(1) of the Act articulates the statutory rationale for federal support of small businesses, based on their essential contribution to the economic well-being and security of the nation.[1319] This provision assumes that these broader objectives cannot be attained without free competition, which in turn depends on the *actual and potential*

[1315] R. Corinne Blackford, 'An Overview of Small Business Contracting' (CRS Report R45576, updated May 14, 2024) <https://crsreports.congress.gov/> accessed 17 June 2025.

[1316] Blackford, 'An Overview of Small Business Contracting' (n 1315), at 2 citing US Congress, Senate Select Committee on Small Business, Small Business Administration, committee print, 83rd Cong., 1st sess., 10 August 1953 (GPO, Washington) iv.

[1317] Around 1942, more than 75 per cent available to provide the goods without investing in new plants. This signified a different treatment of Army and Navy contracts were awarded to only 56 out of 184,230 manufacturing businesses, and all of the 56 businesses were large businesses. Moreover, there was reluctance to contract with small businesses. Governments even built new plants for large businesses to start manufacturing while ignoring that there were small businesses between large businesses and small businesses. See Anglund (n 82) 16.

[1318] Small Business Act of 1953, Pub L No 83–163, 67 Stat 232, codified in 15 USC § 631 et seq.

[1319] 15 USC § 631 (a).

capacity of small businesses.[1320] Accordingly, 15 USC 631 (a) mandates that the federal government shall 'aid, counsel, assist, and protect, insofar as is possible' the interests of small businesses.[1321] Four principal, interrelated objectives underpin this mandate: preserving free competitive enterprise; ensuring a fair proportion of total government procurement contracts are allocated to small businesses; ensuring a fair proportion of total sales of government property are made to such enterprises; and maintaining and strengthening the national economy.[1322] Within this framework, ensuring that a fair proportion of government procurement contracts are awarded to small businesses serves both as a standalone objective and as an instrumental mechanism to encourage and develop their actual and potential capacity.[1323]

Section 633 of the Act establishes the SBA as the primary federal agency responsible for executing these policies.[1324] In 1958, Public Law 85–536 amended the Act to provide explicit statutory authority for the use of set-asides, enabling federal agencies to reserve certain contracts exclusively for small businesses.[1325] The SBA was further entrusted with the responsibility of assisting federal agencies in contracting with small businesses and meeting small business contracting goals, which are numerical targets set by Congress.[1326] This framework was reaffirmed and refined through subsequent legislation, notably the Small Business Jobs Act of 2010, which strengthened the

[1320] ibid, emphasis added.
[1321] 15 USC § 631 (a).
[1322] ibid.
[1323] 15 USC § 631 (a).
[1324] 15 USC § 633.
[1325] Small Business Act of 1958, Pub. L. No. 85–536, § 15, 72 Stat. 384, 389-391, codified in 15 USC § 644.
[1326] The statutory basis for small business contracting goals is set out in 15 USC § 644(g), while § 644(h) imposes subcontracting plan obligations on large prime contractors.

SBA's oversight of set-aside programmes and enhanced enforcement mechanisms against fraud and misrepresentation in those programmes.[1327]

Since the enactment of the Act in 1953, the scope and complexity of small business programmes have expanded significantly.[1328] What began as an economic assistance programme for small businesses has evolved into a diversified regime, incorporating elements of affirmative action to advance not only ordinary small businesses, but also specific socioeconomic small businesses, such as those owned by socially or economically disadvantaged individuals.[1329] While all set-aside programmes aim to promote inclusion in federal procurement, the underlying rationale for these socioeconomic set-asides extends beyond economic assistance for ordinary small businesses.[1330] They are intended to mitigate systemic barriers to market access faced by historically underrepresented or disadvantaged groups.[1331] In this respect, these programmes may be understood as part of a broader policy associated with affirmative action, particularly in their focus on race, gender, veteran status, or geographic disadvantage.[1332] Currently, there are four major government-wide set-aside programmes designed to support socioeconomic small businesses: socially and economically disadvantaged small businesses (SDBs, primarily through the 8(a)

[1327] See Small Business Jobs Act of 2010, Pub L No 111–240, pt IV, §§ 1341–1347, 124 Stat 2504.

[1328] For an overview of current small business set-asides and socioeconomic programmes, see Blackford, 'An Overview of Small Business Contracting' (n 1315).

[1329] See Nagle (n 27) ch 17.

[1330] See Anglund (n 82).

[1331] ibid 11.

[1332] Defining affirmative action is challenging as it comprises components from various sources of legislation and court rulings rather than constituting a single coherent policy. It is considered to encompass policies in different spheres, including employment, education, and government contracting. See Harry Holzer and David Neumark, 'Assessing Affirmative Action' (2000) 38 Journal of Economic Literature 483; James E Jr Jones, 'The Origins of Affirmative Action Essay' (1987) 21 U.C. Davis Law Review 383; William M Leiter and Samuel Leiter, *Affirmative Action in Antidiscrimination Law and Policy: An Overview and Synthesis* (2nd edn, State University of New York Press 2011).

Business Development programme), service-disabled veteran-owned small businesses (SDVOSBs), woman-owned small businesses (WOSBs), and those located in Historically Underutilised Business Zones (HUBZones).[1333]

Although both use reserved contracts as a form of support, small business set-asides and socioeconomic set-asides are underpinned by distinct rationales as discussed earlier. From a definitional perspective, small business eligibility is defined by reference to economic characteristics, usually by the number of employees and annual revenue, as discussed in Chapter 2.[1334] Support for small businesses is therefore aimed at improving their economic capacity. By contrast, eligibility for socioeconomic set-asides incorporates both economic and social attributes, most notably the disadvantaged status of the owners of those small businesses.[1335] Such set-asides do not seek to alter those social attributes, but rather to counterbalance the past discrimination through providing them with better access to federal procurement contracts.

This chapter primarily focuses on the effectiveness of set-aside programmes in achieving their core statutory objective: to encourage and develop the actual and potential capacity of small businesses. While acknowledging the social dimension of set-asides, the analysis remains focused on the impact of set-asides on small

[1333] The 8(a) Programme is a subset of the SDB category: while SDB status is generally self-certified, entry into the 8(a) Programme requires formal qualification and admission by the SBA. Unlike other socioeconomic programmes, 8(a) Programme has a nine-year limitation. See 15 USC § 637(a); 13 CFR pt 124 subpt B. For a discussion of socioeconomic programmes, see CRS, 'Minority Contracting and Affirmative Action for Disadvantaged Small Businesses: Legal Issues' (CRS Report RL33284, 1 April 2010) <https://crsreports.congress.gov> accessed 12 Jan 2024.

[1334] See Chapter 2.

[1335] ibid.

businesses in general, regardless of their socioeconomic attributes, which is consistent with the overall approach of the thesis.

In summary, the statutory purpose of small business assistance outlined in the Act is to encourage and develop their capacity.[1336] Ensuring that small businesses are awarded a fair proportion of government procurement contracts is both an objective and a means for achieving the broader goal of developing small business capacity. Whether these objectives have been achieved in practice remains a contested issue. This chapter examines this question critically and considers how the design and implementation of set-asides interact with other objectives of the federal procurement system. The framework is intricate, encompassing both general assistance to small businesses and targeted support for socioeconomic groups, each subject to agency-specific and government-wide contracting goals.[1337] The operational rules governing these programmes are prescribed in the FAR, which will be discussed in the following section.

7.3 Set-asides for Small Businesses in US Federal Procurement

On the statutory level, the current federal procurement rules are mainly established in the Competition in Contracting Act (CICA) of 1984, which laid the foundation of the FAR.[1338] The FAR, jointly issued by the Department of Defense, the General Services Administration (GSA), and the National Aeronautics and Space Administration (NASA),

[1336] 15 USC § 631 (a).

[1337] See Section 7.3.5.

[1338] Competition in Contracting Act of 1984, Pub L No 98–369, div B, tit VII, 98 Stat 1175, codified at 10 USC ch 320 and 41 USC ch 33 ('CICA'); Ellen Terrell, 'Research Guides: Federal Government Contracting: A Resource Guide: Understanding the Past' <https://guides.loc.gov/federal-government-contracting/understand-past> accessed 20 January 2024.

is codified at Chapter 1 of Title 48 of the Code of Federal Regulations (CFR) and governs procurement activities of all executive agencies.[1339] Pursuant to Section 644 of the Act, Part 19 FAR establishes the framework for federal small business programmes and prescribes the conditions under which agencies are required to set aside contracts for small businesses.[1340]

7.3.1 The principles and objectives of the FAR

As set out in FAR 1.102, the overarching vision for the federal procurement system is to 'deliver on a timely basis the best value product or service to the customer, while maintaining the public's trust and fulfilling public policy objectives'.[1341] FAR 1.102(b) contains four guiding principles that operationalise this vision, the first of which emphasises satisfying customer needs in terms of cost, quality, and timeliness, implicitly prioritising efficiency.[1342] In pursuit of this, it provides that agencies should maximise the use of commercial products and services and contract with businesses that have either a proven track record or a demonstrated superior ability to perform.[1343] It also requires the promotion of competition as a means of securing the best value.[1344] The other three principles concern minimising administrative operating costs, conducting business with integrity, fairness, and openness, and fulfilling public policy objectives,[1345] Based on these principles, federal procurement shall pursue the 'best

[1339] 48 CFR ch 1.
[1340] 15 USC § 644; 48 CFR § pt 19.
[1341] 48 CFR § 1.102 (a).
[1342] 48 CFR § 1.102 (b)(1).
[1343] See 48 CFR § 1.102 (b)
[1344] See 48 CFR § 1.102 (b)
[1345] 48 CFR § FAR 1.102 (b).

value' while at the same time fulfilling public policy objectives, which include, though not exclusively, providing maximum practicable opportunities to small businesses.[1346]

Schooner has identified nine objectives of public procurement systems, including competition, integrity, transparency, efficiency, customer satisfaction, best value, wealth distribution, risk avoidance, and uniformity.[1347] Among all these objectives, he argues that the federal procurement system is governed by three overarching principles: competition, transparency, and integrity.[1348] Notably, efficiency has not been universally accepted as a principal objective or principle of the system. The limitation on contract bundling exemplifies this stance, specifying that 'the reduction of administrative or personnel costs alone' is not sufficient for a contract bundling decision, unless the cost savings are substantial.[1349] Although competition is regarded as a key objective and principle of the federal procurement system, this chapter contends that it is, in practice, a compromised principle.[1350] FAR 19.203 explicitly provides that small business set-asides take precedence over 'acquisitions using open and full competition'.[1351] It may be argued that the reference to 'competition' in the guiding principles (FAR 1.102) pertains to market dynamics, that is, a competitive environment, whereas 'full and open competition', as defined in FAR 6.1, refers more narrowly to procedural openness in source selection.[1352] From this perspective, small

[1346] 48 CFR § 19.201.

[1347] Schooner, 'Desiderata: Objectives for a System of Government Contract Law' (n 24) 104.

[1348] ibid.

[1349] Schooner, 'Desiderata: Objectives for a System of Government Contract Law' (n 24). For instance, Schooner contends that the 'efficiency' of procurement has not universally been accepted as a fundamental goal within the procurement process. The anti-bundling rule exemplifies this stance, specifying that 'the reduction of administrative or personnel costs alone shall not be a justification for bundling of contract requirements unless the cost savings are expected to be substantial.' See 15 USC § 644(e)(2)(C).

[1350] See Section 7.4.2.

[1351] 48 CFR § 19.203.

[1352] 48 CFR § 6.1.

business set-asides represent a departure from the principle of full and open competition, in that they exclude large businesses from bidding for those contracts. However, they may nonetheless foster robust competition within the small business sector, potentially preserving, or even enhancing, the system's ability to deliver best value. This is achieved through an intricate design of the reserved contracts regime, as discussed in the subsequent sections.

7.3.2 Procurement below the simplified acquisition threshold

Part 19 of the FAR governs small business programmes, primarily the use of set-asides.[1353] Under FAR 19.502-2, contracting officers are generally required to set aside contracts valued between the micro-purchase threshold and the simplified acquisition threshold (SAT) exclusively for small businesses, unless the contracting officer reasonably expects that there would not be two or more responsible small businesses bidding for this contract.[1354] If only one such offer is received, the contracting officer is required to proceed with an award to that small business, effectively allowing a sole-source award.[1355] Sole-source set-asides differ from competitive set-asides in that they allow a contract to be awarded without competition. It is important to note that this authority to proceed with a sole-source award under FAR 19.502-2 applies only within the micro-purchase to SAT range. For acquisitions exceeding the SAT, sole-source awards are authorised only under specific

[1353] 48 CFR § pt 19.

[1354] 48 CFR § 19.502-2. 'Responsible small businesses' refer to small businesses that satisfy the criteria under the determination of responsibility in 48 CFR § pt 9, the equivalent term in EU public procurement law is selection criteria, or qualification criteria. More on the qualification, see Chapter 6.

[1355] 48 CFR § 19.502-2.

socioeconomic small business programmes and within defined statutory thresholds.[1356]

According to FAR 2.101, the micro-purchase threshold is USD 10,000, and the SAT is USD 250,000 in most cases.[1357] Agencies are required to use 'simplified acquisition procedures'(SAPs) to the 'maximum extent' for contracts valued not exceeding the SAT, including contracts not exceeding the micro-purchase threshold.[1358] The purpose of the SAP is to reduce administrative costs, which is consistent with guiding principles for federal procurement, but also to improve opportunities for small businesses in general and socioeconomic small businesses to secure a fair portion of procurement contracts.[1359]

Prima facie, the scope of small business set-asides is extensive between micro-purchase and the SAT, but there are mandatory resources which have higher priority over small businesses. Before applying a SAP, the agency shall assess if their procurement needs can be satisfied by the required sources of supply, notably the Federal Prison Industries (FPI), the Committee for Purchase from People Who are Blind or Severely Disabled, the Federal Supply Schedules operated by the GSA, or any existing indefinite delivery/indefinite quantity (IDIQ) contracts.[1360] IDIQ contracts are multiple-award contracts which involve more than two contractors in a single solicitation.[1361] Multiple-award contracts are similar to framework agreements in the

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[1356] For example, see 48 CFR § 19.8051(a)(2) regarding sole-source awards in 8(a) business development programme.
[1357] 48 CFR § 2.101.
[1358] 48 CFR § 13.003 (a); 48 CFR § 2.101. According to 48 CFR § 2.101, the micro-purchase threshold is generally USD 10,000 and the simplified acquisition threshold is generally USD 250,000, although higher thresholds apply in specific circumstances such as contingency operations or overseas procurements.
[1359] 48 CFR § 13.002.
[1360] 48 CFR § 13.003 (a).
[1361] 48 CFR § 2.101.

EU.[1362] As discussed in Chapter 3, in some countries, framework agreements could be a barrier for small businesses.[1363]

Although SAPs have fewer procedural requirements, they still follow reasonable rules and ensure the best value is guaranteed. For instance, the contracting officer needs to display the procurement needs publicly, but the solicitation can be done orally if it is more efficient.[1364] In these procedures, competition must be promoted by the contracting officer, but the sources are from small businesses, including all socioeconomic small businesses.

Agencies are required to use the government-wide commercial purchase card when the value of the procurement does not exceed the micro-purchase threshold.[1365] The purchase card is a method of payment, and it does not limit the contracting officer's discretion to procure from a sole source or a competitive procedure.[1366] FAR 13.203 permits that micro-purchases can be made without a soliciting competitive procedure when the price is reasonable. Thus, the contracts below the micro-purchase are not exclusively reserved for small businesses, and it can be challenging for them to find information about those contracts if they are not publicly solicited.

[1362] For a comparative analysis, see Christopher R Yukins, 'Are IDIQs Inefficient? Sharing Lessons with European Framework Contracting' (2008) 37 Public Contract Law Journal 545.

[1363] See Chapter 3.

[1364] 48 CFR § 13.106-1(c).

[1365] 48 CFR § 13.201 (b).

[1366] According to FAR 32.1108, a purchase card charge authorises a financial institution to make instant payments to the contractors, and the government will reimburse the financial institution. See 48 CFR § 32.1108.

7.3.3 Procurement exceeding the simplified acquisition threshold (the Rule of Two)

For procurement above the SAT (USD 250,000), FAR 19.502-2 requires that contracting officers shall set aside any acquisition for small business when there is a reasonable expectation that 'offers will be obtained from at least two responsible small business concerns' and 'award will be made at a fair market price'.[1367] If such an expectation does not exist, the contracting officer shall consider partial set-asides, which reserve part of a contract for small businesses to compete.[1368] The factors that a contracting officer shall consider include past experiences, market research of an item or a similar item, and the mix of costs, performance and schedules.[1369] This rule is also known as the 'Rule of Two'.[1370]

Apart from soliciting a single award, agencies can award multiple delivery order contracts, termed as multiple-award contracts (MACs).[1371] A MAC can be a contract that is a Multiple Award Schedule issued by the GSA or an indefinite delivery/indefinite quantity contract (IDIQ) that involves more than two sources in the same solicitation.[1372] Such contracts usually operate through a pre-established list of contractors, with limited opportunities for new entrants to join outside designated solicitation periods.[1373] As discussed in Chapter 3 Section 3.3.2, small businesses

[1367] 48 CFR § 19.502-2 (b).
[1368] ibid.
[1369] 48 CFR § 19.502-2 (b).
[1370] Max V Kidalov and Keith F Snider, 'Once More, with Feeling: Federal Small Business Contracting Policy in the Obama Administration' (2013) 1 Public Procurement Law Review 15.
[1371] 48 CFR § 52.216-27.
[1372] 48 CFR § 2.101.
[1373] Executive Office of the President, Office of Management and Budget (OMB), Memorandum for Chief Acquisition Officers, Senior Procurement Executives, 'Increasing Small Business Participation on Multiple Award Contracts' (25 Jan 2024) <https://bidenwhitehouse.archives.gov/wp-content/uploads/2024/01/REV_Increasing-Opportunities-to-Small-Businesses-under-MACs-CATS-Final-Copy-1-25-24.pdf> accessed 16 May 2024.

have encountered difficulties accessing contract opportunities under MACs, and there is an increasing use of MACs over single award procedures.[1374] Moreover, the Rule of Two does not automatically apply to MACs, as FAR 19.504 specifies that 'contracting officers may, at their discretion, set aside orders' placed under MACs for small businesses.[1375]

If the contracting officer decides to set aside for small businesses in a MAC, there are three approaches.[1376] Firstly, it can be totally set aside for small businesses or any socioeconomic groups, and then the bidders and suppliers under the contract will all be small businesses.[1377] The second way is to set aside a portion of a MAC and reserve this portion for competition only among small businesses or any socioeconomic groups.[1378] The rest of the contract is solicited under open and full competition. The third approach, termed 'reserves', allows contracting officers to set aside orders to small businesses or any socioeconomic groups under a fully and openly competed MAC, given that two or more small businesses are on the supplier list in this contract.[1379] Orders under 'reserves' can only be used when a total or partial set-aside is not feasible.[1380]

The rule concerning 'reserves' appears across multiple provisions in the FAR, potentially causing confusion for small businesses and contracting officers. Firstly, 'reserves' cannot be used when total or part set-asides are feasible.[1381] Secondly, one

[1374] See Chapter 3, Section 3.3.2.
[1375] 48 CFR § 19.504.
[1376] ibid.
[1377] 48 CFR § 19.504 (b).
[1378] 48 CFR § 19.504 (b) (2).
[1379] 48 CFR § 19.504 (c).
[1380] 48 CFR § 19.501 (a)(2).
[1381] 48 CFR § 19.503(a).

presumption for using ‘reserves’ is that there are awards to small businesses under a MAC, i.e., at least two small businesses are on the contractor list of the MAC, which means they have succeeded in the first stage of the competition to secure a place on the contractor list.[1382] The intricacies of implementing reserved contracts in multiple-award contracts add additional burdens on contracting officers to reserve contracts for small businesses. Thus, set-asides in MACs are not frequently used by federal agencies in practice.[1383] Although there are three approaches to reserve contracts for small businesses under MACs, making this decision is only at the contracting officer’s discretion.[1384] In 2024, the White House announced a new executive memorandum through the Office of Management and Budget (OMB) for all chief acquisition officers and senior procurement executives.[1385] This memorandum urged federal agencies to increase small business participation in MACs.[1386] The Memorandum especially requires that agencies apply the Rule of Two to all contract orders under multiple-award contracts with limited exceptions.[1387] At the time of writing, new regulations proposed in January 2025 are intended to formalise and expand these requirements by mandating the application of the Rule of Two to orders under MACs, thereby aiming to enhance small business participation.[1388] Currently, these regulations remain pending, and their practical effect is yet to be observed.[1389]

[1382] 48 CFR § 19.504.

[1383] Kidalov and Snider, ‘Once More, with Feeling: Federal Small Business Contracting Policy in the Obama Administration’ (n 1370) 30.

[1384] ibid.

[1385] OMB, ‘Increasing Small Business Participation on Multiple Award Contracts’ (n 1373).

[1386] ibid.

[1387] OMB, ‘Increasing Small Business Participation on Multiple Award Contracts’ (n 1373).

[1388] FAR: Small Business Participation on Certain Multiple-Award Contracts, Proposed Rule, 90 Fed Reg 1597 (15 January 2025).

[1389] ibid.

7.3.4 Limitations on subcontracting and the nonmanufacturer rule

When a reserved contract is awarded, FAR 19.505 requires that a small business shall not pay subcontractors that are not 'similarly situated entities' more than 50 per cent of the payment from the agency for the contract execution.[1390] Some exceptions exist, such as in construction procurement, where the percentage is 85 per cent.[1391] The 'similarly situated entity' refers to a subcontractor in the same category as the contractor. For instance, if the prime contractor is a small business owned and controlled by women, the 'similarly situated entity' is such a business.[1392] This rule ensures that the small contractor will perform the majority of the set-aside contract itself. Even if the contractor intends to subcontract the contract, it cannot subcontract most of it to a non-similarly situated entity. Without this rule, a small contractor may subcontract most of the contract to a large business. As a result, this may incur additional costs for the federal agency, and the actual performer of the contract may not be selected through a competitive procedure.[1393] A scandal occurred with the Food and Drug Administration in 2008 when an Alaska Native-owned business (Alaska Newspaper Inc.) was awarded a public relations campaign contract valued at USD 300,000 through a set-aside. After the award was made, Alaska Newspaper Inc. subcontracted most of the contract to Qorvis Communications, the company that the agency had initially intended to contract with, as reported by The Washington Post.[1394]

[1390] 48 CFR § 19.505 (b) (1).

[1391] 48 CFR § 19.505 (b) (iii).

[1392] 15 USC § 657s (e)(2).

[1393] Kate M Manuel, 'The Inapplicability of Limitations on Subcontracting to "Preference Contracts" for Small Businesses: Washington-Harris Group' (CRS Report R40998, 6 October 2010) <https://crsreports.congress.gov> accessed 14 Jan 2024.

[1394] Robert O'Harrow Jr, 'FDA Takes End Run to Award Contract to PR Firm' (2 October 2008) <http://www.washingtonpost.com/wp-dyn/content/article/2008/10/01/AR2008100103061.html> accessed 15 January 2024.

In this case, the set-aside programme was used as a way to avoid competition and manipulate the supplier. As Schooner pointed out, this is against the principles of federal procurement; it is neither transparent nor competitive.[1395] Although the selection of subcontractors is not regulated by procurement law in general, in reserved contracts, subcontracting needs to be regulated to some extent. As discussed earlier, set-aside programmes are one of the justified exceptions to open and full competition in federal procurement. Limitations on subcontracting ensure that set-asides are not exploited by large businesses to bypass competition. Additionally, they ensure that small businesses actively perform on contracts to gather experience in federal procurement, as past performance is usually included as a factor in the determination of responsibility or tender evaluation.[1396]

The limitation on subcontracting rule does not extend to contracts that are not reserved for small businesses, even where a small business receives a preference under the evaluation criteria (award criteria).[1397] This principle was affirmed in a GAO decision of a bid protest regarding limitations on subcontracting.[1398] In this protest, the Department of the Army conducted a negotiated procedure in which offerors were evaluated based on several factors, with the most important weighted factors being: understanding the solicitation requirement and the SDVOSB status.[1399] Price was explicitly designated as the least important factor.[1400] The solicitation thus granted an evaluation preference to SDVOSBs, but did not constitute a set-aside. After the award, the SDVOSB contractor proposed to subcontract more than 50 per cent of the

[1395] ibid.
[1396] See Chapter 5, Section 5.2.2.2.
[1397] See Manuel (n 1393) 1.
[1398] US GAO, *Washington-Harris Group*, B-401794; B-401794.2 (16 November 2009).
[1399] ibid.
[1400] GAO, B-401794; B-401794.2 (n 1398).

contract's value to a non-SDVOSB entity. The protestor contended that this arrangement violated the limitation on subcontracting. The GAO denied this protest, holding that the limitation on subcontracting is applicable only where the contract has been set aside for small businesses or SDVOSBs. As the solicitation was conducted on a non-reserved basis, albeit with an evaluation preference for SDVOSBs, the limitation did not apply.[1401]

Many small businesses are resellers or distributors, rather than direct manufacturers of goods.[1402] To prevent large manufacturers from simply using a small reseller as a channel to access set-aside contracts, the nonmanufacturer rule (NMR) requires that a small business bidding on a set-aside supply contract must either manufacture the product itself or offer a product manufactured by another small business.[1403] In other words, a small business cannot act as a middleman to supply products that are produced by large businesses through set-asides, unless the SBA grants a waiver for this requirement, which it sometimes does if no small manufacturer exists for a particular product.[1404] The NMR applies to set-asides for general small businesses and socioeconomic set-asides valued at above USD 250,000, implying that for contracts below the threshold (SAT), small businesses can provide products produced by large businesses. The rationale for the NMR is to guarantee that the primary beneficiary of set-asides is limited to small businesses, rather than large businesses. Moreover, it requires that the products supplied by small businesses be manufactured in the US, which prohibits products manufactured in other countries from being

[1401] ibid. The GAO call this type of procedure a 'preference contract'.
[1402] Erik Hurst, Benjamin Wild Pugsley, 'What Do Small Businesses Do' (Brookings Papers on Economic Activity, 2011, No.2) <https://www.brookings.edu/articles/what-do-small-businesses-do/> accessed 16 June 2025, 85.
[1403] 48 CFR § 19.505 (c)(1).
[1404] 13 CFR § 121.406(b).

supplied through small business set-asides over the SAT.[1405] This reflects that the protection for small businesses in federal procurement also extends to domestically manufactured products, as discussed in Chapter 2 on the US definition of small businesses.

Together, the limitations on subcontracting and the NMR protect the set-aside system against loopholes. They underscore that reserved contracts are intended to build the capacity of small businesses themselves, either by performing services or strengthening their capacity to supply products.

7.3.5 Federal small business contracting goals

In 1988, Congress enacted the first government-wide goals in prime contracting with small businesses, known as small business contracting goals, and these goals have increased and expanded to include socioeconomic small businesses since then.[1406]

Each fiscal year, not less than 23 per cent of the total value of prime contract awards is targeted for small businesses overall.[1407] Within this figure, sub-targets are set for specific categories: at least 5 per cent for small disadvantaged businesses, 5 per cent for women-owned small businesses, 5 per cent for service-disabled veteran-owned small businesses, and 3 per cent for businesses located in historically underutilised business zones (HUBZones).[1408]

Apart from government-wide contracting goals, each federal agency is required to establish individual agency contracting goals with small businesses and subgroups of

[1405] 13 CFR § 121.406(a).
[1406] 15 USC § 644(g).
[1407] 15 USC § 644 (g)(1)(A).
[1408] 15 USC § 644 (g)(1).

small businesses, which may differ from the government-wide goals.[1409] As for the SBA, apart from meeting its own goals, it also tracks and reports on other agencies' performance toward meeting these goals. Although the SBA is responsible for ensuring that each agency sets goals annually and their achievements are 'relative' to the goals, there is no punitive outcome or result for agencies that cannot meet the goals.[1410] When an agency fails to meet its small business contracting goal, the only result is a corrective action report to be delivered to the SBA.[1411] The government-wide goals are legally binding, as they are established by statute.[1412] By contrast, agency-specific contracting goals, typically set out in annual reports, are aspirational targets rather than legal obligations or enforceable administrative mandates.

Although the government-wide goals are legally established, federal government's performance in achieving them has been inconsistent. The SBA publishes a 'Small Business Procurement Scorecard' (SBA Scorecard) annually to monitor and assess the performance of agencies in meeting these goals.[1413] Since 2013, progress has been made towards meeting these goals, but the goals for WOSB and HUBZone small businesses have rarely been met, except in 2015 and 2019 for WOSBs.[1414] The SDB goal has been met since 2006, and the SDVOSB goal has been met since 2012.[1415] Despite the satisfaction with exceeding the goals, concerns have arisen about the accuracy of calculations and proper attribution of credits to small business

[1409] 15 USC § 644 (g)(2).
[1410] R. Corinne Blackford, 'Federal Small Business Contracting Goals' (CRS IN12018, updated 22 July 2025) <https://crsreports.congress.gov> accessed 08 August 2025.
[1411] ibid.
[1412] 15 USC § 644 (g)(1)(A).
[1413] SBA, 'Small business procurement scorecard', <https://www.sba.gov/federal-contracting/contracting-data/small-business-procurement-scorecard> accessed 16 July 2025.
[1414] ibid.
[1415] SBA, 'Small business procurement scorecard' (n 1413).

programmes by agencies.[1416] In 2014, the SBA's Inspector General reported that approximately USD 400 million in contracts were awarded to ineligible small businesses, which were nonetheless included in agencies' calculations to meet small business goals.[1417] However, these contracts were included by agencies in their calculations towards meeting small business goals.[1418] Additionally, it is controversial to include contracts awarded to former programme participants towards contracting goals.[1419] These issues suggest a potential overestimation in calculations, which may inaccurately portray federal agencies as effectively achieving their contracting goals with small businesses.[1420] SBA's goaling guideline allows a single contract to be credited toward every socioeconomic category for which the contractor qualifies. For example, a contract awarded to a small business that is both SDVOSB and WOSB is be counted toward the small business, SDVOSB, and WOSB goals.[1421] Yet this system also creates a statistical complication: because the same award may appear in multiple categories, the percentages cannot be meaningfully aggregated. This highlights a persistent tension in reporting small business participation, while the rules

[1416] SBA Office of Inspector General (OIG), 'Agencies are Overstating Small Disadvantaged Business and HUBZone Goaling Credit by Including Contracts Performed by Ineligible Firms' (Evaluation Report 14-18, 14 September 2014) <https://www.sba.gov/document/report-14-18-audit-report-14-18-evaluation-select-8a-business-development-hubzone-contract-awards> accessed 15 January 2024.

[1417] ibid 7.

[1418] SBA OIG (n 1416) 7.

[1419] ibid, 11; also see GAO, 'Small Business Administration: Leadership Attention Needed to Overcome Management Challenges' (Report to Congressional Requesters, GAO-15-347) <https://www.gao.gov/assets/680/672929.pdf> accessed 15 January 2024.

[1420] SBA OIG (n 1416) 9; also see Henry B. R. Beale, 'Evaluation of the Small Business Procurement Goals Established in Section 15(g) of the Small Business Act' (SBA Office of Advocacy, report under contract SBA HQ-13-M-0102, June 2014) <https://advocacy.sba.gov/wp-content/uploads/2019/05/rs423tot.pdf> accessed 15 January 2024, 22.

[1421] For example, see SBA, 'FY2025 Goaling Guidelines' (10 February 2025) <https://www.sba.gov/document/report-sba-goaling-guidelines> accessed 10 June 2025, 8.

prevent undercounting in individual categories, they also risk misinterpretation of the overall totals.

According to the SBA's 2024 Small Business Scorecard, the federal government set a new record by directing 28.76 per cent (approximately USD 183 billion) of all prime contracting dollars to small businesses, surpassing the previous high of 28.35 per cent (USD 178.6 billion) in 2023.[1422] While these figures suggest steady progress, they also raise the question of what qualifies as 'a fair proportion', articulated in the Small Business Act.[1423] 15 USC § 644(g)(2)(D) stipulates that federal agencies should 'make a consistent effort to annually expand' participation by small businesses in each industry.[1424] Consistent with this objective, federal agencies are encouraged to prioritise small business set-aside programmes over open and full competition, a principle underscored by case law.[1425] In Management & Training Corporation v. United States, the US Court of Federal Claims upheld the authority of agencies to reserve contracts for small businesses, even after meeting the small business contracting goals.[1426]

This legal framework theoretically allows agencies to reserve as many contracts as possible for small businesses and socioeconomic small businesses. In practice, however, agencies appear to treat the statutory goals as ceilings rather than baselines: the total value of the total value of contracts awarded to small businesses has consistently been approximately the same as the established contracting goals,

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[1422] See SBA, 'Scorecard details' <https://www.sba.gov/federal-contracting/contracting-data/small-business-procurement-scorecard/scorecard-details> accessed 16 June 2025.
[1423] 15 USC § 644(a).
[1424] 15 USC § 644(g)(2)(D).
[1425] Set-asides for small businesses have priority over full and open competition procedure. See 48 CFR § 19.203 (e).
[1426] *Management & Training Corp v United States* (2014) 115 Fed Cl 26, 36.

indicating that agencies are not substantially incentivised to contract with small businesses beyond the numerical targets.

Similarly, certain socioeconomic contracting goals have seldom been achieved, reflecting the absence of any punitive consequences when agencies fall short of the goals. Hemmatian et al. identified three critical organisational factors influencing decisions on set-asides within federal agencies: administrative discretion, workplace discrimination, and legislative oversight.[1427] Of these factors, legislative oversight demonstrates a positive correlation with the contract values of socioeconomic set-asides, whereas administrative discretion and workplace discrimination show negative correlations.[1428] This finding is corroborated by Resh and Marvel, whose study underscores the positive impact of an internal SBA oversight office on the contract value of small business set-asides.[1429] Thus, effective oversight plays a pivotal role in ensuring agencies achieve their small business contracting goals.[1430] Despite Congress assigning oversight responsibilities to the SBA for small business contracting within federal agencies, there is no statutory framework empowering the SBA to enforce action against agencies failing to meet small business contracting goals.[1431]

[1427] Iman Hemmatian and others, 'Exploring the Effects of Discretion, Discrimination, and Oversight on the Inclusiveness of Small Business Contracting' in Bruno S. Sergi, Cole C. Scanlon, and Luke R. I. Heine (eds), *Entrepreneurship for Social Change* (Emerald Publishing 2021) 203.

[1428] ibid.

[1429] William Resh and John Marvel, 'Loopholes to Load-Shed: Contract Management Capacity, Representative Bureaucracy, and Goal Displacement in Federal Procurement Decisions' (2012) 15 International Public Management Journal 525.

[1430] See Chapter 8, Section 8.5.

[1431] Blackford, 'Federal Small Business Contracting Goals' (n 1410).

7.4 An Impact Analysis of Small Business Set-asides

Previous sections have discussed the regulatory framework in the FAR governing reserved contracts for small businesses in federal procurement, as well as the performance of agencies in meeting small business contracting goals. This section shifts focus to the impact of reserved contracts on small businesses and federal procurement, aiming to evaluate whether reserved contracts have achieved the statutory objectives. These objectives include ensuring small businesses are awarded a fair share of federal procurement contracts and encouraging and developing their actual and potential capacity.[1432] To answer the research question of the thesis, this section analyses the balance between small business set-asides and other objectives of the federal procurement system, especially value for money, competition, and efficiency.[1433] The balance between small business programmes and other objectives reflects the trade-offs incurred by such programmes on competition and the cost of federal agencies.

7.4.1 The impact of set-asides on small businesses

This section mainly assesses if reserving contracts in federal procurement for small businesses has effectively achieved the objective of encouraging and developing their capacity. This section addresses this inquiry from three perspectives: whether federal agencies have implemented set-asides in accordance with the regulatory framework; an interpretation of the mixed signals in data on small business contracting; and the

[1432] See Section 7.2.

[1433] See Section 7.3.1.

empirical evidence on the long-term impact of reserved contracts on small business development.

7.4.1.1 The implementation of set-aside programmes in federal procurement

As discussed in Section 7.2, the statutory objectives underpinning small business programmes in federal procurement are to ensure that such businesses receive a *fair proportion* of federal procurement contracts, and more broadly, to encourage and develop their actual and potential capacity.[1434] The abstract notion of a 'fair proportion' is operationalised through the statutory government-wide contracting goal, fixed at 23 per cent of the total value of prime contract awards since it was established in 1997.[1435] According to the SBA Scorecard, this statutory goal has been met or exceeded consistently since 2013.[1436]

While the SBA Scorecard records compliance with small business contracting goals at both the governmental and agency levels, it does not differentiate between awards secured through set-asides and those obtained through open competition with large businesses.[1437] This distinction is not merely technical; it is central to assessing whether the capacity-development objective of small business policy is being realised. Since 2023, the SBA Scorecard has incorporated detailed data on the value of set-asides, enabling a more precise analysis of the extent to which small business contract awards are attributable to reserved contracts as opposed to open competition.[1438] If

[1434] 15 USC § 631 (a).
[1435] See Small Business Reauthorization Act 1997, Pub L No 105–135, § 502, 111 Stat 2592, codified at 15 USC § 644(g)(1).
[1436] See Section 7.3.5.
[1437] The SBA Scorecard incorporated this detail since 2023. See SBA, 'Small business procurement scorecard' (n 1413).
[1438] ibid.

the majority of contracts awarded to small businesses are secured exclusively through set-asides, two inferences may be drawn: first, that small businesses may lack the incentive to bid for non-reserved contracts; and second, that they may face structural barriers that hinder their ability to compete successfully against larger businesses. The data presented in Figure 7.1 underscored this concern. Between 2010 and 2024, the proportion of total value of contracts awarded to small businesses through set-asides has increased from approximately 52 per cent in 2010 to almost 64 per cent in 2024, with both the absolute value of set-asides and the overall value of contracts awarded to small businesses increasing over the period.[1439] While the growth may indicate that set-aside programmes are effective in directing a certain share of federal procurement opportunities towards small businesses, it also suggests a persistent reliance on preferential mechanisms. Such reliance raises important questions as to whether these programmes are cultivating the competitive capacity of small businesses in the broader market, or whether they are entrenching a parallel market in which small businesses remain dependent on preferential measures rather than competing in open markets.

[1439] See HigherGov, 'Small Businesses Awarded Record $159 Billion from Federal Government in 2022' (Research Report, 13 February 2023) <https://www.highergov.com/reports/small-business-trends-2022/> accessed 17 January 2024.

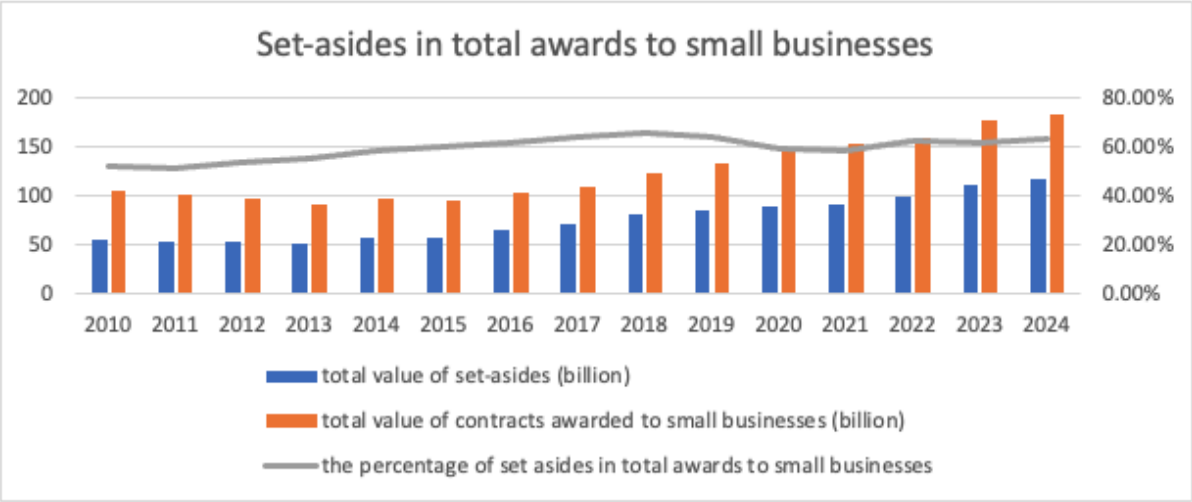

Figure 7.1 Set-asides in total awards to small businesses[1440]

Moreover, the intricacy of small business programmes and the overlap of eligibility criteria can cause tension among different small business programmes. The lack of guidance for agencies regarding priorities among such programmes exacerbates this issue.[1441] FAR 19.203 regulates the relationship among small business programmes, but it only specifies that socioeconomic set-asides shall be considered first before considering general small business set-asides in acquisitions above the simplified acquisition threshold, and there is no order of precedence among socioeconomic set-aside programmes.[1442] It is reasonable that there is no explicitly stated priority among different socioeconomic programmes, as prioritising one group may be at the expense

[1440] The data from 2010 to 2022 is from HigherGov report in 2023, which extracted data from the Federal Procurement Data System, System for Award Management, etc. Its methodology is different from the SBA Small Business Procurement Scorecard (the SBA Scorecard), which may exaggerate the value of total awards to small businesses due to double credit for certain contract awards. More importantly, the SBA Scorecard did not publish detailed data on the value of set-asides until 2023. Thus, the data in this figure from 2023 to 2024 is extracted from the SBA Scorecard. Despite the difference in their methodologies, they show a similar trend. See HighGov (n 1439); SBA, 'Small business procurement scorecard' (n 1413).

[1441] Resh and Marvel (n 1429).

[1442] 48 CFR § 19.203.

of another.[1443] Based on the small business contracting scorecard published by the SBA, Figure 7.3 shows that from 2007 to 2022, socioeconomic groups have been awarded more contracts than small businesses without any socioeconomic attributes (named as 'General SB', shown by the dark blue line in Figure 7.2). In fact, the share of contract value awarded to small businesses without any socioeconomic attributes has been decreasing, and this trend is likely to remain as socioeconomic set-asides have precedence over set-asides for small businesses in general.

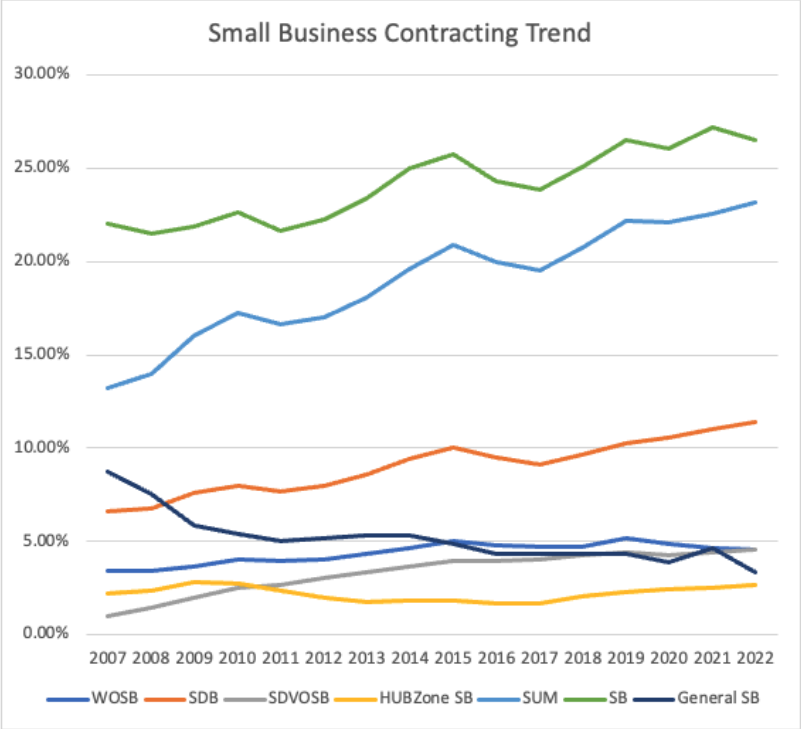

Figure 7.2 Small Business Contracting Trend[1444]

In practice, a contracting officer may employ a 'cascade' or 'tiered' approach to assess bids from different categories of small businesses.[1445] The evaluation proceeds in

[1443] Similarly, Resh and Marvel have argued that goals pursued by public organisations are often in tension and pursuing one might be at the expense of another. See Resh and Marvel (n 1429) 525.
[1444] SBA, 'Small business procurement scorecard' (n 1413)
[1445] Acquisition Advisory Panel, 'Report of the Acquisition Advisory Panel to the Office of Federal Procurement Policy and the United States Congress' (January 2007)

cascading tiers until a successful offeror is identified.[1446] For instance, if the initial tier is restricted to WOSBs and the subsequent tier to SDVOSBs, the contracting officer ceases evaluation upon identifying a winner in the first tier, thereby excluding tenders in the second tier from the evaluation process. The contracting officer retains discretion over the number of tiers to be assessed.[1447] The cascade evaluation method may have introduced more inefficiencies than anticipated.[1448] The tension created by the cascading evaluation method fails to motivate small businesses towards greater competitiveness, but instead encourages them to acquire additional socioeconomic attributes that guarantee benefits from set-aside programmes in the short term. As a result, FAR 15.101-3 explicitly prohibited the use of a cascading or tiered evaluation system, unless there is statutory authority to do so.[1449] However, this limitation is only for MACs in negotiation procedures, and agencies may still be able to use cascading evaluation in set-asides, as long as they follow the limited rules where the priority of a specific socioeconomic groups is explicitly made, for example, FAR 19.800 requires that 8(a) set-asides shall be considered before small business set-asides in acquisitions above the simplified acquisition threshold.[1450]

Within small businesses, set-asides tend to benefit those who are more successful in winning contracts, raising concerns that a limited number of 'successful' small businesses may dominate within target groups.[1451] For instance, in the HUBZone

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<https://www.acquisition.gov/sites/default/files/page_file_uploads/ACQUISITION-ADVISORY-PANEL-2007-Report_final.pdf> accessed 12 January 2024, 22.

[1446] ibid

[1447] Acquisition Advisory Panel (n 1445) 22.

[1448] ibid.

[1449] 48 CFR § 15.101-3.

[1450] 48 CFR § 19.800

[1451] Steven L Schooner and Christopher R Yukins, 'Public Procurement: Focus on People, Value for Money and Systemic Integrity, Not Protectionism' (The George Washington University Law School

programme, 94 per cent of the contract value was awarded to 12 out of 357 eligible businesses that received federal contracts in that period.[1452] On one hand, these small businesses could be successful in their capacity to compete and deliver a contract, which is the objective of these programmes.[1453] A question then emerges as to whether these successful small businesses should qualify for set-asides after participating in a programme for a specified period. Among the federal socioeconomic programmes, the 8(a) Business Development Programme is the only one imposing a nine-year limit on participation; other programmes allow small businesses to remain eligible as long as they continue to meet the criteria.[1454] However, the effectiveness of the programme has been questioned since participants rarely graduate and become self-sufficient.[1455] Empirical data indicate that more than 63 per cent of 8(a) programme graduates secured fewer federal contracts within five years of graduation, and only 23 per cent of such businesses managed to secure more federal contracts.[1456] Although set-aside programmes are designed to support small businesses to enhance their capacity over the long term, there is no reward for leaving a programme and a lack of incentives for them to compete with large businesses in

Public Law and Legal Theory Working Paper No 460, Legal Studies Research Paper No 460, 2009) 87, 89.

[1452] SBA, 'Performance Audit Report 14-03 : Opportunities Exist to Further Improve Quality and Timeliness of HUBZone Certifications' (19 November 2013) <https://www.sba.gov/document/report-14-03-audit-report-14-03-opportunities-exist-further-improve-quality-timeliness-hubzone-certifications> accessed 17 August 2025, 1.

[1453] See Section 7.2.

[1454] 13 CFR § 124.2; 13 CFR § 124.102.

[1455] Timothy Bates, 'Utilizing Affirmative Action in Public Sector Procurement as a Local Economic Development Strategy' (2009) 23 Economic Development Quarterly 180; Robert Jay Dilger and R. Corinne Blackford, 'SBA's "8(a) Program": Overview, History, and Current Issues' (CRS Report R44844, updated July 29, 2022) < https://crsreports.congress.gov> accessed 17 January 2024, 37.

[1456] HigherGov, '8(a) Graduation: A Survival Guide' (July 2023) <https://www.highergov.com/news/8-a-graduation-a-survival-guide-2098934/> accessed 17 January 2024.

non-set-aside contracts.[1457] In the long term, it might create a bigger gap between large businesses and small businesses.

On the other hand, some small businesses can be 'successful' to obtain more than one socioeconomic status to be eligible for multiple socioeconomic set-aside programmes. Yukins and Schooner have commented that these procurement preferences operate as 'blunt, rather than surgical' instruments, highlighting their inherent imprecision, which tends to benefit a narrow subset of 'sophisticated participants' within the designated groups.[1458] Such sophisticated participants may exploit their eligibility in multiple set-aside programmes, for instance, a company qualifying as both a WOSB and SDVOSB. In this circumstance, a federal agency can receive credit against two categories in the small business contracting scorecard, a distinct advantage over contracts awarded to small businesses lacking socioeconomic attributes. This dynamic creates tension among various categories of small businesses competing for set-aside contracts, yet it does not necessarily foster improved competitiveness within the small business sector. Instead, it incentivises small businesses to accumulate additional socioeconomic attributes rather than to develop economic capacity. Ultimately, as discussed in Chapter 2, the development of economic capacity may lead small businesses to exceed the thresholds defining small-business size, thereby rendering them ineligible for future set-aside programmes.[1459]

[1457] See David J. Berteau and Amanda Swanson, 'The Impact of 8(a) Small Business Graduation' (Naval Postgraduate School Acquisition Research Program, Proceedings of the Fifteenth Annual Acquisition Research Symposium, Thursday Sessions Volume II, SYM-AM-18-087, 2018) 226.

[1458] Schooner and Yukins (n 1451) 89.

[1459] See Chapter 2.

7.4.1.2 Mixed signals in small business contracting data

Although the value of contracts awarded to small businesses has been consistently increasing, the number of small businesses being awarded contracts in federal procurement has decreased drastically from 121,270 in 2010 to 58,681 in 2022.[1460] This trend raised concern from small business stakeholders.[1461] Furthermore, the number of new small businesses entering the federal procurement market has declined sharply by 79 per cent between 2005 and 2019.[1462] As a result, the average value awarded to each small business contractor has increased significantly from USD 0.9 million to USD 2.7 million in 2022.[1463] In FY 2024, the value of contracts awarded to the top 10 small-business contractors amounts to USD 12.85 billion, which is around 7.2 per cent of the total value of contracts awarded to 78,677 small businesses (USD 176.11 billion).[1464]

This significant decrease in the number of small businesses first entering the federal procurement market indicates that there are still entry barriers hindering them from accessing the market, or there is a lack of interest from small businesses. The combination of a decrease in the number of small-business contractors and an increase in the average value awarded to a small-business contractor could also be attributed to multiple factors,[1465] one of which could be due to an increasing use of

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[1460] HigherGov (n 1439).

[1461] Bipartisan Policy Center (n 339) 3.

[1462] HigherGov (n 1439).

[1463] ibid.

[1464] Archisha Mehan, 'Federal Contract Awards Hit $773.68B in FY24, Small Businesses See $4B Increase' (GovSpend Blog 24 February 2025) <https://govspend.com/blog/federal-contract-awards-hit-773-68b-in-fy24-small-businesses-see-4b-increase/> accessed 10 June 2025. The data published by GovSpend is sourced from Federal Procurement Data System.

[1465] The Director of Policy, Planning, and Liaison within SBA's Office of Government Contracting and Business Development, Sam Le, referred to this mixed trends 'a bit of a puzzle', and expressed the concern over small businesses' willingness to participate in federal procurement. See Jory Heckman, 'SBA seek to grow shrinking pool of small businesses getting federal contracts', (Federal News Network,

MACs, government-wide acquisition contracts (GWACs), and category management by federal agencies. In 2019, OMB reported that category management eliminated 5 per cent of duplicative contracts that were previously awarded to small businesses.[1466]

The increasing use of those contracts is supported by policies to increase efficiency and reduce administrative costs in federal procurement, by shifting towards fewer, larger, and longer-term contracts.[1467] To implement this initiative, the OMB and the Category Management Leadership Council developed a tiered maturity model to categorise agencies' purchase activity using Spending Under Management (SUM) principle.[1468] Agencies are required to use the highest tier contract 'whenever possible'.[1469] Tier 0 purchase means the agency can procure in a decentralised manner.[1470] Tier 1 purchase means the agency conducts procurement following contract management practices at an agency-wide level, sharing information across the agency, conducting data analysis, etc.[1471] Tier 2 contracts refer to those procured across multiple agencies, termed a multiple-agency solution.[1472] Tier 2 does not necessarily have to be government-wide, but Tier 3 is.[1473] The highest level is Tier 3 contracts, where federal agencies use Best-In-Class (BIC) solutions, including non-Tier 2 GSA schedules.[1474]

May 8, 2023) <https://federalnewsnetwork.com/contracting/2023/05/agencies-spending-record-amounts-on-small-business-contracts-amid-shrinking-pool-of-firms/> accessed 17 August 2025.

[1466] GAO, GAO-21-40 (n 414) 49.

[1467] Bipartisan Policy Center (n 339) 13.

[1468] Memorandum M-19-13 (n 412).

[1469] ibid.

[1470] Memorandum M-19-13 (n 412) 4.

[1471] ibid.

[1472] Memorandum M-19-13 (n 412) 5.

[1473] ibid

[1474] Memorandum M-19-13 (n 412) 5.

To balance different aims, the OMB requires that if a contract is awarded to a small business to achieve statutory goals, this contract can be considered Tier 1 spending, provided it is awarded subject to an organised agency-wide strategy.[1475] In Tier 2 and Tier 3 spending, federal agencies rarely contract with small businesses, except when certain BIC Contracting Vehicles are used, and small businesses are on the contractor lists.[1476] Small businesses have consistently expressed concerns that they are not able to get access to BIC contracts due to the large size of those contracts and more stringent requirements.[1477] Thus, the mixed signals derived from small business contracting data can be interpreted to indicate that entry barriers within federal procurement are not diminished. Rather, the expansion of category management has reinforced these barriers, as procurements are increasingly consolidated into larger, multi-agency contracts, and agencies are rewarded for directing spend toward contractors capable of performing at scale across multiple agencies.

7.4.1.3 The impact of reserved contracts on small businesses

From the perspective of small businesses, reserved contracts do not reduce contract sizes or participation costs, nor do they ease the qualification requirements. However, reserved contracts facilitate small business participation by allowing them to compete exclusively against businesses with similar levels of capacity and development. This reduces the pressure of competing with large businesses, thereby motivating more small businesses to participate in government procurement.

[1475] ibid.
[1476] GAO, GAO-21-40 (n 414) 49.
[1477] ibid 46.

Regarding the impact of reserving contracts on small businesses, empirical research incorporating data at the business level has found that winning public procurement contracts does facilitate the growth of businesses, and this growth effect is more significant for businesses that are smaller and younger.[1478] However, the businesses sampled in this research secured contracts through competitive auctions designed to promote open competition.[1479] Reserved contracts, in contrast, may foster a reliance among small businesses, and this reliance is shown to be detrimental rather than beneficial for their development.[1480] Brown and Girth have found that small businesses with a diversified portfolio of contracts across multiple federal agencies are more likely to exceed the small business size standard, based on a ten-year assessment period.[1481] However, some businesses were recertified as small enterprises after exceeding the size standards, indicating that small businesses may have attempted to maintain their small-business status in order to continue benefiting from reserved contracts.[1482]

Bates and Williams have observed a similar trend that small and young firms relying heavily on public procurement are more likely to fail compared with businesses with more diversified revenue streams.[1483] They found that businesses with less than 25

[1478] See Ferraz, Finan, and Szerman (n 59). In this research, only close auctions are included in the empirical analysis. A close auction is defined as an auction in which both the winner and loser place a bid within the last 30 seconds of the auction, and the winning margin is less than 0.5 per cent. Bids are compared solely based on price.

[1479] ibid.

[1480] Timothy Bates and Darrell Williams, 'Do Preferential Procurement Programs Benefit Minority Business?' (1996) 86(2) The American Economic Review 294, 297.

[1481]Trevor L Brown and Amanda M Girth, 'Examining the Effects of Set Aside Policies on Competition and Growth for Small and Mid-Sized Suppliers' (Naval Postgraduate School Acquisition Research Program, Proceedings of the Fifteenth Annual Acquisition Research Symposium, Thursday Sessions Volume II, SYM-AM-18-089, 2018) <https://calhoun.nps.edu/server/api/core/bitstreams/2e0b1809-b4fa-4cf1-a4fe-a52d85fe2a53/content> accessed 21 January 2024, 196.

[1482] ibid.

[1483] ibid 297.

per cent of their total revenue from government procurement last longer than those with a heavy proportion of income from government procurement; those businesses have shorter life spans.[1484] Nevertheless, Bates and Williams argue that these short-lived small businesses could be front companies established by large businesses to be able to bid for reserved contracts, only to dissolve once the contract concludes.[1485] This situation introduces risks of manipulation and inefficiency in government contracting, topics to be explored in the subsequent section. Small business owners have also expressed this concern in a recent hearing hosted by the House Committee on Small Business on small business programmes, stating that large businesses have been seeking benefits from small business programmes through gaps in rules or set up front small businesses. Legally, some large businesses gain access to the reserved contracts through partnerships with small businesses through the Mentor-Protégé programme[1486]; illegally, some large businesses set up front small businesses and participate in set-asides.[1487]

In summary, while reserving contracts supports small businesses competing for government procurement contracts by excluding competition from large businesses, it inevitably fosters small businesses' reliance on set-aside programmes, which is unsustainable for long-term business competitiveness. Small businesses relying on procurement contracts face negative repercussions when government risk is

[1484] Brown and Girth (n 1481) 295.

[1485] Bates and William (n 1480) 297.

[1486] Large businesses can be eligible for small business set asides as a mentor to a small business in a joint venture under a Mentor-Protégé Programme. 13 CFR pt 125, subpart A. For an overview of Mentor-Protégé Programmes, see Robert Jay Dilger and R. Corinne Blackford, 'Small Business Mentor-Protégé Programs' (CRS Report R41722, updated 10 June 2022) <https://crsreports.congress.gov/> accessed 14 January 2024.

[1487] Keith F Snider, Max V Kidalov and Rene G Rendon, 'Diversity Governance by Convenience? Federal Contracting for Minority-Owned' (2013) 37 Public Administration Quarterly 393.

involved.[1488] Reserved contracts establish a comfort zone for small businesses to circumvent competition with large businesses. Although business opportunities are provided for small businesses in the short term, reserved contracts do not motivate small businesses to compete with large businesses for non-reserved contracts. Consequently, there is not sufficient evidence to conclude that reserved contracts effectively achieved the objectives outlined in the Act to encourage and develop the potential capacity of small businesses over time.

7.4.2 The balance between small business set-asides and competition

Competition is regarded as one of the fundamental principles in federal procurement;[1489] however, various interpretations of this concept exist.[1490] FAR 6.101(a) explicitly requires federal agencies to pursue full and open competition in contract awards with certain limited exceptions.[1491] The term 'competition' as used in FAR 6.101(a) refers to the principle of open and full competition.[1492] In contrast, FAR 1.102(b)(1)(iii) states that the federal acquisition system must promote competition to ensure the customer is satisfied with cost, quality, and timeliness of the product or service delivered.[1493] Here, 'competition' pertains to its outcomes rather than a principle of open and full competition.[1494] The reason is that if it refers to a principle of

[1488] Rhett Buttle, 'Looming Federal Government Shutdown Threatens Small Business Growth And Productivity' (*Forbes,* 28 September 2023) <https://www.forbes.com/sites/rhettbuttle/2023/09/28/looming-Federal-government-shutdown-threatens-small-business-growth-and-productivity/> accessed 7 January 2024.

[1489] See Section 7.2.

[1490] For a discussion of different meanings of 'competition' in the context of public procurement in the EU, see Harlem Losnedahl (n 109).

[1491] 48 CFR § 6.101(a).

[1492] ibid.

[1493] 48 CFR § 1.102(b)(1)(iii).

[1494] ibid.

open and full competition, such a process could result in more tenders being evaluated, leading to increased cost and time for contracting officers, which contradicts the objective of FAR 1.102(b)(1).[1495] In fact, FAR 6.000 differentiates the principle of open and full competition and the outcomes of competition, stating that 'this part does not deal with the results of competition (e.g., adequate price competition)'.[1496] According to FAR 15.403-1(c)(1), adequate price competition involves two or more responsible offerors competing independently at reasonable prices, with their offers meeting the solicited requirements.[1497]

By their very nature, reserving contracts for small businesses limits the pool of competitors for a contract to a subset of the market, representing the main criticism that such programmes have received.[1498] Indeed, in reserved contracts, competition from large businesses is eliminated, but competition from small businesses is enhanced compared with non-reserved contracts.[1499] Nakabayashi estimates that without reserved contracts, approximately 36 per cent of small businesses would not participate in the procurement market.[1500] The overall impact of reserved contracts on competition results from decreased participation by large businesses and increased competition from small businesses. A more rigorous assessment should also consider

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[1495] 48 CFR § 1.102(b)(1).

[1496] 48 CFR § 6.000. According to FAR 15.403 – 1 (c)(1), adequate price competition refers to two or more responsible offerors competing independently with reasonable prices, and their offers satisfying the solicited requirements.

[1497] 48 CFR § 15.403 – 1 (c)(1) (2023).

[1498] Andrew George Sakallaris, 'Questioning the Sacred Cow: Reexamining the Justifications for Small Business Set Asides' (2007) Public Contract Law Journal Vol. 36, No.4, 699; Kirkwood (n 106) 315; Carol Cravero, 'Socially Responsible Public Procurement and Set-Asides: A Comparative Analysis of the US, Canada and the EU' (2017) 8 Arctic Review on Law and Politics 174.

[1499] Matilde Cappelletti and Leonardo M. Giuffrida, 'Targeted Bidders in Government Tenders' (2022) ZEW Discussion Papers, No 22-030, ZEW - Leibniz-Zentrum für Europäische Wirtschaftsforschung, Mannheim.

[1500] Jun Nakabayashi, 'Small Business Set-Asides in Procurement Auctions: An Empirical Analysis' (2013) 100 Journal of Public Economics 28, 29.

the impact of reserved contracts on non-reserved contracts; however, there is a lack of literature on this. In principle, when large businesses recognise that a specific proportion of contracts is reserved for small businesses, they might participate more vigorously in competitions for non-reserved contracts, unless they are discouraged and exit the procurement market. Given that the proportion of contracts awarded to small businesses has remained consistently around 28 per cent, it is evident that large businesses continue to dominate the federal procurement market.[1501]

Comparing the numbers of bids in these two types of contracts, Cappelletti and Giuffrida have found that reserved contracts in federal procurement from 2008 to 2018 had attracted a higher number of bids from small businesses than non-reserved contracts, which offsets the decreased competition from large businesses. [1502] Similarly, Tkachenko et al. observed that reserved contracts attracted more bids than non-reserved contracts in the procurement procedures for homogeneous goods, thereby lowering the price paid by the contracting authority, which will be discussed in the subsequent section.[1503] The evidence above suggests that reserved contracts do not undermine competition in the procurement market, but serve as a tool to incentivise alternative competition that was discouraged in open competition procedures.

Furthermore, the discussion about open and full competition in procurement is more idealistic than practical in federal procurement. Among contracting methods, sealed bidding (including two-step sealed bidding) and competitive proposals are competitive

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[1501] See Section 7.3.5.

[1502] Cappelletti and Giuffrida (n 1499); also see Andrey Tkachenko and others, 'Efficient Design of Set-aside Auctions for Small Businesses: an Empirical Analysis' (October 2019) <https://www.economia.unipd.it/sites/economia.unipd.it/files/20190240-b.pdf> accessed 19 May 2023, 3.

[1503] Tkachenko and others (n 1502) 3.

procedures that pursue open and full competition, whereas contracting by negotiation is not a competitive procedure.[1504] Contracting officers are not permitted to discuss or negotiate with bidders in a sealed bidding procedure, and the award is made solely based on price or price-related factors.[1505] Even though the FAR clearly states that agencies shall pursue competition and use competitive procedures, most procurement contracts are awarded through negotiated procedures.[1506] Sealed bidding was frequently used until the twentieth century, when contracting officers began to favour multilateral competitive negotiations.[1507] In 2014, sealed bidding was used in only 2.06 per cent of all federal procurement contracts.[1508] Negotiated proposals are the most used procedures, accounting for 38.64 per cent of all federal procurement.[1509] Single-source solicitation (28.68 per cent) and IDIQ contracts (21.42 per cent) were also used frequently.[1510] Regarding the number of bids, sealed bidding has the lowest ratio of one bid, and it is common to have only one bidder for a solicitation across all federal procurements.[1511] Competitive procedures are less used compared with non-competitive procedures, especially contracting by negotiation.[1512] This observation may reveal that agencies favour procedures other than sealed bidding because they

[1504] 48 CFR § 6.102.

[1505] 48 CFR § 14.101.

[1506] See Patrick Bajari, Robert McMillan and Steven Tadelis, 'Auctions Versus Negotiations in Procurement: An Empirical Analysis' (2009) 25 The Journal of Law, Economics, and Organization 372, 373; also see Brad Nathan, 'Show Your Hand: The Impacts of Fair Pricing Requirements in Procurement Contracting' (2024) 62 (4) Journal of Accounting Research 1405, 1412.

[1507] Yukins, 'The U.S. Federal Procurement System: An Introduction' (n 253) 79.

[1508] ibid 81.

[1509] Yukins, 'The U.S. Federal Procurement System: An Introduction' (n 253) 81.

[1510] ibid 81.

[1511] Karam Kang and Robert A Miller, 'Winning by Default: Why Is There So Little Competition in Government Procurement?' (2022) 89 The Review of Economic Studies 1495, 1496.

[1512] Yukins, 'The U.S. Federal Procurement System: An Introduction' (n 253) 82.

would evaluate fewer bids, whereas sealed bidding often necessitates evaluating more bids.

In summary, as a statutory exception to the principle of open and full competition, reserving contracts for small businesses does not undermine this principle and may create more competition in the market as a result. In US federal procurement, the principle of open and full competition is a compromised principle that must be balanced with the pursuit of public policy objectives, including small businesses support.[1513]

7.4.3 The balance between small business set-asides and best value for money

As discussed in Section 7.3.1, the core principle of federal procurement is the pursuit of best value in a timely manner, typically achieved through market competition.[1514] Reserving contracts for small businesses is a statutory exception to the principle of full and open competition.[1515] However, rather than diminishing competition, they foster an alternative form of competition limited to small businesses. The key question, therefore, is whether this alternative competition undermines, if not supports, the overarching objective of best value for money.

In reserved contracts, the balance between best value and small business assistance is struck by the pursuit of 'a fair market price'.[1516] The Rule of Two requires that contracting officers shall only set aside a contract for small businesses when there is an expectation that two or more responsible small businesses will submit tenders, and

[1513] 48 CFR § 1.102 (a).
[1514] 48 CFR § 1.102 (b).
[1515] See Section 7.4.2.
[1516] 15 USC § 644 (a)(7).

an award will be made at fair market prices.[1517] Contracting officers are empowered under 15 U.S.C. 644 (a)(7) to withhold reserving contracts if small businesses cannot offer a fair price.[1518] However, this does not imply that contracting officers may circumvent a set-aside by asserting that large businesses can offer a lower price, unless the difference is substantial.[1519] The GAO has addressed this issue in bid protests where a small business challenges a contracting officer's decision to withdraw a set-aside. In case B-196588, the GAO upheld the agency's withdrawal after determining that the price offered by large businesses was 7.2 per cent lower than the price offered by the only responsible small business.[1520] With no fixed thresholds to determine a 'fair market price', contracting officers exercise their business judgments based on market research to determine whether a contract can be reserved for small businesses or not.[1521] Given the discretionary authority of contracting officers to assess reasonable pricing expectations, it is reasonable to infer that products or services procured through reserved contracts do not significantly exceed fair market prices.[1522]

Nakabayashi's research indicates that contracting authorities may not experience cost increases; in fact, they would potentially save costs when contracts are reserved for small businesses.[1523] Similarly, Tkachenko et al. have observed that the price paid by the contracting authority for homogeneous goods in reserved contracts is lower than in non-reserved contracts, as the reserved contracts attracted more bids.[1524]

[1517] 48 CFR § 19.502-2; 15 USC § 644 (a)(7).
[1518] 15 USC 644 § (a)(7).
[1519] See GAO, *Lipps, Inc*, B-196588 (15 February 1980).
[1520] Ibid.
[1521] See GAO, *Mountain West Helicopters, LLC; Trans Aero, Ltd.* B-408150, B-408150.2 (01 July 2013).
[1522] See US House Committee on Small Business (n 455).
[1523] Nakabayashi (n 1500) 41.
[1524] Tkachenko and others (n 1502) 3.

Szerman's study found no significant effect on unit prices of off-the-shelf goods between reserved contract auctions and non-reserved auctions.[1525] Despite these findings suggesting that set-asides do not increase costs for contracting authorities, Cappelletti and Giuffrida's analysis of federal procurement from 2008 to 2018 revealed higher cost overruns and more frequent contract performance delays in reserved contracts for small businesses.[1526] Moreover, they noted that reserved contracts for socioeconomic small businesses exhibited poorer contract performance compared to those for general small businesses.[1527] It is argued that the more restricted the target group is, the higher the risk of poor performance of the contract, regardless of the competition during bidding.[1528] Nevertheless, Roy et al observe that contract performance and cost overruns are related to factors such as a contractor's prior procurement experience and the timing of the contract award within the fiscal year.[1529] This finding suggests that well-calibrated set-asides do not necessarily compromise contract performance and impose additional costs on agencies.[1530]

In summary, reserving contracts for small businesses does not undermine the pursuit of best value, provided that federal agencies do so in accordance with the regulatory framework, namely, when there is a reasonable expectation of fair market pricing and competition from at least two small businesses.[1531] It is evident that for homogeneous products or off-the-shelf goods, reserved contracts do not significantly increase costs

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[1525] Dimitri Szerman, 'Public procurement auctions in Brazil' (PhD thesis, The London School of Economics and Political Science 2012) <https://etheses.lse.ac.uk/681/> accessed 23 June 2023, 80.
[1526] Cappelletti and Giuffrida (n 1499) 2.
[1527] ibid 17.
[1528] See Cappelletti and Giuffrida (n 1499) 5.
[1529] Dwaipayan Roy, Anant Mishra and Kingshuk K Sinha, 'Advancing Small Business Inclusion in Public Procurement: Evidence From U.S. Federal Government R&D Contracts' (2024) 33 Production and Operations Management 2201, 2210.
[1530] ibid 2217.
[1531] See 48 CFR § 19.502-2.

and may even reduce costs when increased competition among small businesses occurs in reserved contracts.[1532] Conversely, for services and works lacking clear standards, the uncertainties surrounding contract performance can result in higher costs for contracting authorities. Nevertheless, the risk of suboptimal performance exists in both reserved and non-reserved contracts. This necessitates the implementation of more robust tools to monitor contract performances and the enhancement of supplier qualification evaluation.

7.4.4 The balance between small business set-asides and administrative costs

Given that minimising administrative operating costs constitutes one of the general objectives established under FAR 1.102(b), it is essential to evaluate whether reserving contracts for small businesses may compromise this objective.[1533] The minimisation of administrative operating costs represents a pursuit of enhanced efficiency in procurement procedures.

The empirical literature presents a nuanced picture regarding the administrative burden of set-aside programmes. Cappelletti and Giuffrida have observed that set-asides for small businesses in federal procurement incurred higher cost overruns and more delays in contract performance.[1534] In contrast, Snider et al have found that agencies implement socioeconomic set-aside programmes because such programmes render their administrative processes more convenient.[1535] They further identified that contracting officers often lack contracting capacity to evaluate a large

[1532] Thomas A Denes, 'Do Small Business Set-Asides Increase the Cost of Government Contracting?' (1997) 57 Public Administration Review 441.
[1533] 48 CFR § 1.102(b).
[1534] ibid.
[1535] Snider, Kidalov and Rendon (n 1487).

number of tenders, potentially attributable to personnel downsizing.[1536] This organisational capacity deficit incentivises them to reserve contracts for socioeconomic small businesses to reduce the potential number of bidders.[1537] Notably, Hawkins et al. have discovered that set-aside procedures cost USD 91,000 less than non-reserved contracts for federal agencies in terms of transaction cost.[1538] This cost reduction may be attributed to the fact that proposals submitted by small businesses are less complex, and the process is more streamlined.[1539]

However, if contracting officers could genuinely reduce their workload by reserving contracts for small businesses, one would expect the SBA scorecard to reflect considerably more positive outcomes than currently observed. This suggests that while some agencies may exploit set-aside programmes to reduce the administrative burden of evaluating offers, there may be procedures with even less cost, for example, placing orders in GSA Schedule or the Best In Class established contractor list, etc, as discussed in 7.4.1.2.

In summary, there is insufficient evidence to argue that set-asides incur significantly higher administrative costs for federal agencies or undermine the pursuit of best value in the federal procurement system. Within the range of procurement procedures available to agencies, it is reasonable to anticipate that contracting officers intend to use the procedures with lower administrative costs when making a purchase. Small business set-asides may not be the least costly ones, but also not the most expensive ones.

[1536] ibid 399.

[1537] Snider, Kidalov and Rendon (n 1487).

[1538] Timothy Hawkins, Michael Gravier and Wesley S Randall, 'Socio-economic sourcing: benefits of small business set-asides in public procurement' (2018) 18 Journal of Public Procurement 217, 234.

[1539] ibid.

7.5 Conclusion

This chapter analysed reserved contracts for small businesses in US federal procurement, focusing on the regulatory framework and the impact of these contracts on small businesses and federal procurement. The federal government's performance in achieving small business contracting goals has improved since 2013. [1540] Nevertheless, the number of small contractors in federal procurement decreased significantly in recent years due to multiple factors, especially the increasing use of category management.[1541] This trend may continue under the current administration, as President Donald Trump issued an executive order aimed at reforming the FAR and strengthening the efficiency objective.[1542]

In summary, the reserved contracts mechanism may increase the number of contracts awarded to small businesses; however, over the longer term, it does not create incentives for small businesses to enhance their capacity and compete effectively with larger businesses. Instead, it may encourage them to preserve their small-business status in order to remain eligible for set-aside programmes. The cascade evaluation system, in particular, incentivises small businesses to acquire socioeconomic attributes to qualify for the first tier of bidders and multiple set-aside programmes

[1540] See Section 7.3.5.

[1541] See Section 7.4.1.2.

[1542] The White House, Restoring Common Sense to Federal Procurement (Executive Order 14275, 15 April 2025); Executive Office of the President, OMB, 'Overhauling the Federal Acquisition Regulation' (Memorandum M-25-26, 2 May 2025) <https://www.whitehouse.gov/wp-content/uploads/2025/02/M-25-26-Overhauling-the-Federal-Acquisition-Regulation-002.pdf> accessed 17 July 2025; also see Bibi Hidalgo, 'Main Street undermined: The federal decision to shift contracting from small innovators to corporate giants—and ways to fix it' (Brookings, 12 May 2025) <https://www.brookings.edu/articles/main-street-undermined-the-federal-decision-to-shift-contracting-from-small-innovators-to-corporate-giants-and-ways-to-fix-it/> accessed 17 August 2025.

rather than focusing on growing and developing their economic and technical capacity. Reserved contracts may provide small businesses with contract opportunities in the short term. However, sustained reliance on reserved contracts can hinder their ability to compete with larger businesses in both public procurement and the private sector over time. Such reliance contradicts the objectives of small business policies outlined in the Act, which aim to cultivate a robust small business sector and uphold market competition within the national economy.

Nevertheless, this chapter has demonstrated that reserving contracts for small businesses does not undermine other objectives of the federal procurement system, such as best value, competition, and efficiency. Although reserved contracts represent an exception to the principle of full and open competition, they may not necessarily diminish actual competition compared to non-reserved contracts.[1543] Actual competition depends on the potential combined effect of increased participation from small businesses and decreased participation from large businesses. The impact of reserved contracts on procurement prices varies case by case, with current evidence indicating that reserved contracts generally do not exert a significant upward pressure on prices.[1544]

It is important to note that the US approach is distinctive in that statutory preferences for small businesses, first established in the Small Business Act of 1953, long predated the creation of the modern federal procurement framework under the Competition in Contracting Act of 1984 and the FAR.[1545] It is reasonable to assert that small business preference constitutes an intrinsic objective within the US federal procurement system,

[1543] See Section 7.4.2.
[1544] See Section 7.4.3.
[1545] See Nagle (n 27) ch 23.

pursued alongside other objectives within a balanced framework. Although much similar to the pendulum swinging between regulation and deregulation, the emphasis placed upon different objectives within the federal procurement system may shift across different administrations.[1546] For jurisdictions without small business preference embedded in the procurement system, the introduction of reserved contracts as a supportive measure for small businesses may generate tension with competing objectives. The implications of this issue will be examined in the Concluding chapter.

[1546] Joshua I Schwartz, 'Regulation and Deregulation in Public Procurement Law Reform in the United States' in Gustavo Piga and Khi Thai (eds), *Advancing Public Procurement: Practices, Innovation and Knowledge-Sharing* (PrAcademics Press 2007) 177; also see Trybus, 'Beyond Competition and Value for Money' (n 36) 225.

Chapter 8 Conclusions and Key Considerations for Policymakers

8.1 Introduction

This concluding chapter synthesises the principal findings of the thesis and addresses the research questions. The thesis has examined four legally binding SME-friendly measures, division into lots,[1547] management of qualification processes,[1548] bid preferences,[1549] and reserved contracts,[1550] analysing their legal frameworks, implementation, and effectiveness where empirical evidence permits evaluation.

This thesis addressed three interrelated research questions (RQs):

RQ1: what barriers limit SME participation in public procurement?

RQ2: how effective are the selected SME-friendly measures in addressing the specific barriers faced by SMEs in public procurement?

RQ3: what trade-offs arise from the implementation of SME-friendly measures in public procurement, particularly with respect to other procurement objectives such as value for money, competition, non-discrimination, and efficiency?

These questions are inherently interconnected: understanding the barriers SMEs face (RQ1) is essential for evaluating whether measures effectively address those specific

[1547] See Chapter 4.
[1548] See Chapter 5.
[1549] See Chapter 6.
[1550] See Chapter 7.

barriers (RQ2), whilst assessing effectiveness requires examining whether any gains in SME participation come at the cost of other procurement objectives (RQ3).

To answer the research questions, this thesis adopts a doctrinal legal analysis of primary and secondary sources, supported by empirical evidence where available.[1551] As explained in Chapter 1, this is not a systematic comparative analysis of different jurisdictions' SME-friendly measures. Rather, it adopts a multi-jurisdictional illustrative approach that examines each measure primarily in the jurisdiction(s) where it has been most extensively developed and implemented. This approach enables in-depth analysis of how each measure can be designed and calibrated whilst acknowledging that legal contexts differ significantly across jurisdictions.

The jurisdictional scope varies depending on the measure under discussion.[1552] Chapter 4 (division into lots) focuses on the EU due to its long tradition of supporting SMEs in public procurement since 1990, and the 2014 introduction of division into lots has been widely discussed regarding its effectiveness and limitations.[1553] The analysis of the division into lots consists not only of how it was prescribed in Directive 2014/24/EU, but also of how it was transposed and implemented in Member States. To complete these two levels of analysis, Germany and France were selected due to their long tradition of supporting SMEs in public procurement through dividing contracts into lot regimes.[1554] Chapter 5 (managing the qualification process) draws primarily on the EU and US federal procurement regimes to illustrate different regulatory approaches to addressing SMEs' difficulties with financial capacity

[1551] See Chapter 1, Section 1.4.
[1552] ibid, Section 1.4.2.
[1553] See Chapter 4.
[1554] ibid.

requirements, past performance records, and shortlisting.[1555] Chapter 6 (bid preferences) examines Brazil, the US (both federal HUBZone preferences and California's state-level bid preferences), and South Africa, representing four distinct models of how bid preferences can be designed and calibrated to support SMEs in the competition for public procurement contracts.[1556] Lastly, Chapter 7 (reserved contracts) focuses exclusively on US federal procurement, which provides the most extensively implemented model of reserved contracts for small businesses.[1557]

RQ1, concerning the barriers SMEs face in accessing public procurement, was addressed in Chapter 3, which identified three structural entry barriers arising from procurement rules and practices: excessive contract size that excludes SMEs from participation, disproportionate qualification criteria that impose undue burdens on SMEs, and high transaction costs associated with bidding that weigh more heavily on smaller businesses.[1558] This concluding chapter therefore focuses on answering RQs 2 and 3. Section 8.2 synthesises the principal findings for each of the four measures, addressing RQ2 (effectiveness in addressing barriers and enhancing SME participation) and RQ3 (tensions with other procurement objectives). It draws on insights from Chapters 4-7 to demonstrate how differences in legal design and implementation affect their effectiveness and the trade-offs involved with other procurement objectives, including non-discrimination, value for money, competition, and efficiency. Building this foundation, Section 8.4 compares the four measures across three critical dimensions: how contract value influences measure selection; how eligibility criteria should be structured for preferential measures; and what

[1555] See Chapter 5.
[1556] See Chapter 6.
[1557] See Chapter 7.
[1558] See Chapter 3, Section 3.3.9.

incentives are needed to ensure effective implementation by contracting authorities. This comparison of measures reveals that no single measure is universally superior; rather, effectiveness depends on matching measures to specific barriers, contract characteristics, and institutional contexts.

Section 8.3 examines jurisdictional approaches to SME-friendly measures through preliminary observations. Whilst not a systematic comparative analysis, this section identifies patterns in why certain measures are prominent in particular jurisdictions, considering how legal constraints (domestic and international) and policy priorities shape measure selection across the EU, the US, Brazil, and South Africa.

Having examined how each measure operates in different jurisdictions and the potential reasons behind jurisdictional choices, Section 8.5 presents key considerations for legislators and policymakers designing or reforming SME-friendly measures. These considerations, derived from the comprehensive analysis of the four measures, identify important factors that policymakers should take into account, such as defining beneficiaries, assessing existing SME participation, and understanding legal constraints. These considerations are necessarily generic rather than prescriptive, requiring adaptation to specific legal frameworks and policy priorities. Section 8.6 offers concluding remarks and directions for future research.

8.2 Principal Findings and Response to the Research Questions

This section answers the research questions and synthesises the key findings concerning four prominent SME-friendly measures investigated in Chapters 4-7, with a focus on their effectiveness in achieving their intended objectives. It draws on the

analysis of barriers and challenges discussed in Chapter 3, considering how each measure is designed to address specific barriers faced by SMEs. It also examines the extent to which each measure creates tensions with other objectives of public procurement systems.

8.2.1 Dividing large contracts into lots

Dividing large contracts into lots reduces the size and complexity of procurement opportunities, thereby making them more accessible and manageable for SMEs.[1559] In addition, it can potentially alleviate the financial qualification burden often linked to the overall estimated contract value. As such, the division into lots addresses two key entry barriers and has the potential to increase SME participation, particularly among micro and small enterprises (MSEs).[1560] Although medium-sized enterprises are generally less constrained by contract size, dividing contracts in areas where they are less represented may also facilitate their involvement.[1561] The effectiveness of this measure, however, depends on the careful design of both the size and number of lots, as different configurations may benefit different categories of SMEs.[1562]

As discussed in Chapter 4, the impact of the division into lots hinges on nuanced aspects of the legal and procedural design. Six key regulatory elements can vary across countries and influence its implementation: (1) the scope of discretion that contracting authorities have, i.e. whether contract division is mandatory or voluntary

[1559] See Chapter 3, Section 3.3.2; Chapter 4.
[1560] For the definition of SMEs, MSEs, and small businesses, see Chapter 2.
[1561] See Chapter 3, Section 3.2.2.
[1562] See Chapter 4, Section 4.4.

('divide') and the scope of justification required for a non-division ('or explain') decision; (2) the methods of division, and the size and number of lots; (3) the limitation on the number of lots that can be awarded to a single bidder; (4) whether lot bundling is acceptable; (5) whether alternative bids are acceptable; (6) and whether lots can be reserved for SMEs.[1563] The regulation of these aspects depends on the priorities of a procurement system and can significantly impact the effectiveness of the measure. For example, in France, the aim of lot division is a combination of increasing SME participation and competition in public procurement, which means increasing SME participation without compromising competition from large businesses.[1564] Under this constraint, contracting authorities have much discretion not to divide contracts. In contrast, the objective of lot division in Germany is to protect the interests of SMEs rather than increasing competition, which leads to a stricter approach where contracting authorities have limited discretion.[1565]

The legal design, or drafting of the division into lots regime, involves an inherent balance between facilitating SME access and preserving the value for money and cost-efficiency of contracting authorities. When the cost efficiency of contracting authorities is prioritised, lot bundling and alternative bids shall not be prohibited, as such practices may decrease administrative burden for contracting authorities, compared with contract awards on a lot-by-lot basis. However, allowing lot bundling puts large businesses in an advantageous position, as they can bid for the whole contract by bundling all lots together and offering a lower price. In this case, the division into lots struggles to achieve its intended objective of increasing SME

[1563] ibid, Section 4.3.
[1564] See Chapter 4. Section 4.2.2.
[1565] See Chapter 4, Section 4.3.1.2.

participation, as set out in Recital 78 Directive 2014/24/EU.[1566] If SMEs' interest is prioritised, lot bundling and alternative bids shall be either prohibited or restricted, only acceptable when there is a disproportionate cost savings for contracting authorities, which is exemplified by the regulation of lot division in Germany.[1567]

In summary, dividing contracts into lots presents efficiency trade-offs, as contracting authorities must manage multiple smaller contracts rather than engaging a single prime contractor. However, this efficiency compromise can be calibrated through judicious lot bundling arrangements, which may safeguard efficiency and value for money whilst preserving SME access. The extent to which efficiency may be subordinated to SME interests varies jurisdictionally, as demonstrated by German practice, where SME considerations may legitimately override efficiency concerns to a certain extent.

8.2.2 Managing the qualification process

Excessive qualification criteria act as a barrier to entry for most SMEs across different jurisdictions.[1568] Therefore, managing the qualification process to limit such criteria and reduce the associated administrative costs has the potential to increase SME participation. This measure differs from the other three measures analysed in this thesis, as it includes multiple aspects where SME-friendly consideration can be embedded, including financial capacity thresholds, past performance records, and bid guarantees. The timing of the verification process and the criteria of the shortlisting

[1566] Directive 2014/24/EU, recital 78.
[1567] See Chapter 4, Section 4.3.
[1568] See Chapter 3, Section 3.3.2.

process in restricted procedures can also be altered to facilitate SME access to public procurement markets. Methods to manage the qualification process range from imposing turnover requirement caps to reducing bidding costs through standardised qualification documents, such as the European Single Procurement Document (ESPD), as discussed in Chapter 5.

There is synergy between dividing contracts into lots and the financial capacity requirement, as discussed in Chapter 5 with reference to Article 58(3) Directive 2014/24/EU.[1569] To ensure that potential contractors have sufficient financial capacity to perform the contract, contracting authorities typically require a certain level of financial capacity, often evidenced by annual turnover (revenue).[1570] In order to avoid this requirement becoming a barrier to SME participation, Article 58(3) Directive 2014/24/EU provides that the required annual turnover must not exceed twice the estimated contract value of the contract.[1571] This issue becomes particularly relevant when a contract is divided into lots. If the turnover requirement continues to reflect the total estimated value of the overall contract rather than the value of the individual lot, smaller bidders may still be excluded, even where the lot itself is of a manageable size. To address this, Article 58(3) Directive 2014/24/EU requires that the financial capacity requirement be proportionate to the value of the specific lot, rather than the total value of the contract, and be adjusted accordingly if a bidder is awarded multiple lots.[1572]

In US federal procurement, instead of prescribing specific financial capacity requirements, contracting officers evaluate offerors' responsibility by examining

[1569] Directive 2014/24/EU, article 58(3).
[1570] See Chapter 5, Section 5.2.2.
[1571] Directive 2014/24/EU, art 58(3); Chapter 5, Section 5.2.1.1.
[1572] Directive 2014/24/EU, art 58(3).

evidence of their ability to obtain sufficient financial resources to perform the contract.[1573] From the perspective of small businesses, permitting proof of resource access instead of immediate possession reduces entry barriers and alleviates the necessity for substantial upfront investments. The timing of the qualification process also matters. Directive 2014/24/EU generally requires that qualification be assessed before the submission of tenders, whereas under the US FAR the determination of a bidder's responsibility determination (the functional equivalent of qualification) usually occurs after bid submission and evaluation of the offers.[1574] This procedural divergence is important because it affects both administrative efficiency and the accessibility of procurement procedures for SMEs. Early qualification assessment, as required in Directive 2014/24/EU, may deter SMEs that struggle to meet demanding requirements and provide documents at the outset, even if they are capable of delivering the contract. In contrast, the US approach lowers the initial barrier to entry by allowing all bidders to participate in the tender process, deferring the responsibility assessment until after the evaluation stage. This arrangement reduces administrative burden on SMEs and may encourage broader participation. However, this involves a balance between the cost efficiency of contracting authorities and the interests of SMEs. Lower entry barriers may induce a higher volume of tenders, which in turn increases the workload of contracting authorities during evaluation.

Under Directive 2014/24/EU, apart from the cap on the turnover requirement, the principle of proportionality can also be used to support SMEs.[1575] For example,

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[1573] See Chapter 5, Section 5.2.1.2.

[1574] See Chapter 5, Section 5.2.4.

[1575] ibid, Section 5.2.1. Also see Chris Jansen, 'Stretching the proportionality principle: how Dutch law facilitates the participation of SMEs in public procurement' (2022) 4 Public Procurement Law Review 214.

contracting authorities shall not require experience of public procurement exclusively, but also accept evidence showing the bidder's technical capacity with an equivalent contract experience, even if that was not in public procurement. In another example, bid guarantees may be justified in complex service contracts or negotiated procedures, where significant time and effort are invested in selecting the best offer.[1576] Conversely, in standardised goods procurement, where the withdrawal of the best tenderer may not result in substantial damages, requiring a bid guarantee may be unnecessary.[1577] In the US, the Small Business Administration (SBA) operates a Surety Bond Guarantee Program to assist small businesses unable to obtain such guarantees independently.[1578] The support provided by the SBA is also discussed in Chapter 7 on reserved contracts.[1579]

Lastly, Chapter 5 pointed out that the shortlisting process in procedures other than open procedures under Directive 2014/24/EU may discriminate against SMEs, as contracting authorities usually rank qualified bidders based on selection criteria and invite a certain number of them to submit bids.[1580] The challenge posed by the shortlisting process to SMEs seems to be overlooked by Directive 2014/24/EU.[1581] One approach to mitigate this disadvantage is to consider alternative methods that do not solely rely on ranking by economic capacity or size. For example, in France, contracting authorities have the option to draw lots from qualified candidates to determine which are invited to tender.[1582]

[1576] See Chapter 5, Section 5.2.3.
[1577] ibid.
[1578] See Chapter 5, Section 5.2.3.2
[1579] See Chapter 7, Section 7.3.
[1580] See Chapter 5, Section 5.2.4.
[1581] ibid.
[1582] ibid.

Since managing the qualification process typically does not interfere with tender evaluation, they generally remain consistent with core procurement objectives. However, where measures explicitly prioritise SME interests, such as the US FAR's Certificate of Competency (COC) process,[1583] which empowers the SBA to override contracting authority responsibility determinations, risks to other objectives may emerge if protected small businesses subsequently default or underperform. Nevertheless, underperformance concerns warrant careful examination, as some criticisms may reflect pro-large business attitudes, which assume superiority of larger contractors in terms of capability and cost-effectiveness.[1584] In practice, however, there is evidence that large businesses may submit lower initial bids but subsequently increase prices or create market dependencies that deter competitor participation, thereby compromising long-term competition and value for money. [1585]

8.2.3 Bid preferences

Bid preferences operate differently from division into lots and managing qualification processes. Whilst the latter two address entry barriers that prevent SMEs from participating in tenders, bid preferences operate at the award stage, providing a margin of preference or scoring advantage to increase SMEs' likelihood of winning contracts once they have submitted bids.[1586] This means bid preferences do not assist SMEs in overcoming entry barriers such as identifying opportunities, dealing with large

[1583] See Chapter 5, Section 5.2.2.

[1584] Loader, 'Is Public Procurement a Successful Small Business Support Policy? A Review of the Evidence' (n 74).

[1585] Francesco Decarolis, 'Awarding Price, Contract Performance, and Bids Screening: Evidence from Procurement Auctions' (2014) 6 American Economic Journal: Applied Economics 108.

[1586] See Chapter 6, Section 6.1.

contract sizes, or meeting stringent qualification criteria. However, for SMEs that have already overcome these entry barriers, bid preferences can enhance their competitiveness against larger bidders.

Intuitively, the trade-off associated with bid preferences lies in the potential increase in procurement costs, weighed against the policy objective of promoting SME participation. However, as discussed in Chapter 6, bid preferences do not invariably lead to higher procurement costs or compromise value for money. By altering competitive dynamics, preferences may incentivise unfavoured bidders to submit more competitive offers, thereby offsetting the advantage granted to SMEs. The actual cost impact depends on factors such as the size of the preference and the competition dynamics between favoured and non-favoured bidders.[1587]

Moreover, different designs of bid preferences vary in their cost implications. For example, Brazil's 'fictitious-tie' model, introduced under LC 123/2006, allows MSEs to match the lowest bid if their offer is not higher than 5 per cent or 10 per cent, depending on the type of procurement procedure.[1588] This design preserves competitive pricing while offering targeted support to MSEs. Empirical data from 2006 to 2013 indicates a rise in the number of contracts awarded to SMEs under this scheme, demonstrating its effectiveness in enhancing participation and contract awards without significantly increasing procurement costs.[1589] In contrast, the price preference available to HUBZone small businesses under the US FAR has shown only limited

[1587] Geo Quinot and Benjamin V Rosa, 'Colloquium' in Annalisa Castelli, Gustavo Piga and Tünde Tátrai (eds), *The Economics and Law of Public Procurement: New Global Scenarios* (Routledge 2024) 163, 168

[1588] See Chapter 6, Section 6.2.1.

[1589] See Chapter 6, Section 6.2.3.

effectiveness.[1590] This is largely due to the coexistence of multiple small business programmes, with HUBZone small businesses often securing contracts through reserved contracts rather than bid preferences.[1591]

8.2.4 Reserved contracts

Like bid preferences, reserved contracts do not reduce contract sizes or participation costs, nor do they ease the qualification criteria; they do respond to concerns voiced by small businesses, such as the competition pressure from large businesses or the potential pro-large bias of contracting authorities. Specifically, reserved contracts provide small businesses a chance to compete exclusively against businesses with similar levels of capacity and development.[1592] This eliminates the pressure of competing with large businesses, thereby motivating more small businesses to participate in government procurement.

As discussed in Chapter 7, preferences for small businesses in federal procurement are rooted in the Small Business Act and operationalised through the FAR, which mandates that contracts with a value below the simplified acquisition threshold (currently USD 250,000) be reserved for small businesses.[1593] For contracts valued above the simplified acquisition threshold, federal agencies shall investigate the market and determine if there will be two or more small businesses submitting tenders, and a contract shall be reserved when such expectation is satisfied.[1594] Moreover,

[1590] See Chapter 6, Section 6.3.1.2.
[1591] ibid.
[1592] See Chapter 7, Section 7.1.
[1593] 48 CFR § 19.201; see Chapter 7, Section 7.3.
[1594] ibid.

reserved contracts are used together with statutory and regulatory spending targets. The SBA monitors the performance of federal agencies against the small business contracting targets that they set. The federal government has consistently achieved the 23 per cent contracting goal with small businesses since 2013.[1595] While reserved contracts can provide short-term benefits to SMEs by providing them with business opportunities, they may also foster dependency, discouraging SMEs from expanding and competing with larger firms. This reliance undermines the long-term goal of promoting the competitiveness of SMEs.

As for the trade-off that emerged in reserved contracts, academic literature often highlights the tension between the compromised competition and the interests of small businesses.[1596] In theory, reserved contracts limit competition only to small businesses, and the decreased competition from large businesses may increase procurement costs and compromise value for money. However, empirical evidence does not support this concern.[1597] Despite deviating from the principle of full and open competition, the analysis in Chapter 7 demonstrates that competition within reserved contracts is not necessarily inferior to non-reserved contracts.[1598] Although competition from large businesses decreases, reserved contracts attract greater participation from small businesses, generating sufficient competitive pressure to maintain or even reduce procurement costs. Moreover, the regulatory framework incorporates safeguards to balance value for money with small business support. Under 15 USC. 644 (a)(7), a contract may not be reserved for small businesses if the offer from small businesses would exceeds a fair market price, ensuring that small

[1595] See Chapter 7, Section 7.3.5.
[1596] See Trybus and Andrecka (n 55) 225.
[1597] See Chapter 7, Section 7.3.2.
[1598] See Chapter 7, Section 7.3.3.

business support does not compromise value for money.[1599] Nevertheless, there is evidence of poor contract performance of reserved contracts, and those underperforming ones are usually works or services contracts, where more transparent technical standards shall be stipulated. For standardised off-the-shelf procurement, reserved contracts do not exhibit underperformance.[1600]

8.2.5 Summary

To assess whether measures effectively enhance SME participation, it is essential to determine whether they address entry barriers or grant SMEs competitive advantages during tender evaluation. The evidence examined in this thesis indicates that entry barriers sufficiently deter SME participation in most contexts, making market access the primary concern.[1601] Therefore, addressing entry barriers should constitute the primary consideration in designing SME-friendly measures, unless empirical data demonstrates adequate market entry by SMEs, evidenced by substantial SME bidding volumes with low success rates, in which case preferential measures addressing competitive disadvantages may be warranted.

If SMEs do not face significant entry barriers, preferential measures may increase contract awards to SMEs in the short term. However, as demonstrated in Chapters 6 (bid preferences) and 7 (reserved contracts), such measures carry long-term risks of entrenching incumbent SME winners, potentially creating new barriers for inexperienced SMEs seeking market entry, as established SME contractors may enjoy

[1599] 15 U.S.C. 644 (a)(7); Chapter 7, Sections 7.3.2 and 7.3.3.
[1600] See Chapter 7, Section 7.4.2.
[1601] See Chapter 3, Section 3.1.

advantages within preferential frameworks. This risk can be mitigated through graduation mechanisms that limit the duration of preferential access, though such mechanisms require careful design to prevent circumvention through fronting arrangements.

Regarding the trade-offs between SME interests and other objectives of public procurement, the relationship is fundamentally characterised by balancing competing considerations rather than fixed hierarchies. Crucially, the analysis reveals that the prioritisation of objectives varies across jurisdictions: whilst some systems prioritise traditional procurement objectives such as value for money and competition, others elevate SME advancement or transformative goals to address historical disadvantages.[1602] Moreover, not all procurement systems pursue competition or efficiency as primary objectives, demonstrating that the relationship between SME support and other goals must be assessed contextually rather than assumed universally.

Preferential measures are frequently perceived as posing greater risks to value for money, competition, and efficiency objectives.[1603] However, the analysis in Chapters 6 and 7 demonstrates these concerns may be overstated, provided contracting authorities exercise appropriate caution in tender evaluation processes. With calibrated measure design, such as the size of a bid preference, preferential measures may increase competition and even lower procurement costs for contracting authorities.[1604] This is mainly because SMEs represent an untapped competition

[1602] See Section 8.3.2 on small business policy in the US and Section 8.3.4 on South Africa's transformative objectives.
[1603] Ancarani and others (n 128) 1107.
[1604] See Chapter 6, Section 6.3.2.2.

resource in many public procurement markets, and targeted legal interventions can support their participation directly, broadening the pool of bidders. When comparing bid preferences and reserved contracts, both approaches have the potential to effectively enhance SME participation in the short term, yet where open competition constitutes a fundamental principle, bid preferences may prove superior by maintaining competitive pressure from large businesses.

While facilitative measures, such as division into lots and managing the qualification process, are generally regarded as less controversial and aligned with principles of equal treatment and proportionality, they often impose greater administrative burdens on contracting authorities and thus face implementation resistance. In contrast, preferential measures, particularly reserved contracts, are more easily adopted in practice due to their administrative simplicity. The effectiveness of each measure depends not only on its legal design but also on its practical compatibility with the incentives and constraints faced by contracting authorities, as discussed in Section 8.4.3.[1605]

If legislators or policymakers seek to design SME-friendly measures that improve their participation without deterring large businesses, they are effectively aiming for a Pareto improvement, which is exceedingly rare.[1606] Economic theory, and particularly welfare analysis, recognises that when a Pareto improvement is unattainable, a Kaldor-Hicks improvement may still be desirable, where the overall gains outweigh the losses.[1607] In this context, if the broader social and economic benefits of increased

[1605] See Section 8.4.3.

[1606] Richard A Posner, Economic Analysis of Law (9th edn, Wolters Kluwer 2014).

[1607] Nicholas Kaldor, 'Welfare Propositions of Economics and Interpersonal Comparisons of Utility' (1939) 49 Economic Journal 549; also see John R Hicks, 'The Foundations of Welfare Economics' (1939) 49 Economic Journal 696.

SME participation outweigh the marginal disadvantages to large businesses, then a well-calibrated preferential measure may be justified. Even if it does not leave all parties better off, there is a net benefit to the overall welfare in society.

8.3 Preliminary Observations on Jurisdictional Approaches to SME-friendly Measures

The preceding analysis has examined four distinct SME-friendly measures across four jurisdictions, with each measure analysed primarily in the jurisdiction(s) where it has been most extensively developed. This approach was deliberate: examining measures where they are most mature provides the richest insights into their design possibilities, implementation challenges, and effectiveness. The analysis also reveals patterns in how different jurisdictions approach SME support in public procurement. Whilst this thesis does not undertake systematic comparative analysis, the multi-jurisdictional illustrative approach enables preliminary observations regarding why certain measures are prominent in particular jurisdictions and what factors appear to influence their selection and calibration. This section identifies such patterns, considering how legal constraints and policy priorities shape jurisdictional approaches to SME-friendly measures.

8.3.1 The EU

Supporting SMEs is at the top of the EU's political agenda, and this commitment extends to public procurement.[1608] Directive 2014/24/EU introduced a series of facilitative measures aimed at improving SME access, including the division into lots, limiting the turnover requirements, the ESPD, and direct payments to subcontractors.[1609] In contrast to the US, the EU does not adopt an explicit preferential treatment for SMEs. It is argued that the EU's approach ensures that SMEs compete with large businesses on a level playing field.[1610] However, the level playing field argument is worth considering. Competing on a level playing field means both SMEs and large businesses have an equal chance to compete for a procurement contract, with neither of them having any inherent advantage over the other, but only on the merit of their tenders. Under facilitative measures, SMEs may still not be able to compete with large businesses on a level playing field. For example, if a contract is divided into lots but lot bundling is allowed, SMEs are not competing with large businesses on an equal footing, as large businesses have the advantage of bundling all lots back together into a large contract so that they can generate economies of scale and offer a more competitive price.

The reasons behind the EU's objection to preferential measures for SMEs are two-fold: legal concerns and economic concerns. In 1990, when the European Commission investigated the measures to promote SME participation in public procurement across jurisdictions, it was argued that preferences are 'administratively costly and protecting

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[1608] TFEU, art 173(1); Directive 2014/24/EU, recital 2.

[1609] Directive 2014/24/EU. For a comprehensive discussion on SME-friendly measures in Directive 2014/24/EU, see Trybus and Andrecka (n 55).

[1610] Pierre-Henri Morand, 'SMEs and Public Procurement Policy' (2003) 8 Review of Economic Design 301, 303.

economic inefficiency, distorting competition and discouraging modernisation and improvements in productivity'.[1611] More importantly, there are significant legal concerns that preferences for SMEs might not be consistent with EU law.

First and foremost, preferential measures for SMEs shall comply with the principle of non-discrimination, which is a fundamental principle in the EU.[1612] Member States are prohibited from adopting a measure to favour their domestic suppliers in public procurement procedures, as it constitutes a measure having equivalent effect to a quantitative restriction, which is prohibited under Article 34 TFEU.[1613] In Case C-21/88, *Du Pont*, an Italian law required that contracting authorities shall procure at least 30 per cent of their supplies from industrial and agricultural undertakings and small businesses established in Southern Italy.[1614] The CJEU decided that it constituted a violation of Article 34 TFEU, only domestic suppliers benefited from this rule, even though not all domestic suppliers did.[1615] In this case, one might argue that a preferential measure for all SMEs across the EU may be compliant with the principle of non-discrimination.[1616] This could take the form of reserving a certain share of contracts or providing a preference for suppliers satisfying a universal size standard.

Some argue that Article 67 Directive 2014/24/EU can accommodate adding the size of bidders into the Most Economically Advantageous Tender (MEAT) criterion, as SMEs could be regarded as a vulnerable group and company size could thus be a social award criterion.[1617] However, this argument overlooks the requirement of a link

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[1611] COM (90) 166 final, 4, para 13.
[1612] TFEU, art 18(1).
[1613] TFEU, art 34.
[1614] See Case C-21/88 *Du Pont*, para 3.
[1615] ibid para 13-18.
[1616] Balsh⊘j (n 127) 965.
[1617] ibid.

to the subject matter of the contract (LtSM) for the award criteria stipulated in Article 67 (3) Directive 2014/24/EU.[1618] The LtSM requires that the award criteria shall relate to the works, supplies, or services to be provided under that contract, including factors in the specific process of production, provision or trading, or a specific process for another stage of their life cycle.[1619] It is challenging to link the size of bidders with the process of production, as the size of bidders does not relate to the quality of the products, or to 'organisation, qualification and experience of staff assigned', or to after-sales service either.[1620] Nevertheless, some SMEs may indirectly benefit from award criteria with social considerations incorporated, for example, employing long-term unemployed or disadvantaged individuals.[1621]

Moreover, the adoption of preferential measures for SMEs throughout the EU may appear non-discriminatory in legal terms, as it does not explicitly distinguish between enterprises based on nationality. However, in practice, such measures may generate cross-border inequalities due to the differing levels of economic development, industrial capacity, and market structure among Member States. Even when such preferences are applied uniformly to all SMEs in accordance with the definition set out in Recommendation 2003/361/EC, structural disparities remain. Enterprises established in larger Member States often operate on a greater scale than those in smaller Member States, despite all qualifying as SMEs under the same criteria. As a result, the competitive landscape is skewed when public contracts or specific lots are reserved exclusively for SMEs.

[1618] Directive 2014/24/EU, art 67(3).

[1619] ibid.

[1620] Directive 2014/24/EU, art 67(2); also see Burgi (n 48) 288.

[1621] Directive 2014/24/EU, art 20; also see Schoenmaekers (n 11) 176.

For instance, as discussed in Chapter 2, the average number of employees per SME in Germany is 7.1, which is the highest among all EU Member States, while the EU-wide average is 3.6, illustrating the structural disparities that exist within the supposedly uniform SME definition.[1622] The higher level of capacity enables German SMEs to participate more effectively in procurement processes and to derive greater benefit from potential preferential measures. In contrast, SMEs from smaller Member States may be less equipped in terms of human and financial resources, and consequently less able to compete for such opportunities, particularly in cross-border contexts. To illustrate, consider a contract reserved for SMEs by a German contracting authority. While a German SME may be well-positioned to take advantage of this opportunity, a large Lithuanian enterprise would be excluded solely based on its size. In principle, a Lithuanian SME could also compete for the contract on equal terms. However, in practice, SMEs from smaller Member States may face significant structural disadvantages when attempting to participate in procurement procedures across borders.[1623] These disadvantages may include higher costs of cross-border operations, limited access to information, and unfamiliarity with administrative procedures in other Member States.[1624] As a result, the formal availability of the opportunity does not guarantee effective access, particularly for SMEs with more limited resources or international experience.

Therefore, while adopting preferential measures for EU-wide SMEs does not constitute a violation of the principle of non-discrimination *de jure*, its practical

[1622] IfM Bonn 'SMEs in the EU: Comparison' (n 219). For a discussion on this, see Chapter 2, Section 2.2.
[1623] See European Commission, *Study on the Measurement of Cross-Border Penetration in the EU Public Procurement Market: Final Report* (n 760).
[1624] ibid.

implications may lead to indirect discrimination. In effect, such measures tend to favour local or better-resourced SMEs, particularly those from larger Member States, regardless of whether that outcome is intentional.

8.3.2 The US

Although the US adopts an explicitly preferential approach for small businesses, there are multiple public policies embedded in federal procurement and federal agencies are left with unclear guidance regarding the priorities of these policies.[1625] For example, to increase efficiency and reduce costs, federal agencies use Multiple Award Contracts, such as the GSA schedule contracts administered by the General Services Administration; however, the Rule of Two does not automatically require small businesses set-asides for orders placed under these contracts.[1626]

Apart from preferential measures, facilitating measures also exist in US federal procurement; for example, FAR 19.202-1(a) requires that contracting officers shall divide contracts into reasonably small lots when applicable.[1627] As discussed in Chapter 2, contracting officers are required to allocate only one North American Industry Classification System (NAICS) code for each procurement contract, and these codes correspond to detailed sectors.[1628] For example, under the construction category, flooring, framing, and roofing correspond to different NAICS codes.[1629] This may explain why contract division into lots is not the primary approach for supporting

[1625] See Chapter 7, Section 7.4.
[1626] See Chapter 7, Section 7.3.2.
[1627] 48 CFR § 19.202-1(a).
[1628] See Chapter 2, Section 2.3.
[1629] 13 CFR § 121.201, 'Small Business Size Standards by NAICS Industry', 'Sector 23-Construction'.

small businesses in US federal procurement, as the contracts are already segmented by sector (subject matter).[1630]

Comparing the length of the rules themselves, the dividing contracts rule (FAR 19.202-1) is less prescriptive than the reserved contracts rules in FAR 19.5.[1631] Based on the obligation on contracting officers, they have much more discretion in considering a contract division, and less discretion when deciding if a contract shall be reserved for small businesses. Where a contracting officer determines that a contract is not appropriate for division into smaller lots, the FAR merely requires an explanation, without limiting the types of justifications that may be relied upon; by contrast, a decision not to reserve a contract for small businesses is subject to more constraints.[1632] The differing degree of prescription is not incidental but reflects the distinct regulatory purposes of the two regimes. FAR 19.202-1 is framed as a facilitative policy aimed at 'encouraging small business participation in acquisitions', whereas FAR 19.5 seeks to 'assure that a fair proportion of Government contracts in each industry is placed with small business concerns'.[1633] The latter therefore embodies a more directive and redistributive objective, which justifies tighter constraints on administrative discretion. In practice, this reveals that the US system relies primarily on the set-aside regime as its principal instrument for advancing small business participation, while contract division operates as a softer, more discretionary complement.

[1630] See Chapter 2, Section 2.4.
[1631] See 48 CFR § 19.202-1(a); 48 CFR § 19.502.
[1632] 48 CFR § 19.502-5.
[1633] See 48 CFR § 19.202-1, 19.502-1(a)(2).

The underlying rationales for promoting SME participation in public procurement diverge between the US and the EU. In the US, the justification is framed primarily from the perspective of small businesses themselves. The legal and policy frameworks are designed to support the development of small businesses, particularly those with recognised socioeconomic disadvantages, such as businesses owned by minorities. By contrast, the EU adopts a more neutral approach to support SMEs, without undermining the core objective to facilitate the Internal Market. The support for SMEs in procurement is conceived not as an end, but as a means of fostering a more open and integrated procurement market across Member States. While the EU recognises the economic and social importance of SMEs, its institutional emphasis lies in their contribution to the Internal Market. Individual Member States may share policy motivations akin to those in the US, but their discretion is constrained by overarching EU legal principles, most prominently the principle of non-discrimination.

Lastly, preferential measures for domestic small businesses, such as reserved contracts and bid preferences, conflict with the principle of non-discrimination enshrined in the World Trade Organisation (WTO) Agreement on Government Procurement (GPA).[1634] As a founding Party to the GPA, the US was able to secure an exclusion for such preferential measures in its schedule of commitments.[1635] This exemption applies to both ordinary and socioeconomic small businesses programmes, including reserved contracts and bid preferences.[1636] However, for other jurisdictions, particularly those that are already GPA Parties or are considering accession, caution must be taken when adopting preferential measures for SMEs. Meanwhile, when such

[1634] GPA, art IV.

[1635] See WTO GPA: United States General Notes, Annex 7 to Appendix I (accessed via e-GPA, 2024) https://e-gpa.wto.org/en/GPACoverage/Annex7/106 accessed 30 July 2025.

[1636] ibid.

measures are already embedded in domestic procurement frameworks, GPA accession becomes more complex. This is because a preference for domestic suppliers is inherently incompatible with the GPA's core principle, the principle of non-discrimination, which obliges Parties to treat the suppliers of other Parties no less favourably than their own.[1637] The tension between these domestic policies and GPA obligations is evident in Brazil's recent accession experience, which is discussed in the next section.

8.3.3 Brazil

Like the US, Brazil presents a model that strongly integrates support for MSEs into the broader framework of national economic development. Article 179 of the Brazilian Constitution, along with Complementary Law No. 123/2006 (LC 123/2006), mandates preferential treatment for MSEs, particularly in the context of public procurement.[1638] Article 47 LC 123/2006 explicitly requires contracting authorities to adopt simplified procedures and preferential treatment aimed at promoting economic and social development at the municipal and regional levels.[1639] While these objectives are not specific to MSEs, those preferential measures are often the tools through which these objectives are pursued. Unlike the EU's neutral approach or the US's dual emphasis on economic and social equity, Brazil's approach is predominantly economic in orientation.

[1637] GPA, art IV.

[1638] Brazilian Constitution, art 170, LC 123/2006. The scope of small enterprises is limited to Brazilian small enterprises. See Chapter 2, Section 2.4.

[1639] LC 123/2006, art 47.

As discussed in Chapter 2, medium-sized enterprises are not given a legal status in Brazil.[1640] However, the size threshold of MSEs under LC 123/2006 is substantially lower than the size standard of small businesses in the US.[1641] This means that the beneficiaries of preferential measures are a much smaller group of enterprises in Brazil, compared with the US.[1642] In 2014, LC 147/2014 introduced an automatic reserved contract rule for MSEs when contracts are valued at up to BRL 80,000, which is a relatively low threshold compared with the reserved contracts threshold in the US at USD 250,000.[1643] Not surprisingly, the addition of the reserved contracts rule did not create positive results based on current evidence, as the proportion of MSEs in public procurement decreased from 25 per cent in 2013 to 15 per cent in 2017.[1644]

In addition, Brazil explicitly allows contracting authorities to reserve up to 25 per cent of the lots within a divisible contract for MSEs.[1645] In practice, this means that in contracts involving divisible items, authorities may dedicate a portion, capped at 25 per cent, specifically for MSEs. However, this is a discretionary mechanism, available when contracts are tendered in lots, which itself is also optional under Brazilian procurement law.[1646] As discussed in Section 8.3.3, contracting authorities lack incentives to undertake division into lots when it is a discretionary measure, which adds more uncertainty in reserving lots for MSEs.[1647] Since both division and

[1640] See Chapter 2, Section 2.4.
[1641] For a comparison of SME size criteria, see Chapter 2, Section 2.6.
[1642] ibid.
[1643] LC 123/2006, art 48(I), amended by LC 147/2014.
[1644] There are other macroeconomic factors which potentially resulted in this decrease. See Chapter 6, Section 6.2.3.
[1645] LC 123/2006, art 48(III).
[1646] Law 14.133/2021, art 40 V(b).
[1647] See Section 8.3.3.

reservation of lots are discretionary in Brazil, it remains to be seen whether this rule is widely implemented, highlighting a potential gap between the legal rules and practice.

In contrast, the bid preferences for MSEs introduced in LC 123/2006 has proved arguably more successful in supporting MSEs, including a fictitious-tie preference and a traditional bid preference.[1648] The fictitious-tie preference only allows MSEs to secure contracts when they agree to match or undercut the lowest bid, and the traditional bid preference allows MSEs to secure a contract even if they do not match the lowest bid. *Prima facie*, fictitious-tie bid preferences provide MSEs with a second chance to secure a contract while preserving cost efficiency for contracting authorities. The empirical evidence shows limited effectiveness of this type of bid preference, potentially due to MSEs' limited capacity to match the lowest bid.[1649]

From an international trade perspective, Brazil presents a compelling example of the tension between GPA obligations and preferential measures for MSEs. Unlike the US, Brazil only became an observer to the GPA in 2017 and formally applied for accession in 2020, before withdrawing its offer in 2023.[1650] Since Brazil has incorporated preferential measures for domestic MSEs, its accession to the GPA has been a concern since the beginning, as such measures are difficult to reconcile with the GPA's fundamental commitment to market liberalisation and non-discrimination.[1651] Under the GPA, the principal derogation to this obligation is found in Articles III and V(3). Article III permits exclusion for defence procurement and certain public policy

[1648] See Chapter 6, Section 6.1.
[1649] See Chapter 6, Section 6.2.3.
[1650] Cesar Pereira and Rafael Wallbach Schwind, 'The GPA/WTO and Latin America: lessons from Brazil's accession process' (2023) 5 Public Procurement Law Review 249.
[1651] ibid.

objectives, such as supporting the goods or services of persons with disabilities.[1652] Brazil's MSE preferences do not fall within these categories under Article III. Article V(3), on the other hand, allows developing countries to adopt transitional measures, such as bid preferences for domestic goods or services, during a transitional period.[1653] However, these measures are time-limited, as the term 'transitional' implies. Therefore, to maintain its existing preferential measures for MSEs on a long-term basis, Brazil would have needed to propose an exclusion of those measures from GPA coverage, similar to the approach taken by the US. The success of such a proposal depends significantly on the acceding country's market power and the willingness of existing GPA Parties to accept the terms.[1654]

Although Brazil's accession offer is not publicly available, the Brazilian government has explained that GPA membership would place significant limitations on its ability to use procurement as a tool for economic and social development, especially in areas such as public health, technology, and innovation.[1655] It is therefore plausible that Brazil attempted to reserve the right to maintain its MSE preferences, as reflected in the recently revised texts of the EU-Mercosur Partnership Agreement and the signed Mercosur-Singapore Free Trade Agreement. Both agreements contain provisions allowing Brazil to apply bid preferences and set-asides for MSEs.[1656] Brazil's

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[1652] GPA, art III; Directive 2014/24/EU, art 20. The reserved contracts regime under Article 20 Directive 2014/24/EU can fall under Article III GPA, as reserved contracts in the EU are limited to sheltered workshops and economic operators whose main aim is the social and professional integration of disabled or disadvantaged persons.

[1653] GPA, art V(3).

[1654] Linarelli (n 1311) 462.

[1655] Ministry of Foreign Affairs of Brazil, 'Brazil Withdraws Offer to Accede to the WTO Government Procurement Agreement' (Press release, 30 May 2023) <https://www.gov.br/mre/en/contact-us/press-area/press-releases/brazil-withdraws-offer-to-accede-to-the-wto-government-procurement-agreement> accessed 30 July 2025.

[1656] See Draft EU–Mercosur Partnership Agreement, Annex X-C (Brazil's Coverage on Government Procurement) <https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-

experience highlights the legal and practical difficulties that countries with entrenched domestic preference regimes face when negotiating trade agreements or acceding to the GPA. In contrast, existing GPA Parties that adopt facilitating measures for SMEs face fewer legal constraints, such as the division into lots or managing the qualification process. These facilitating measures are also recommended by the GPA Committee as a means of supporting SME participation without violating GPA principles.[1657]

8.3.4 South Africa

South Africa represents a paradigmatic example of a procurement regime explicitly designed to serve transformative constitutional objectives. [1658] The term 'transformation' is defined as using public procurement to redress the unfair discrimination of the past and achieve socioeconomic objectives.[1659] The Constitution and subsequent legislation allow contracting authorities to provide preferences for businesses owned by historically disadvantaged individuals, including those disadvantaged by race, gender, or disability, and a large number of those businesses are MSMEs.[1660]

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and-regions/mercosur/eu-mercosur-agreement/text-agreement_en> accessed 30 June 2025; MERCOSUR – Singapore Free Trade Agreement (MCSFTA) Legal Text, Annex 13-A (Schedule of Commitment on Government Procurement Brazil) <https://www.enterprisesg.gov.sg/-/media/esg/files/non-financial-assistance/for-companies/free-trade-agreements/mcsfta/mcsfta-legal-text.pdf> accessed 30 June 2025.

[1657] See WTO, *Report of the Committee on Government Procurement on Best Practices for Promoting and Facilitating the Participation of SMEs in Government Procurement* (n 831).

[1658] Constitution of the Republic of South Africa, 1996, s 217(1).

[1659] See PPA 2024, ch 1.

[1660] See Chapter 6, Section 6.4.

Under the Preferential Procurement Policy Framework Act (PPPFA) 2000, South Africa operates a distinct bid preference system integrated into its broad-based black economic empowerment (BBBEE) policies.[1661] While South Africa's system does not single out SMEs by size alone, it indirectly supports them through awarding points to them when they satisfy the definition of Exempted Micro Enterprises (EMEs) or Qualified Small Enterprises (QSEs), and they will receive higher points if they are owned by historically disadvantaged individuals.[1662] However, the new Public Procurement Act 2024 has replaced the point-based bid preference system with a combination of reserved contracts, prequalification criteria, and subcontracting preferences.[1663] More importantly, the new act explicitly recognises MSMEs as potential beneficiaries of preferences such as reserved contracts and does not use the more limited and intricate categories of EMEs and QSEs.[1664] Although not in force yet, the new act has the potential to simplify the preferential procurement system, and MSMEs may be motivated to participate in procurement under the new regime.

South Africa's approach shares some similarities with the US, particularly in recognising the role of procurement in redressing injustices and promoting equality. However, South Africa's model is more narrowly focused on transformative justice, reflecting its unique constitutional and historical context. South Africa's framework is less concerned with MSMEs per se and more with leveraging public procurement to restructure economic participation by different groups of individuals. This distinction highlights the need for a nuanced legal design of preferential measures, especially the

[1661] See Chapter 2, Section 2.5; Chapter 6, Section 6.4.
[1662] See Chapter 2, Section 2.5.
[1663] See PPA 2024, ch 4.
[1664] See Chapter 2, Section 2.5; also see Chapter 6, Section 6.4.

eligibility criteria, implementation, and potentially a graduation scheme, that must not only reflect economic considerations but also entrenched structural inequalities.

8.4 A Comparison of SME-friendly Measures: contract value, eligibility, and incentives

To further investigate the effectiveness of these four measures and determine which measure works more effectively under which conditions, this section distils the findings from previous chapters based on three aspects: the suitability of contracts based on their size; the eligibility of SMEs; and the incentive level of contracting authorities. The first aspect reflects on which measure is more effective in relatively larger contracts, and which is more effective in relatively smaller contracts. The second aspect links the definition of SMEs with specific measures, especially SMEs' eligibility to benefit from preferential measures, inquiring whether all SMEs should be eligible for those preferences and for how long they should benefit from preferences. Lastly, the effectiveness of SME-friendly measures depends on whether contracting authorities are implementing these measures as intended by legislators or regulators. If contracting authorities lack incentives to implement a measure, this policy-practice divide may lower the effectiveness of a measure, unless it leaves contracting authorities limited discretion. These three aspects shall be considered by legislators and contracting authorities when selecting and calibrating SME-friendly measures.

8.4.1 Balancing contract value and SME-friendly measures

Among the four SME-friendly measures selected and discussed, there is a common type of criterion when applying these measures, which is the size of contracts. In the EU, the division into lots regime applies to contracts with an estimated value above the EU thresholds under Article 46 Directive 2014/24/EU, unless a Member State adopts a mandatory division into lots regime for contracts below the EU threshold. This size criterion for division into lots is reasonable, as SMEs are capable of bidding for smaller contracts. If a small contract is divided into lots, some SMEs, especially medium-sized enterprises, might find them unprofitable and refrain from bidding for these lots.[1665] Thus, if a country decides to introduce the division into lots regime to public procurement law, the threshold should be calibrated carefully regarding which subgroup of SMEs is being prioritised and promoted, or this can be left to contracting authorities to decide. In the EU, contracts valued at more than EUR 300,000 are considered large for micro-sized enterprises, EUR 1 million for small enterprises, and EUR 5 million for medium-sized enterprises.[1666] In general, the division into lots should be applied to relatively large contracts to increase SME participation.

In managing the qualification process to facilitate SME access, contracting authorities should also take account of contract value. Lower-value contracts should not be subject to onerous qualification criteria; in fact, easing such requirements may encourage wider SME participation. The primary function of qualification criteria is to exclude bidders lacking adequate capacity. If such a bidder secures a contract and subsequently fails to deliver, the authority incurs additional costs. This risk, however,

[1665] See Chapter 4, Section 4.3.1.
[1666] See Chapter 3, Section 3.2.

must be weighed against the exclusionary impact that excessive qualification criteria may have on SMEs. For lower-value contracts, the potential losses to the authority are correspondingly smaller, which justifies a proportionate relaxation of requirements. Simplifying the qualification process in these cases can also reduce the administrative burden on SMEs and further support their participation.[1667]

In Brazil, fictitious-tie bid preferences are used for contracts with a value lower than the maximum annual gross revenue limit for small enterprises as defined in LC 123/2006, which is BRL 4.8 million.[1668] Under the US HUBZone small business price preference, there is no limitation on the value of contracts. However, in the case study of bid preferences for small businesses in California, the value of the preference itself is capped at USD 50,000, meaning that for a contract with a value exceeding USD 1 million, the preference will be USD 50,000 at most, rather than the stipulated 5 per cent of the contract value.[1669] This consideration is to control the potential increase in costs of contracting authorities, which shows a balance of interests between contracting authorities and small businesses. Similarly, in South Africa, the use of the 80/20 point system is limited to contracts up to R50 million and adopts the 90/10 system for larger contracts. 80/20 and 90/10 refer to how much weight is granted to those socioeconomic factors ('specific goals', usually BBBEE, SME status, etc) compared with price as the award criterion.[1670] The ZAR 50 million threshold reflects a priority that the higher the contract value, the more weight will be given to price and performance reliability.[1671] In summary, to mitigate the potential negative effects of bid

[1667] See Chapter 5, Section 5.4.
[1668] See Chapter 6.
[1669] CGC §14838(b)(1)-(4).
[1670] See Chapter 6, Section 6.4.1.
[1671] ibid.

preferences on contracting authorities, legislators may adopt mechanisms such as the Brazilian fictitious-tie model, where the favoured bidder must match the lowest offer, or implement thresholds for the application of preferences and caps on the maximum permissible value of such advantages.

Reserved contracts are more frequently used when the contract value is relatively lower. Under the US FAR, contracts with a value between the micro-purchase threshold (USD 10,000) and simplified acquisition threshold (USD 250,000) are reserved for small businesses.[1672] For contracts valued above the simplified acquisition threshold, a reservation applies where there is a reasonable expectation of offers from at least two businesses at fair market prices (the Rule of Two).[1673] In Brazil, LC 123/2006 (amended by LC 147/2014) mandates exclusive tendering for MSEs for contracts up to BRL 80,000.[1674] The fact that reserved contracts are more frequently used in lower-value contracts across countries reflects an intentional choice to balance SME access with administrative efficiency, competition, and performance risk.

To summarise, bid preferences and reserved contracts are usually confined to lower-value contracts. By contrast, dividing contracts into lots is apt for higher-value contracts that would otherwise exceed SMEs' capacity. Managing the qualification process can apply to all contracts. However, in lower-value contracts, qualification criteria may be calibrated more SME-friendly so as to reduce entry barriers for SMEs.

[1672] 48 CFR § 19.502.
[1673] ibid; also see Chapter 7.
[1674] LC 123/2006, art 48; also see Section 8.4.3.

8.4.2 Rethinking SMEs' eligibility for preferential measures

Facilitative measures, unlike preferential measures, do not explicitly grant advantages to SMEs. Thus, the precise definition or eligibility criteria for SMEs have less practical significance. By contrast, preferential measures directly confer tangible benefits, raising important considerations regarding eligibility criteria.

In Chapters 6 and 7, both reserved contracts and bid preferences have exhibited a common issue: only a limited number of SMEs (as compared to the total number of SMEs) win contracts when these measures are applied. For example, in Chapter 6 on bid preferences, Section 6.3.1.2, the SBA OIG has found that 12 contractors have secured approximately 94 per cent of the value of all federal procurement contracts awarded to HUBZone-certified small businesses.[1675] Consequently, there may be merit in introducing experience or time-based limitations in the eligibility criteria, ensuring SMEs graduate from preferential measures after a specified period of successful participation, thus preventing the continuous dominance of experienced SMEs and promoting broader access for new entrants. Brazil provides an instructive example, explicitly prohibiting the use of bid preferences once an MSE has executed a contract exceeding its designated revenue threshold.[1676] The underlying rationale is clear: once an MSE proves capable of winning substantial contracts independently, continued preferential treatment is no longer justified.

The notion of temporal eligibility limitations also merits consideration in socioeconomic programmes. SMEs benefit from socioeconomic classifications (for example, HUBZone small businesses) often retain their social attributes indefinitely, unlike their

[1675] See Chapter 6, Section 6.3.1.2.
[1676] See Chapter 6, Section 6.2.

economic size or competitive standing, which typically evolve. Under the US FAR, the 8(a) Business Development programme uniquely imposes a nine-year graduation limit, allowing small businesses to benefit from 8(a) set-asides and related advantages only within nine years.[1677] Moreover, individuals may participate in the 8(a) programme only once in their lifetime.[1678] While recognising the permanence of social attributes and the enduring nature of structural inequalities these programmes address, introducing clear time-based or experience-based eligibility criteria can be beneficial. Without such limits, preferential programmes risk entrenching dominant positions for a select group of experienced businesses, diminishing opportunities for new entrants within the same socioeconomic groups. Incorporating explicit graduation mechanisms helps to ensure that preferential measures remain dynamic and continue to facilitate broad and inclusive market participation, aligning more closely with their foundational policy objectives.

8.4.3 Incentivising contracting authorities to implement SME-friendly measures

Across four SME-friendly measures, there exists a recurrent misalignment of incentives in implementation. Although these measures are intended to advance SME or broader socioeconomic objectives, contracting authorities often bear the administrative costs without receiving direct or proportionate benefits. From a principal-agent perspective, contracting officers, functioning as agents to the

[1677] See Chapter 2. To qualify for the 8(a) programme, a small business has to be at least 51 per cent owned and controlled by US citizens who are socially and economically disadvantaged. Once the 9 years are up, the business must graduate, though it can continue doing business with the government through other means, for example, as an ordinary small business or through being other socioeconomic small businesses.

[1678] 13 CFR 124.108(a).

government or society, do not inherently internalise the broader policy objectives of the principal (i.e., the government or society).[1679] While an increase in SME participation may, in principle, reduce procurement costs through enhanced competition, the immediate consequence for contracting authorities is often increased workload and process complexity, for example, evaluating a larger volume of tenders and administering or co-ordinating multiple lots rather than a single contract.

To bridge the gap, legislators and policymakers shall calibrate measures to minimise enforcement costs for contracting authorities. Such an approach aligns with the economic principle of rational choice theory, which posits that individuals (or institutions) naturally perform cost-benefit analyses and favour actions that incur the least effort or cost relative to their anticipated benefit.[1680] Amongst these four measures, reserved contracts do not tend to incur additional burden for contracting authorities, as empirical evidence suggests that contracting officers even prefer reserved contracts to open competition due to the administrative convenience.[1681] Bid preferences also do not increase complexity to the procurement process, if the size of the preference and the conditions to apply it are prescribed. Division into lots, in contrast, significantly increases evaluation complexity and contract management burdens, and limiting disproportionate qualification criteria can run counter to contracting authorities' intrinsic risk-averse attitudes, which often favour stringent financial and technical thresholds to ensure reliable performance.

[1679] Yukins, 'A Versatile Prism: Assessing Procurement Law Through the Principal-Agent Model' (n 548) 67.
[1680] Becker (n 547).
[1681] See Chapter 7, Section 7.4.3.

Moreover, even well-designed SME-friendly measures may fail to achieve intended objectives if contracting authorities lack the necessary administrative capacity to implement them. [1682] Crucially, measures that grant discretion to contracting authorities require more incentives for them. Conversely, legally mandated measures, such as obligatory reserved contracts under certain conditions, constrain authorities' discretion and thus ensure high compliance rates and a greater likelihood of achieving the intended objectives.

Finally, when more than one SME-friendly measure is adopted in public procurement law, contracting authorities should retain some discretion in selecting the most appropriate measure based on specific contexts. For instance, in long-term contracts spanning several years, dividing the contract into lots covering shorter periods may offer more tangible benefits for SMEs than debating whether financial criteria should be proportionate to the contract's total value or its annual value.[1683] Such flexibility acknowledges the crucial influence of contracting authorities on the practical and effective implementation of SME-friendly measures.

8.4.4 Summary

As shown in Table 8.1, the four SME-friendly measures differ in suitability by contract value and characteristics, SME eligibility, and the incentive structure facing contracting authorities. For such measures to enhance SME participation effectively, these three dimensions should be taken into account at the design and implementation stages.

[1682] DCED (n 42) 21.
[1683] See Chapter 5, Section 5.2.1.1.

Factors	Dividing contracts into lots	Managing the qualification process	Providing bid preferences	Reserving contracts
Suitability of contracts based on value	Usually apply to large contracts	Broadly applicable	Lower-value contracts or higher-value contracts with certain limitations	Lower-value contracts or higher-value contracts with certain limitations
Eligibility of SMEs	No eligibility required	No eligibility required	Often restricted to businesses meeting certain eligibility criteria	Often restricted to businesses meeting certain eligibility criteria
Incentive level of contracting authorities	Low	Low	Moderate	High

Table 8.1 A comparison of SME-friendly measures across three dimensions

8.5 Key Considerations in Selecting, Combining, and Calibrating SME-friendly Measures

Based on the preliminary observations on jurisdictional approaches in Section 8.3, and the comparison of the four measures across three dimensions in Section 8.4, this section presents key considerations for legislators and policymakers organised around three aspects: selection, combination, and calibration.

Selection involves determining which measures are appropriate for specific contexts. This begins with assessing whether intervention is necessary. In jurisdictions where SMEs participate extensively in public procurement, further measures may be

unwarranted unless targeted support for particular subcategories of SMEs is intended. Where intervention is pursued, policymakers must identify the nature of challenges SMEs face: entry barriers (low participation rate) suggest facilitative measures, whilst challenges to contract awards (low success rate despite participation) may warrant preferential approaches, Selection must also account for legal constraints, particularly constitutional principles and obligations under international trade agreements.

Combination addresses whether measures should operate independently or be complemented with other measures. As Section 8.2 has demonstrated, the four measures target different stages of the procurement process and address distinct barriers: division into lots reduced contract size at the planning stage; managing the qualification process addresses eligibility requirements before tender submission; bid preferences operate at tender evaluation stage; and reserved contracts restrict competition to SMEs only. However, combination must be structured carefully to ensure measures reinforce rather than undermine each other. For instance, dividing contracts into lots loses effectiveness if qualification criteria remain calibrated to the undivided contract value.

Calibration encompasses the tailoring of measures through thresholds, eligibility criteria, duration limits, and implementation mechanisms. Calibration decisions determine the intensity of support, the breadth of beneficiaries, and the balance between SME interests and other procurement objectives. Effective calibration also requires establishing monitoring systems to assess outcomes and enabling periodic adjustments as market conditions or SME capabilities evolve. The following considerations are organised thematically rather than sequentially, recognising that policy design involves iterative decision-making across all three dimensions.

1. Define the intended beneficiaries precisely.

As Chapter 2 demonstrated, SME definitions vary significantly across jurisdictions, reflecting different economic structures and policy objectives. For facilitative measures, broader definitions may be appropriate as these measures remove barriers without conferring competitive advantages. For preferential measures, however, precise definitions become critical for both legal certainty and practical implementation. Definitions should be verifiable by contracting authorities and comprehensible to potential beneficiaries.

2. Assess existing SME participation and match measures to identified barriers.

As emphasised in Chapter 3, barriers operate differently: some SMEs cannot participate, whilst others participate but rarely win contracts. Empirical data disaggregated by firm size and contract value reveals where intervention is most needed. Division into lots and management of qualification processes address entry barriers, whilst bid preferences and reserved contracts operate at the award stage to enhance SMEs' competitiveness or ensure contract awards. Selecting measures inappropriate to the identified barriers will prove ineffective, implementing bid preferences where SMEs cannot participate due to large contract sizes, for instance, addresses the wrong stage of the procurement process.

3. Consider combining measures where evidence indicates multiple barriers exist.

Where entry barriers are the primary concern, facilitative measures should be prioritised; preferential measures alone will not increase SME participation in such cases. Where entry is adequate but more contract awards to SMEs are desired, preferential measures can be adopted alone or combined with facilitative measures. Combination requires coordination: for instance, if contracts are divided into lots,

financial capacity requirements should be proportionate to lot value rather than total contract value.

4. Balance SME support with other public procurement objectives.

Legislators should clarify how SME support fits within the broader objectives of their procurement system, such as value for money, competition, efficiency, and non-discrimination. In particular, they should determine whether SME support is intended as an interim tool to enhance competition in public procurement or as a standalone policy objective. Clearly articulating these priorities helps prevent conflicts between goals and ensures coherent design and implementation of procurement measures.

5. Account for legal constraints at the supranational and international levels.

Policymakers must also recognise that SME-support measures are shaped and limited by binding legal frameworks beyond the national level. For example, obligations under the WTO Government Procurement Agreement (GPA) and free trade agreements may constrain the use of domestic preference schemes unless specific exemptions apply. Where such constraints rule out preferential measures, policymakers should instead consider facilitative approaches that support SME participation without breaching legal commitments.

6. Calibrate measures to contract value and SME capacity.

As Section 8.3.1 analysed, division into lots proves most effective for higher-value contracts that would otherwise exceed SME capacity, whilst reserved contracts and bid preferences typically apply to lower-value procurement. Calibration should also address preference intensity: Brazil's fictitious-tie mechanism limits cost impacts by requiring beneficiary SMEs to match the lowest offer, whilst California caps the

monetary value of small business preferences at USD 50,000 regardless of contract size.

7. Establish eligibility criteria that prevent incumbent entrenchment and ensure verification.

The analysis in Chapters 6 and 7 revealed that preferential measures risk concentrating benefits among experienced SME contractors. Graduation mechanisms address this through temporal limits (such as the nine-year cap in the US 8(a) programme) or threshold-based restrictions (such as Brazil's prohibition on preferences for MSEs exceeding their revenue ceiling), ensuring support rotates among eligible firms. Where preferential measures apply, verification and review mechanisms are essential to prevent fraud and enable challenges to improper eligibility claims or implementation failures.

8. Design measures to align with contracting authority incentives.

As Section 8.4.3 demonstrated, implementation effectiveness depends significantly on whether measures impose administrative burdens on contracting authorities. Reserved contracts prove relatively popular with contracting officers due to administrative simplicity, whilst division into lots faces resistance due to increased evaluation and contract management complexity. Where measures grant discretion, stronger mandates or incentives become necessary; alternatively, measures can be structured to minimise compliance costs, enhancing voluntary adoption.

9. Develop data collection systems and enable periodic adjustments.

Effective procurement systems require mechanisms to track SME participation and contract awards, enabling assessment of whether measures achieve intended objectives and ensuring contracting authority compliance. Data disaggregated by firm

size, contract value, and sector generates evidence to inform calibration adjustments over time, such as revising thresholds for reserved contracts based on evolving SME participation and competitiveness.

10. Establish a review system to oversee SME-friendly measures.

Where SME-friendly measures are adopted, an appropriate review mechanism should be incorporated to enable bidders to challenge non-compliance by contracting authorities or to contest the improper application of such measures. This promotes transparency and accountability in implementation. For example, in the US, the Small Business Administration supports oversight of small business policies by monitoring agency performance and administering compliance in certain programmes.

These considerations do not constitute prescriptive solutions applicable across all contexts. Rather, they represent principles derived from analysing how different measures operate under varying legal and institutional conditions. The effectiveness of SME-friendly measures depends fundamentally on matching design choices to specific barriers, legal constraints, institutional capacities, and policy objectives within each jurisdiction.

8.6 Concluding Remarks

This thesis has examined three interconnected dimensions of SME-friendly measures in public procurement: the barriers hindering SME participation, the effectiveness of different measures in addressing these barriers, and the extent to which such measures create tensions with other procurement objectives. The analysis examined four distinct measures (division into lots, management of qualification processes, bid preferences, and reserved contracts), drawing on examples from four jurisdictions (the

EU, the US, Brazil, and South Africa) where these measures have been most extensively developed.

The findings demonstrate that SME-friendly measures can enhance participation without necessarily undermining value for money, competition, or efficiency when carefully designed and calibrated. Facilitative measures prove effective where SMEs face entry barriers, whilst preferential measures can increase contract awards where participation exists but success rates remain low. However, not all implementation challenges can be resolved through legal design alone; effectiveness depends significantly on aligning measure design with the incentives and constraints of contracting authorities.

The comparison of the four measures reveals that selection must account for contract value, SME eligibility criteria, and contracting authorities' incentives. Division into lots suits larger contracts, whilst reserved contracts and bid preferences typically apply to lower-value procurement. Preferential measures require carefully defined eligibility criteria and graduation mechanisms to prevent incumbent entrenchment, whilst all measures benefit from designs that minimise administrative burdens on contracting authorities.

The preliminary observations on jurisdictional approaches underscore that different legal and policy contexts shape measure selection. The EU's facilitative approach reflects its fundamental principle of non-discrimination, which precludes preferential treatment for SMEs. The US preferential model reflects statutory commitments to small business support established in the 1950s and exemptions from international trade obligations secured through its accession to the WTO GPA. Brazil and South Africa demonstrate how procurement can advance national developmental goals and

address historical inequalities where legal frameworks permit preferential measures. These divergent approaches confirm that there is no universal model. Rather, the selection of appropriate measures depends on matching measures to specific barriers, legal constraints, and policy priorities within each jurisdiction.

Building on these findings, the thesis presents key considerations for policymakers organised around selection, combination, and calibration of measures. These considerations identify important factors that should be taken into account when designing SME-friendly procurement systems, such as defining beneficiaries, matching measures to barriers, accounting for legal constraints, and establishing monitoring mechanisms.

Beyond these policy implications, the findings of this thesis also suggest several directions for future research. First, combining legal analysis with econometric methods could establish stronger causal claims about measure effectiveness. Second, the interaction between international trade law (particularly WTO GPA obligations) and domestic SME-friendly measures warrants deeper examination. Third, ongoing EU procurement reform creates opportunities to re-examine the legal constraints on preferential measures for SMEs.

The underlying challenge is not recognising the value of SMEs, but calibrating appropriate measures within procurement systems characterised by competing objectives. The question is not whether to support SMEs, but how to do so effectively whilst managing trade-offs and guarding against unintended consequences. Well-calibrated measures can simultaneously broaden competition, improve market outcomes, and advance economic objectives. With SME-friendly measures, public procurement law transcends its conventional role as a compliance framework. It

becomes a strategic instrument for redistributing economic opportunities and shaping who participates in public markets and on what terms, determining not merely what government buys, but from whom.

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